STEWARDSHIP FINANCIAL CORP
Form 10-K
March 15, 2019
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-K
x ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2018
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 1-33377
Stewardship Financial Corporation
(Exact name of registrant as specified in its charter)

New Jersey	22-3351447
(State of other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
630 Godwin Avenue, Midland Park, NJ	07432
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (201) 444-7100

Securities registered pursuant to Section 12(b) of the Act: Common Stock, no par value

Securities registered under Section 12(g) of the Act: None
Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.
Yes ¨ No x
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 x

Note – Checking the box above will not relieve any registrant required to file reports pursuant to Section 13 or 15(d) of the Exchange Act from their obligations under those Sections.

Indicate by check mark whether the registrant: (1) has filed 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 x No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted 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 and post such files).
Yes x No ¨

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.
x

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company or 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	x
Non-accelerated filer	¨	Smaller reporting company	x

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act).
Yes ¨ No x
The aggregate market value of the voting and non-voting common equity held by non-affiliates of the registrant, as of June 30, 2018, was $90,707,000. As of March 13, 2019, 8,684,456 shares of the registrant's common stock, net of treasury stock, were outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

PART III INCORPORATES CERTAIN INFORMATION BY REFERENCE FROM THE REGISTRANT'S DEFINITIVE PROXY STATEMENT FOR THE REGISTRANT'S 2019 ANNUAL MEETING OF SHAREHOLDERS.

FORM 10-K
STEWARDSHIP FINANCIAL CORPORATION
For the Year Ended December 31, 2018

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Cautionary Note Regarding Forward-Looking Statements

This Annual Report on Form 10-K may contain certain “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995 with respect to the financial condition, results of operations and business of Stewardship Financial Corporation (the “Corporation”) and its wholly owned subsidiary, Atlantic Stewardship Bank (the "Bank"). In some cases, you can identify forward-looking statements by the following words: “anticipate,” “believe,” “continue,” “could,” “estimate,” “expect,” “intend,” “may,” “ongoing,” “plan,” “potential,” “predict,” “project,” “should,” “wil negative of these terms or other comparable terminology, although not all forward-looking statements contain these words. Forward-looking statements are not historical facts and are subject to risks and uncertainties. Forward-looking statements are not a guarantee of future performance or results, and will not necessarily be accurate indications of the times at, or by, which such performance or results will be achieved. Forward-looking statements are based on information available at the time the statements are made and involve known and unknown risks, uncertainties and other factors that may cause our results, levels of activity, performance or achievements to be materially different from the information expressed or implied by the forward-looking statements. These factors include:

- changing bank regulatory conditions, policies or programs, whether arising as new legislation or regulatory initiatives, that could lead to restrictions on activities of banks generally, or the Bank in particular, more restrictive regulatory capital requirements, increased costs, including deposit insurance premiums, regulation or prohibition of certain income producing activities or changes in the secondary market for loans and other products;
- monetary and fiscal policies of the Board of Governors of the Federal Reserve System and the U.S. Government and other government initiatives affecting the financial services industry;
- results of examinations of us by our regulators, including the possibility that our regulators may, among other things, require us to increase our reserve for loan losses or to write-down assets;
- failures of or interruptions in the communications and information systems on which we rely to conduct our business could reduce our revenues, increase our costs or lead to disruptions in our business;
- general economic conditions including unemployment rates, whether national or regional, and conditions in the lending markets in which we participate that may hinder our ability to increase lending activities or have an adverse effect on the demand for our loans and other products, our credit quality and related levels of nonperforming assets and loan losses, and the value and salability of the real estate that we own or that is the collateral for our loans;
- impairment charges with respect to securities;
- unanticipated costs in connection with new branch openings;
- acts of war, acts of terrorism, cyber-attacks and natural disasters;
- fluctuation in interest rates;
- risks related to the concentration in commercial real estate, commercial business loans and commercial construction loans;
- concentration of credit exposure;
- declines in commercial and residential real estate values;
- inability to manage growth in commercial loans;
- unexpected loan prepayment volume;
- unanticipated exposure to credit risks;
- insufficient allowance for loan losses;
- competition from other financial institutions;
- a decline in the levels of loan quality and origination volume; and
- a decline in deposits.

The Corporation undertakes no obligation to update or revise any forward-looking statements in the future based upon future events or circumstances, new information or otherwise.

Part I

Item 1. Business

General

Stewardship Financial Corporation (the "Corporation") is a one-bank holding company, which was incorporated under the laws of the State of New Jersey in January 1995 to serve as a holding company for Atlantic Stewardship Bank (the "Bank"). The only significant activity of the Corporation is ownership and supervision of the Bank.

The Bank is a commercial bank formed under the laws of the State of New Jersey on April 26, 1984. The Bank operates from its main office at 630 Godwin Avenue, Midland Park, New Jersey, and its current eleven additional branches located in the State of New Jersey.

The Corporation is subject to the supervision and regulation of the Board of Governors of the Federal Reserve System (the "FRB"). The Bank's deposits are insured by the Federal Deposit Insurance Corporation, an agency of the federal government (the "FDIC"), up to applicable limits. The operations of the Corporation and the Bank are subject to the supervision and regulation of the FRB, the FDIC and the New Jersey Department of Banking and Insurance (the "NJDOBI").

Stewardship Investment Corp. is a wholly-owned, non-bank subsidiary of the Bank, whose primary business is to own and manage an investment portfolio. Stewardship Realty, LLC is a wholly-owned, non-bank subsidiary of the Bank, whose primary business is to own and manage property at 612 Godwin Avenue, Midland Park, New Jersey. Atlantic Stewardship Insurance Company, LLC is a wholly-owned, non-bank subsidiary of the Bank, whose primary business is insurance. The Bank also has several other wholly-owned, non-bank subsidiaries formed to hold title to properties acquired through foreclosure or deed in lieu of foreclosure. In addition to the Bank, in 2003, the Corporation formed, Stewardship Statutory Trust I, a wholly-owned, non-bank subsidiary for the purpose of issuing trust preferred securities.

The principal executive offices of the Corporation are located at 630 Godwin Avenue, Midland Park, New Jersey 07432. Our telephone number is (201) 444-7100 and our website address is www.asbnow.bank.

The Corporation has adopted a Code of Ethical Conduct for Senior Financial Managers that applies to its principal executive officer, principal financial officer, principal accounting officer, controller and any other person performing similar functions. The Corporation's Code of Ethical Conduct for Senior Financial Managers is posted on our website, www.asbnow.bank. The Corporation intends to satisfy the disclosure requirement under Item 5.05 of Form 8-K regarding an amendment to, or waiver from, a provision of its Code of Ethical Conduct for Senior Financial Managers by filing an 8-K and by posting such information on our website.

Business of the Corporation

The Corporation's primary business is the ownership and supervision of the Bank. The Corporation, through the Bank, conducts a traditional commercial banking business, and offers deposit services including personal and business checking accounts and time deposits, money market accounts and regular savings accounts. The Corporation structures the Bank's specific products and services in a manner designed to attract the business of the small and medium-sized business and professional community as well as that of individuals residing, working and shopping in Bergen, Morris and Passaic Counties, New Jersey. The Corporation engages in a wide range of lending activities and offers commercial, consumer, residential real estate, home equity and personal loans.

In forming the Bank, the members of its Board of Directors envisioned a community-based institution which would serve the local communities surrounding its branches, while also providing a return to its shareholders. This vision has been reflected in the Bank's tithing policy, under which the Bank tithes 10% of its pre-tax profits to worthy Christian and civic organizations primarily in the communities where the Bank maintains branches.

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Service Area

The Bank's service area primarily consists of Bergen, Morris and Passaic Counties in New Jersey, although the Corporation makes loans throughout New Jersey. Throughout 2018, the Bank operated from its main office in Midland Park, New Jersey and eleven additional branch offices in Hawthorne, Ridgewood, Montville, Morristown, North Haledon, Pequannock, Waldwick, Wayne (2), Westwood and Wyckoff, New Jersey.

Competition

The market for banking services remains highly competitive. The Bank competes for deposits and loans with commercial banks, thrifts and other financial institutions, many of which have greater financial resources than the Bank. Many large financial institutions in New York City and other parts of New Jersey compete for the business of New Jersey residents and companies located in the Bank's service area. Certain of these institutions have significantly higher lending limits and expend greater resources on marketing and advertising than the Bank and provide services to their customers that the Bank does not offer.

Management believes the Bank is able to compete on a substantially equal basis with its competitors because it provides responsive, personalized services through management's knowledge and awareness of the Bank's service area, customers and business.

Employees

At December 31, 2018, the Corporation employed 119 full-time employees and 28 part-time employees. None of these employees are covered by a collective bargaining agreement and the Corporation believes that its employee relations are good.

Supervision and Regulation

General

Bank holding companies and banks are extensively regulated under both federal and state law. These laws and regulations are intended to protect depositors, not shareholders. To the extent that the following information describes statutory and regulatory provisions, it is qualified in its entirety by reference to the particular statutory and regulatory provisions and is not intended to be an exhaustive description of the statutes or regulations applicable to the Corporation's and the Bank's business. Any change in the applicable law or regulation may have a material effect on the business and prospects of the Corporation and the Bank.

Dodd-Frank Act

The scope of the laws and regulations and the intensity of supervision to which our business is subject have increased in the decade after the financial crisis, in large part, as a result of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the "Dodd-Frank Act"), and its implementing regulations, most of which are now in place. Provisions in the Dodd-Frank Act and related rules that affect deposit insurance assessments, payment of interest on demand deposits, and interchange fees have increased the costs associated with deposits as well as place limitations on certain revenues that those deposits may generate. The Corporation is subject to the requirements of the Dodd-Frank Act, which includes provisions that, among other things, have:

- centralized responsibility for consumer financial protection by creating a new agency, the Consumer Financial Protection Bureau (the "CFPB"), responsible for implementing, examining, and enforcing compliance with federal consumer financial laws;

• applied to most bank holding companies, the same leverage and risk-based capital requirements applicable to insured depository institutions. The Corporation's existing trust preferred securities continue to be treated as Tier 1 capital;

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- changed the assessment base for federal deposit insurance from the amount of insured deposits to consolidated assets less tangible equity, eliminated the ceiling on the size of the Deposit Insurance Fund (“DIF”) and increased the floor on the size of the DIF, which generally requires an increase in the level of assessments for institutions with assets in excess of $10 billion;
- implemented corporate governance revisions, including with regard to executive compensation and proxy access by shareholders, that apply to all public companies, not just financial institutions;
- made permanent the $250,000 limit for federal deposit insurance;
- repealed the federal prohibitions on the payment of interest on demand deposits, thereby permitting depository institutions to pay interest on business transactions and other accounts; and
- restricted the interchange fees payable on debit card transactions for issuers with $10 billion in assets or greater.

The Economic Growth Act, as defined and described below, could result in meaningful regulatory changes for community banks and their holding companies. However, the Corporation and the Bank remain subject to extensive regulation and supervision.

2018 Regulatory Reform

In May 2018, Congress enacted the Economic Growth, Regulatory and Consumer Protection Act (the “Economic Growth Act”) to modify or remove certain post-financial crisis financial reform rules and regulations, including some of those implemented under the Dodd-Frank Act. The Economic Growth Act maintains most of the regulatory structure established by the Dodd-Frank Act, but amends certain aspects of the regulatory framework for small depository institutions with assets of less than $10 billion and for large banks with assets of more than $50 billion.

The Economic Growth Act, among other matters, expands the definition of qualified mortgages which may be held by a financial institution and simplifies the regulatory capital rules for financial institutions and their holding companies with total consolidated assets of less than $10 billion by instructing the federal banking regulators to establish a single “community bank leverage ratio” of between 8% and 10%. Any qualifying depository institution or its holding company that exceeds the “community bank leverage ratio” will be considered to have met generally applicable leverage and risk-based regulatory capital requirements and any qualifying depository institution that exceeds the new ratio will be considered to be “well capitalized” under the prompt corrective action rules

In addition, the Economic Growth Act includes regulatory relief for community banks regarding regulatory examination cycles, call reports, the proprietary trading prohibition known as the Volcker Rule (as discussed below), mortgage disclosures and risk weights for certain high-risk commercial real estate loans. The Economic Growth Act also expands the category of holding companies that may rely on the “Small Bank Holding Company Policy Statement” by raising the maximum amount of assets a qualifying holding company may have from $1 billion to $3 billion and excluding such holding companies from the minimum capital requirements of the Dodd-Frank Act.

It is difficult at this time to predict when or how any new standards under the Economic Growth Act will ultimately be applied to us or what specific impact the Economic Growth Act and its yet-to-be-written implementing rules and regulations will have on us and other community banks.

Volcker Rule

In December 2013, federal banking and securities regulators adopted final rules to implement the Volcker Rule contained in Section 619 of the Dodd-Frank Act. The Volcker Rule prohibits an insured depository institution and its affiliates (referred to as "banking entities") from engaging in “proprietary trading” and investing in or sponsoring certain types of funds subject to certain limited exceptions. The Volcker Rule also effectively prohibits short-term trading strategies by any U.S. banking entity if those strategies involve instruments other than those specifically permitted for trading and prohibits the use of some hedging strategies. Based upon management’s review of the Bank's securities portfolio, management believes that there are no securities in our portfolio that are impacted by the Volcker Rule. Consistent with the Economic Growth Act, federal banking agencies have proposed to exclude community banks, such as us, with $10 billion or less in total consolidated assets and total trading assets and liabilities of 5% or less of total consolidated assets from the restrictions of the Volcker Rule.

Bank Holding Company Act

As a bank holding company registered under the Bank Holding Company Act of 1956, as amended (the “BHCA”), the Corporation is subject to the regulation, supervision, examination and inspection of the FRB. The Corporation is required to file with the FRB annual reports and other information demonstrating that its business operations and those of its subsidiaries are limited to banking, managing or controlling banks, furnishing services to or performing services for its subsidiaries or engaging in any other activity which the FRB determines to be so closely related to banking or managing or controlling banks as to be properly incident thereto. The FRB may also conduct examinations of the Corporation and its subsidiaries.

The BHCA requires, among other things, the prior approval of the FRB in any case where a bank holding company proposes to (i) acquire all or substantially all of the assets of any other bank, (ii) acquire direct or indirect ownership or control of more than 5% of the outstanding voting stock of any bank (unless it owns a majority of such bank’s voting shares), or (iii) merge or consolidate with any other bank holding company. The FRB will not approve any merger, acquisition, or consolidation that would have a substantially anti-competitive effect, unless the anti-competitive impact of the proposed transaction is clearly outweighed by a greater public interest in meeting the convenience and needs of the community to be served. The FRB also considers capital adequacy and other financial and managerial resources and future prospects of the companies and the banks concerned, together with the convenience and needs of the community to be served.

Additionally, the BHCA prohibits, with certain limited exceptions, a bank holding company from (i) acquiring or retaining direct or indirect ownership or control of more than 5% of the outstanding voting stock of any company which is not a bank or bank holding company, or (ii) engaging directly or indirectly in activities other than those of banking, managing or controlling banks, or performing services for its subsidiaries; unless such non-banking business is determined by the FRB to be so closely related to banking or managing or controlling banks as to be properly incident thereto. In making such determinations, the FRB is required to weigh the expected benefits to the public, such as greater convenience, increased competition or gains in efficiency, against the possible adverse effects, such as undue concentration of resources, decreased or unfair competition, conflicts of interest, or unsound banking practices.

The BHCA prohibits depository institutions whose deposits are insured by the FDIC and bank holding companies, among others, from transferring and sponsoring and investing in private equity funds and hedge funds.

There are a number of obligations and restrictions imposed on bank holding companies and their depository institution subsidiaries by law and regulatory policy that are designed to minimize potential loss to the depositors of such depository institutions and the FDIC insurance funds in the event the depository institution becomes in danger of default. Under a policy of the FRB with respect to bank holding company operations, a bank holding company is required to commit resources to support such institutions in circumstances where it might not do so absent such a policy. The FRB also has the authority under the BHCA to require a bank holding company to terminate any activity or to relinquish control of a non-bank subsidiary upon the FRB’s determination that such activity or control constitutes a serious risk to the financial soundness and stability of any bank subsidiary of the bank holding company.

Capital Adequacy Guidelines for Banks and Bank Holding Companies

The Corporation is subject to capital adequacy guidelines promulgated by the FRB. The Bank is subject to somewhat comparable but different capital adequacy requirements imposed by the FDIC. The federal banking agencies have adopted risk-based capital guidelines for banks and bank holding companies. The risk-based capital guidelines are designed to make regulatory capital requirements more sensitive to differences in risk profiles among banks and bank holding companies, to account for off-balance sheet exposure, and to minimize disincentives for holding liquid assets. Under these guidelines, assets and off-balance sheet items are assigned to broad risk categories, each with appropriate weights. The resulting capital ratios represent capital as a percentage of total risk-weighted assets and off-balance sheet items.

Federal banking regulators have also adopted leverage capital guidelines to supplement the risk-based measures. Leverage capital to average total assets is determined by dividing Tier 1 Capital as defined under the risk-based capital guidelines by average total assets (non-risk adjusted).

Guidelines for Banks

In December 2010 and January 2011, the Basel Committee on Banking Supervision (the “Basel Committee”) published the final texts of reforms on capital and liquidity, which are generally referred to as “Basel III”. The Basel Committee is a committee of central banks and bank supervisors and regulators from the major industrialized countries that develops broad policy guidelines for the regulation of banks and bank holding companies. In July 2013, the FDIC and the other federal bank regulatory agencies adopted final rules (the “Basel Rules”) to implement certain provisions of Basel III and the Dodd-Frank Act. The Basel Rules revised the leverage and risk-based capital requirements and the methods for calculating risk-weighted assets. The Basel Rules apply to all depository institutions, top-tier bank holding companies with total consolidated assets of $1 billion or more and top-tier savings and loan holding companies.

Among other things, the Basel Rules (a) established a new common equity Tier 1 Capital (“CET1”) to risk-weighted assets ratio minimum of 4.5% of risk-weighted assets, (b) raised the minimum Tier 1 Capital to risk-based assets requirement (“Tier 1 Capital Ratio) from 4% to 6% of risk-weighted assets and (c) assigned a higher risk weight of 150% to exposures that are more than 90 days past due or are on nonaccrual status and to certain commercial real estate facilities. The minimum ratio of Total Capital, as defined under the rules, to risk-weighted assets (including certain off-balance sheet activities, such as standby letters of credit) is 8%. At least 6% of the Total Capital is required to be “Tier 1 Capital”, which consists of common shareholders’ equity and certain preferred stock, less certain items and other intangible assets. The remainder, “Tier 2 Capital,” may consist of (a) the allowance for loan losses of up to 1.25% of risk-weighted assets, (b) excess of qualifying preferred stock, (c) hybrid capital instruments, (d) debt, (e) mandatory convertible securities and (f) qualifying subordinated debt. “Total Capital” is the sum of Tier 1 Capital and Tier 2 Capital less reciprocal holdings of other banking organizations’ capital instruments, investments in unconsolidated subsidiaries and any other deductions as determined by the federal banking regulatory agencies on a case-by-case basis or as a matter of policy after formal rule-making. A small bank holding company that has the highest regulatory examination rating and is not contemplating significant growth or expansion must maintain a minimum level of Tier 1 Capital to average total consolidated assets leverage ratio of at least 3%. All other bank holding companies are expected to maintain a leverage ratio of at least 100 to 200 basis points above the stated minimum.

The Basel Rules also require unrealized gains and losses on certain available-for-sale securities to be included for purposes of calculating regulatory capital unless a one-time opt-out was exercised. Additional constraints are also imposed on the inclusion in regulatory capital of mortgage-servicing assets and deferred tax assets. The Basel Rules limit a banking organization’s capital distributions and certain discretionary bonus payments if the banking organization does not hold a “capital conservation buffer” consisting of 2.5% of CET1 to risk-weighted assets in addition to the amount necessary to meet a minimum risk-based capital requirement. The purpose of the capital conservation buffer is to ensure that banking organizations conserve capital when it is needed most, allowing them to weather periods of economic stress. Banking institutions with a CET1 Ratio, Tier 1 Capital Ratio or Total Capital Ratio above the minimum capital ratios but below the minimum capital ratios plus the capital conservation buffer will face constraints on their ability to pay dividends, repurchase equity and pay discretionary bonuses to executive officers based on the amount of the shortfall. The Basel Rules became effective for the Bank on January 1, 2015. The capital conservation buffer requirement of 0.625% became effective January 1, 2016 and was phased in annually through January 1, 2019, when the full capital conservation buffer requirement of 2.50% became effective. At December 31, 2018, the Bank's capital conservation buffer requirement was 1.875%, and the actual capital conservation buffer was 5.54%.

Bank assets are given risk-weights of 0%, 20%, 50%, 100%, and 150%. In addition, certain off-balance sheet items are given similar credit conversion factors to convert them to asset equivalent amounts to which an appropriate risk-weight will apply. These computations result in the total risk-weighted assets. Most loans are assigned to the 100% risk category, except for performing first mortgage loans fully secured by residential property which carry a 50% risk-weighting. Loan exposures past due 90 days or more or on nonaccrual are assigned a risk-weighting of at least 100%. High volatility commercial real estate ("HVCRE") loan exposures are assigned to the 150% category; provided, however, Section 214 of the Economic Growth Act, prohibits federal banking agencies from requiring the financial institution to assign heightened risk weights to HVCRE loans unless the loan is related to real estate acquisition, development and construction (“HVCRE ADC”). Under the Basel III capital rules, HVCRE ADC loans are assigned a higher risk weight than other commercial real estate loans. Most investment securities (including, primarily, general obligation claims of states or other political subdivisions of the United States) are assigned to the 20% category, except for municipal or state revenue bonds, which have a 50% risk-weight, and direct obligations of the U.S. Treasury or obligations backed by the full faith and credit of the U.S. government, which have a 0% risk-weight. In converting off-balance sheet items, direct credit substitutes, including general guarantees and standby letters of credit backing nonfinancial obligations, and undrawn commitments (including commercial credit lines with an initial maturity of more than one year) have a 50% risk-weighting. Short-term undrawn commitments and commercial letters of credit with an initial maturity of under one year have a 50% risk-weighting and certain short-term unconditionally cancelable commitments are not risk-weighted.

Community Bank Leverage Ratio

The recently enacted Economic Growth Act requires federal banking agencies to develop a “community bank leverage ratio” (the ratio of a bank’s tangible equity capital to average total consolidated assets) for financial institutions with assets of less than $10 billion. A “qualifying community bank” that exceeds this ratio will be deemed to be in compliance with all other capital and leverage requirements, including the capital requirements to be considered “well capitalized” under prompt corrective action rules. The federal banking agencies may consider an institution’s risk profile when evaluating whether it qualifies as a community bank for purposes of the capital ratio requirement. The minimum capital for the new community bank leverage ratio must be set at not less than 8% and not more than 10%. A financial institution can elect to be subject to this new definition. The Economic Growth Act requires the federal banking agencies to consult with state banking regulators and notify the applicable state banking regulator of any qualifying community bank that exceeds or no longer exceeds the Community Bank Leverage Ratio.

Guidelines for Small Bank Holding Companies

The Dodd-Frank Act required the FRB to establish for all bank and savings and loan holding companies minimum consolidated capital requirements that are as stringent as those required for the insured depository subsidiaries. The FRB has updated and amended its Small Bank Holding Company Policy Statement to extend to bank and savings and loan holding companies the applicability of the “Small Bank Holding Company” exception to its consolidated capital requirements and, as a result of the Economic Growth Act, increased the threshold for the exception from $1.0 billion in consolidated assets to $3.0 billion in consolidated assets. As a result of the revised Small Bank Holding Company Policy Statement, Basel III capital rules and reporting requirements do not apply to small bank holding companies (“SBHC”), such as the Corporation, that have total consolidated assets of less than $3 billion unless otherwise advised by the FRB. The minimum risk-based capital requirements for a SBHC to be considered adequately capitalized are 4% for Tier 1 Capital and 8% for Total Capital to risk-weighted assets.

The regulations for SBHCs classify risk-based capital into two categories: “Tier 1 Capital” which consists of common and qualifying perpetual preferred shareholders’ equity less goodwill and other intangibles and “Tier 2 Capital” which consists of (a) the allowance for loan losses of up to 1.25% of risk-weighted assets, (b) the excess of qualifying preferred stock, (c) hybrid capital instruments, (d) debt, (e) mandatory convertible securities and (f) qualifying subordinated debt. Total qualifying capital consists of Tier 1 Capital and Tier 2 Capital less reciprocal holdings of other banking organizations’ capital instruments, investments in unconsolidated subsidiaries and any other deductions as determined by the FRB on a case-by-case basis or as a matter of policy after formal rule-making. However, the amount of Tier 2 Capital may not exceed the amount of Tier 1 Capital. The Corporation must maintain a minimum level of Tier 1 Capital to average total consolidated assets leverage ratio of 3%, which is the leverage ratio reserved for top-tier bank holding companies having the highest regulatory examination rating and not contemplating significant growth or expansion.

Bank holding company assets are given risk-weights of 0%, 20%, 50%, and 100%. In addition, certain off-balance sheet items are given similar credit conversion factors to convert them to asset equivalent amounts to which an appropriate risk-weight will apply. These computations result in the total risk-weighted assets.

As of December 31, 2018, the Corporation and the Bank exceeded all regulatory capital requirements.

Regulation of the Bank by the FDIC and the NJDOBI

As a New Jersey-chartered commercial bank, the Bank is subject to the regulation, supervision, and control of the NJDOBI. As an FDIC-insured institution, the Bank is also subject to regulation, supervision and control by the FDIC. The regulations of the FDIC and the NJDOBI impact virtually all activities of the Bank, including the minimum level of capital the Bank must maintain, the ability of the Bank to pay dividends, the ability of the Bank to expand through new branches or acquisitions, and various other matters.

Insurance of Deposits

Substantially all of the deposits of the Bank are insured up to applicable limits by the DIF of the FDIC and are subject to deposit insurance assessments to maintain the DIF. The Dodd-Frank Act permanently raised the standard maximum deposit insurance amount to $250,000.

The FDIC redefined its deposit insurance premium assessment base to be an institution’s average consolidated total assets minus average tangible equity as required by the Dodd-Frank Act and revised deposit insurance assessment rate schedules in light of the changes to the assessment base. The rate schedule and other revisions to the assessment rules, which were adopted by the FDIC Board of Directors on February 7, 2011, became effective April 1, 2011 and were first used to calculate the June 30, 2011 assessment. The assessment rules were further modified in November, 2014; the revisions became effective on January 1, 2015. Further modified as of September 30, 2016, the Bank’s assessment rate averaged $0.03 per $100 in assessable assets minus average tangible equity.

In addition to the assessment for deposit insurance, institutions are required to make payments on bonds issued in the late 1980s by the Financing Corporation (“FICO”) in connection with the failure of certain savings and loan associations. This payment obligation is established quarterly and averaged 0.31% and 0.52% of the assessment base for the years ended December 31, 2018 and 2017, respectively. The Corporation paid $25,000 and $40,000 under this assessment for the years ended December 31, 2018 and 2017, respectively. These assessments will continue until the FICO bonds mature in 2019.

FDIC’s Capital Adequacy Guidelines for Banks

Similar to the FRB, the FDIC has promulgated risk-based capital guidelines for banks that are designed to make regulatory capital requirements more sensitive to differences in risk profile among banks, to account for off-balance sheet exposure, and to minimize disincentives for holding liquid assets. These guidelines are substantially the same as those put in place by the FRB for bank holding companies.

Dividend Rights

Under the New Jersey Banking Act of 1948, as amended (the "New Jersey Banking Act"), a bank may declare and pay dividends only if, after payment of the dividend, the capital stock of the bank will be unimpaired and either the bank will have a surplus of not less than 50% of its capital stock or the payment of the dividend will not reduce the bank’s surplus.

Federal Securities Laws and Listing Requirements

The common stock of the Corporation is registered with the United States Securities Exchange Commission (the “SEC”) under the Securities Exchange Act of 1934, as amended (the “Exchange Act”) and is listed on the Nasdaq Capital Market under the symbol “SSFN.” The Corporation is subject to the reporting, information disclosure, corporate governance, proxy solicitation, insider trading and other requirements imposed on public companies by the SEC under the Exchange Act as well as the Securities Act. As a company listed on the Nasdaq Capital Market, we are also subject to the standards for Nasdaq-listed companies. The SEC and the Nasdaq have adopted regulations under the Sarbanes-Oxley Act of 2002 and the Dodd-Frank Act intended to improve corporate governance and the reliability of disclosures in SEC filings and provide enhanced penalties for financial reporting fraud. The Corporation's insiders are subject to limits on sales of our common stock and must file insider ownership reports with the SEC. The Corporation is currently a “smaller reporting company”, which allows us to provide certain simplified and scaled disclosures in our SEC filings. In June 2018, the SEC adopted rule amendments that raised the thresholds for a company to be eligible to provide scaled disclosures as a smaller reporting company to $250 million of public float. As such, the Corporation will remain a smaller reporting company for so long as the market value of the Corporation’s common stock held by non-affiliates as of the end of its most recently completed second fiscal quarter is less than $250 million. Although we remain a smaller reporting company, we have become an “accelerated filer” because our public float exceeds $75 million.

USA Patriot Act of 2001

On October 26, 2001, the USA Patriot Act of 2001 (the “Patriot Act”) was signed into law. Enacted in response to the terrorist attacks in New York, Pennsylvania, and Washington, D.C. on September 11, 2001, the Patriot Act is intended to strengthen the ability of U.S. law enforcement and the intelligence community to work cohesively to combat terrorism on a variety of fronts. The Patriot Act contains sweeping anti-money laundering and financial transparency laws and requires various regulations, including, but not limited to: (a) due diligence requirements for financial institutions that administer, maintain, or manage private bank accounts or correspondent accounts for non-U.S. persons; (b) standards for verifying customer identification at account opening; (c) rules to promote cooperation among financial institutions, regulators and law enforcement entities in identifying parties that may be involved in terrorism or money laundering; (d) reports of nonfinancial trades and business filed with the Treasury Department’s Financial Crimes Enforcement Network for transactions exceeding $10,000; and (e) filing of suspicious activities reports by brokers and dealers if they believe a customer may be violating U.S. laws and regulations.

Regulations promulgated under the Patriot Act impose obligations on financial institutions to maintain appropriate policies, procedures and controls to detect, prevent and report money laundering and terrorist financing. Failure of the Corporation or the Bank to comply with the Patriot Act’s requirements could have serious legal consequences for us and adversely affect our reputation.

Item 1A. Risk Factors

Investments in the common stock, no par value, of the Corporation (the "Common Stock") involve risk. The following discussion highlights the risks management believes are material for the Corporation, but does not necessarily include all risks that we may face.

Our operations are subject to interest rate risk and changes in interest rates may negatively affect financial performance.

Our earnings and cash flows are largely dependent upon our net interest income. Net interest income is the difference between interest income earned on interest-earning assets, such as loans and securities, and interest expense paid on interest-bearing liabilities, such as deposits and borrowed money. To be profitable we must earn more interest from our interest-earning assets than we pay on our interest-bearing liabilities. Changes in the general level of interest rates may have an adverse effect on our business, financial condition and results of operations. Interest rates are highly sensitive to many factors that are beyond our control, including general economic conditions, competitive factors and the policies of governmental and regulatory agencies such as the Federal Reserve Bank. Changes in monetary policy and interest rates can also adversely affect customer demand for our products and services and, thus, our ability to originate loans and deposits, the fair value of financial assets and liabilities and the average duration of our assets and liabilities. We are subject to interest rate risk to the degree that our interest-bearing liabilities reprice or mature more slowly or more rapidly or on a different basis than our interest-earning assets.

At December 31, 2018, $45.7 million of the total $65.7 million of our Federal Home Loan Bank borrowings, including $12.7 million of overnight borrowings, will mature during 2019. As these borrowings mature, we will need to either renew the borrowings at a potentially higher rate of interest, which would negatively impact our net interest income, or repay such borrowings. If we sell securities or other assets to fund the repayment of such borrowings, any decline in estimated market value with respect to the securities or assets sold would be realized and could result in a loss upon such sale.

Interest rates do and will continue to fluctuate. Although we cannot predict future Federal Open Market Committee ("FOMC"), or FRB actions or other factors that will cause rates to change, the FOMC indicates that in light of global economic and financial developments and muted inflation pressures, the FOMC will be patient as it determines what future adjustments to the federal funds rate may be appropriate to support a sustained economic expansion, strong labor market conditions and price stability. Despite the increases in short term interest rates experienced during 2018, short term rates remain relatively low and the yield curve remains extremely flat. The continued flat yield curve may adversely impact our net interest rate spread and net interest margin. No assurance can be given that changes in interest rates will not have a negative impact on our net interest income, net interest rate spread or net interest margin.

Our lending is concentrated to local markets and a decline in real estate markets and the local economy could adversely impact our financial condition and results of operations.
At December 31, 2018, our gross loan portfolio amounted to $733.8 million, 82.2% of which consisted of mortgage loans secured predominantly by real estate in Northern New Jersey. The majority of these real estate loans were secured by commercial real estate, amounting to $504.5 million or 68.8% of our loan portfolio at December 31, 2018. In addition, commercial loans amounted to $93.8 million or 12.8% of the gross loan portfolio at December 31, 2018 and commercial construction loans amounted to $9.8 million or 1.3% of the gross loan portfolio at such date. Commercial real estate mortgage loans, commercial loans and construction loans are generally viewed as exposing the lender to a greater risk of loss than fully underwritten one-to-four family residential mortgage loans and typically involve higher principal amounts per loan. Commercial real estate mortgage loans are typically dependent upon the successful operation of the related property. If the cash flow from the property is reduced, the borrower's ability to repay the loan may be impaired. If the borrower defaults, our only remedy may be to foreclose on the property, for which the market value may be less than the balance due on the related mortgage loan. The repayment of commercial business loans (the increased origination of which is part of management's strategy), is contingent on the successful operation of the related business. Repayment of construction loans is contingent upon the successful completion and operation of the project. Changes in local economic conditions and government regulations, which are outside the control of the borrower or lender, also could affect the value of the security for the loan or the future cash flow of the affected properties. Accordingly, a decline in local economic conditions would likely have an adverse impact on our financial condition and results of operations due to our lending concentration and lack of geographic diversity.
Declines in value may adversely impact our investment portfolio.
As of December 31, 2018, the Corporation had approximately $108.8 million and $62.3 million in available for sale and held-to-maturity investment securities, respectively. We may be required to record impairment charges on our investment securities if they suffer a decline in value that is considered other-than-temporary. Numerous factors, including lack of liquidity for sales of certain investment securities, absence of reliable pricing information for investment securities, adverse changes in business climate, adverse actions by regulators, or unanticipated changes in the competitive environment could have a negative effect on our investment portfolio in future periods. If an impairment charge is significant enough it could affect the ability of the Bank to upstream dividends to the Corporation, which could have a material adverse effect on our liquidity and our ability to pay dividends to shareholders and could also negatively impact our regulatory capital ratios.
An improved economy but a prolonged economic recovery has adversely affected the financial services industry and, because of our geographic concentration in northern New Jersey, we could be impacted by adverse changes in local economic conditions.

Our success depends on the general economic conditions of the nation, the State of New Jersey, and the northern New Jersey area. Although the nation's economy has improved, a prolonged economic recovery has severely adversely affected the banking industry and may adversely affect our business, financial condition, results of operations and stock price. Unlike larger banks that are more geographically diversified, we provide financial services to customers primarily in the market areas in which we operate. The local economic conditions of these areas have a significant impact on our commercial, real estate and construction loans, the ability of our borrowers to repay these loans and the value of the collateral securing these loans. While we did not and do not have a sub-prime lending program, any significant decline in the real estate market in our primary market area would hurt our business and mean that collateral

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for our loans would have less value. As a consequence, our ability to recover on defaulted loans by selling the real estate securing the loan would be diminished and we would be more likely to suffer losses on defaulted loans. Any of the foregoing events and conditions could have a material adverse effect on our business, results of operations and financial condition.

Our allowance for loan losses may be insufficient.

There are risks inherent in our lending activities, including dealing with individual borrowers, nonpayment, uncertainties as to the future value of collateral and changes in economic and industry conditions. We attempt to mitigate and manage credit risk through prudent loan underwriting and approval procedures, monitoring of loan concentrations and periodic independent review of outstanding loans. We cannot be assured that these procedures will reduce credit risk inherent in the business.

We make various assumptions and judgments about the collectability of our loan portfolio, including the creditworthiness of our borrowers and the value of the real estate and assets serving as collateral for loan repayments. In determining the size of our allowance for loan loss, we rely on our experience and our evaluation of economic conditions. If our assumptions prove to be incorrect, our current allowance may not be sufficient to cover probable incurred loan losses and adjustments may be necessary to allow for different economic conditions or adverse developments in our portfolio. Significant additions to our allowance for loan losses would materially decrease our net income. Various regulatory agencies, as an integral part of their examination process, periodically review the Corporation’s allowance for loan losses. Such agencies may require the Corporation to make additional provisions for loan losses based upon information available to them at the time of their examination.

If bank regulators impose limitations on the Bank’s commercial real estate lending activities, earnings could be adversely affected.
In 2006, the FDIC, the OCC and the FRB (collectively, the “Agencies”) issued joint guidance entitled “Concentrations in Commercial Real Estate Lending, Sound Risk Management Practices” (the “CRE Guidance”) intended to reinforce sound risk-management practices for financial institutions with high and increasing concentrations of commercial real estate loans on their balance sheets. Although the CRE Guidance did not establish specific lending limits, it provides that a bank’s commercial real estate lending exposure may receive increased supervisory scrutiny where total non-owner occupied commercial real estate loans, including loans secured by apartment buildings, investor commercial real estate and construction and land loans, represent 300% or more of an institution’s total risk-based capital and the outstanding balance of the commercial real estate loan portfolio has increased by 50% or more during the preceding 36 months. The Bank’s level of non-owner occupied commercial real estate equaled 290% of total risk-based capital at December 31, 2018. Including owner-occupied commercial real estate, the ratio of commercial real estate loans to total risk-based capital ratio would be 491% at December 31, 2018. At December 31, 2018, commercial real estate loans amounted to $528.5 million compared to $363.0 million at December 31, 2015, an increase of $165.5 million or 46% over such 36 month period.

In December 2015, the Agencies released a new statement on prudent risk management for commercial real estate lending that expressed the Agencies concerns about easing commercial real estate underwriting standards, direct financial institutions to maintain underwriting discipline and exercise risk management practices to identify, measure and monitor lending risks, and indicate that the Agencies will continue “to pay special attention” to commercial real estate lending activities and concentrations going forward. If the FDIC were to impose restrictions on the amount of commercial real estate loans that the Bank can hold in its portfolio, or require higher capital ratios as a result of the level of commercial real estate loans held, the Bank’s earnings would be adversely affected.
The Corporation’s future growth may require the Corporation to raise additional capital in the future, but that capital may not be available when it is needed or may be available only at an excessive cost.
The Corporation is required by regulatory authorities to maintain adequate levels of capital to support its operations. The Corporation anticipates that current capital levels will satisfy regulatory requirements for the foreseeable future.

The Corporation, however, may at some point choose to raise additional capital to support its continued growth. The

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Corporation's ability to raise additional capital will depend, in part, on conditions in the capital markets at that time, which are outside of the Corporation's control. Accordingly, the Corporation may be unable to raise additional capital, if and when needed, on terms acceptable to the Corporation, or at all. If we cannot raise additional capital when needed, our ability to further expand operations through internal growth and acquisitions could be materially impacted. In the event of a material decrease in the Corporation's stock price, future issuances of equity securities could result in dilution of existing shareholder interests.
A decrease in our ability to borrow funds could adversely affect our liquidity.
Our ability to obtain funding from the Federal Home Loan Bank or through our overnight federal funds lines with other banks could be negatively affected if we experienced a substantial deterioration in our financial condition or if such funding becomes restricted due to deterioration in the financial markets. While we have a contingency funds management plan to address such a situation if it were to occur (such plan includes deposit promotions, the sale of securities and the curtailment of loan growth, if necessary), a significant decrease in our ability to borrow funds could adversely affect our liquidity.
Our inability to fulfill minimum capital requirements could limit our ability to conduct or expand our business or pay a dividend and impact our financial condition, results of operations and the market price of our Common Stock.

In July 2013, the FDIC and other federal bank regulatory agencies adopted final rules that established a new comprehensive capital framework for U.S. banking organizations. These rules, generally referred to as the "Basel Rules," create a new regulatory capital standard based on Tier 1 common equity, increase the minimum leverage and risk-based capital ratios applicable to all banking organizations and change how certain regulatory capital components are calculated. See "Capital Adequacy Guidelines for Banks and Bank Holding Companies" under Item 1 for a detailed description of the various capital requirements to which the Corporation and the Bank are, and in the future may be, subject to. Compliance with these regulatory capital requirements may limit our ability to engage in operations that require the intensive use of capital and could adversely affect our ability to maintain our current level of business or expand our business. Furthermore, if we fail to comply with these regulatory capital requirements, the FRB could place limits or conditions on the operation of our business and subject us to a variety of enforcement remedies, including limiting our ability to pay dividends.

External factors, many of which we cannot control, may result in liquidity concerns for us.

Liquidity risk is the potential that the Corporation will be unable to: meet its obligations as they come due; capitalize on growth opportunities as they arise; or pay regular dividends, because of the Corporation's inability to liquidate assets or obtain adequate funding on a timely basis, at a reasonable cost and within acceptable risk tolerances.

Liquidity is required to fund various obligations, including credit commitments to borrowers, loan originations, withdrawals by depositors, repayment of borrowings, operating expenses, capital expenditures and dividends to shareholders.

Liquidity is derived primarily from deposit growth and retention; principal and interest payments on loans; principal and interest payments on investment securities; sale, maturity and prepayment of investment securities; borrowing capacity; net cash provided from operations and access to other funding sources.

Our access to funding sources in amounts adequate to finance our activities could be impaired by factors that affect us specifically or the financial services industry in general. Factors that could detrimentally impact our access to liquidity sources include a decrease in the level of our business activity due to a prolonged economic downturn or adverse regulatory action against us. Our ability to borrow could also be impaired by factors that are not specific to us, such as a severe disruption of the financial markets or negative views and expectations about the prospects for the financial services industry as a whole.

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Competition within the financial services industry and from non-banks could adversely affect our profitability.

We face strong competition from banks, other financial institutions, money market mutual funds, brokerage firms and non-banks within the New York metropolitan area. A number of these entities have substantially greater marketing and advertising resources and lending limits, larger branch systems and a wider array of banking services. Competition among depository institutions for customer deposits has increased significantly and will likely continue in the current economic environment. Our success depends upon our ability to serve our clients in a more responsive manner than our competitors. If we are unsuccessful in competing effectively, we will lose market share and may suffer a reduction in our margins and adverse consequences to our business, results of operations and financial condition.

The unexpected loss of management or key personnel could impair the Corporation’s future success.
The Corporation’s future success depends in part on the continued service of its executive officers, other key management, and staff, as well as its ability to continue to attract, motivate, and retain additional highly qualified employees. The loss of services of one or more of the Corporation’s key personnel or its inability to timely recruit replacements for such personnel, or to otherwise attract, motivate, or retain qualified personnel could have an adverse effect on the Corporation’s business, operating results and financial condition.
If we cannot keep pace with technological changes in the financial services industry, we may not be able to compete effectively.

The financial services industry continues to undergo rapid technological changes, including developments in internet-based and mobile banking, with the aim to better serve customers and reduce costs. Our ability to compete successfully in the future will depend, in part, upon our ability to anticipate and respond to customer demands for technology-driven banking products and services and to invest the resources required to implement, maintain and upgrade the technology required to provide these products and services. Many of our competitors have substantially greater resources to invest in these technological improvements. Although we continually invest in new technology, we cannot provide assurance that we will have sufficient resources to remain competitive in the future. Our inability to keep pace with technological changes could have a material adverse impact on our business and, in turn, our financial condition and results of operations.

Federal and State regulations could restrict our business and increase our costs and non-compliance would result in penalties, litigation and damage to our reputation.

We operate in a highly regulated environment and are subject to extensive regulation, supervision, and examination by the FDIC, the FRB and the State of New Jersey. The significant federal and state banking regulations that we are subject to are described herein under “Item 1. Business.” The regulation and supervision of the activities in which bank and bank holding companies may engage is primarily intended for the protection of the depositors and the federal deposit insurance funds. These regulations affect our lending practices, capital structure, investment practices, dividend policy and overall operations. These statutes, regulations, regulatory policies, and interpretations of policies and regulations are constantly evolving and may change significantly over time. Any such changes could subject the Corporation to additional costs, limit the types of financial services and products the Bank may offer and/or increase the ability of non-banks to offer competing financial services and products, among other things. New federal and/or state laws and regulations of lending and funding practices and liquidity standards continue to be implemented and bank regulatory agencies are being very aggressive in responding to concerns and trends identified in bank examinations with respect to bank capital requirements. Any increased government oversight may increase our costs and limit our business opportunities. Our failure to comply with laws, regulations or policies applicable to our business could result in sanctions against us by regulatory agencies, civil money penalties and/or reputation damage, which could have a material adverse effect on our business, financial condition and results of operations. While we have policies and procedures designed to prevent any such violations, there can be no assurances that such violations will not occur.

The Dodd-Frank Act requires lenders to make a reasonable, good faith determination of a borrower's ability to repay a mortgage. The CFPB has promulgated a safe harbor rule for any loan that constitutes a "qualified mortgage." Loans that meet this “qualified mortgage” definition will be presumed to have complied with the new ability-to-repay standard. Under the CFPB’s rule, a “qualified mortgage” loan must not contain certain specified features, including: excessive upfront points and fees (those exceeding 3% of the total loan amount, less “bona fide discount points” for prime loans); interest-only payments; negative-amortization; and terms longer than 30 years. Also, to qualify as a “qualified mortgage,” a borrower’s total debt-to-income ratio may not exceed 43%. Lenders must also verify and document the income and financial resources relied upon to qualify the borrower for the loan and underwrite the loan based on a fully amortizing payment schedule and maximum interest rate during the first five years, taking into account all applicable taxes, insurance and assessments. The CFPB’s rule on qualified mortgages could limit our ability or desire to make certain types of loans or loans to certain borrowers, or require that we invest significantly greater resources to make these loans and, therefore, limit our growth and adversely affect our profitability. The recently enacted Economic Growth Act provides for a new safe harbor category of qualified mortgage loans originated by institutions with less than $10 billion in total consolidated assets under existing qualified mortgage and ability to pay rules, which when promulgated by the CFSB should afford to community banks the ability to exercise greater discretion in lending decisions.

A breach of our information systems through a system failure, cyber-security breach, computer virus or disruption or interruption of service or a compliance breach by one of our vendors could negatively affect our reputation, our business and our earnings.

Information technology systems are critical to our business. The financial services industry has experienced an increase in both the number and severity of reported cyber-attacks aimed at gaining unauthorized access to bank systems for purposes of misappropriating assets or sensitive information, corrupting data, or causing operational disruption. We rely heavily upon a variety of computing platforms and networks over the Internet for the purpose of data processing, communication and information exchange and to conduct and manage various aspects of our business and provide our customers with the ability to bank online. We have business continuity and data security systems, policies and procedures designed to prevent or limit the effect of the failure, interruption or security breach of our information systems and controls in place to monitor vendor risks. Despite the safeguards instituted by management, our systems may be vulnerable to a breach of security through unauthorized access, phishing schemes, computer viruses and other security problems, as well as failures and disruptions of services resulting from power outages and other circumstances.

The Corporation maintains policies and procedures to prevent or limit the impact of system failures, interruptions and security breaches (including privacy breaches), but such events may still occur or may not be adequately addressed if they do occur. In addition, any compromise of our systems could deter customers from using our products and services. Although we rely on security systems to provide security and authentication necessary to effect the secure transmission of data, these precautions may not fully protect our systems from compromises or breaches of security.

Our information technology environment/network, including disaster recovery and business continuity planning, are outsourced to a third party hosted environment. In addition, we rely on the service of a variety of third-party vendors to meet our data processing needs. If any of these third-party providers encounters a system failure, cyber-security breach or other difficulties, or if we have difficulty communicating with any of these third-party providers, our ability to adequately process and account for transactions could be affected, and our business operations could be adversely affected. Threats to information security also exist in the processing of customer information through various other vendors and their personnel.

The occurrence of any system failures, interruption or breach of security involving us or our vendors could result in the compromise of our confidential information and the confidential information of our customers, employees and others. In such event, we could be exposed to claims, litigation, financial losses, costs and damages. Such damages could materially affect our earnings. In addition, any failure, interruption or breach in security could also result in failures or disruptions in our general ledger, deposit, loan and other systems and could subject us to additional regulatory scrutiny. In addition, the negative affect on our reputation could affect our ability to deliver products and services successfully to existing customers and to attract new customers. Any of the foregoing events and conditions could have a material adverse effect on our business, results of operations and financial condition. The Corporation has not experienced any cyber incidents that are, individually or in the aggregate, material. The Corporation outsources certain cyber security functions, such as penetration testing, to third party service providers but does not outsource any cyber security function that has material cybersecurity risk.

We may not be able to sustain or increase the market price of our Common Stock.

The trading history of our Common Stock, which trades on the Nasdaq Capital Market, has been characterized by relatively low trading volume. The limited trading market for our Common Stock may cause fluctuations in the market value of our Common Stock to be exaggerated and lead to price volatility in excess of that which would occur in a more active trading market. The current market price of our Common Stock may not be indicative of future market prices and we may be unable to sustain or increase the value of an investment in our Common Stock. Volatility in the market price of our Common Stock may occur in response to numerous factors, including, but not limited to, the factors discussed in the other risk factors and the following:

- actual or anticipated fluctuation in our operating and financial results;
- press releases, publicity, or announcements concerning us, our competitors or the banking industry;
- changes in expectations as to future financial performance, including estimates by securities analysts and investors;
- changes in accounting standards, policies, guidance, interpretations or principles;
- future sales of our Common Stock or other equity securities;
- developments in laws or regulations or new interpretations of existing laws or regulations affecting us or our competitors; and
- general domestic economic and market conditions.

These factors may adversely affect the trading price of our Common Stock, regardless of our actual operating performance, and could prevent a shareholder from selling our Common Stock at or above the current market price.

We may be unable to generate sufficient cash to service our Subordinated Notes and other debt obligations.

The Corporation’s principal source of cash flow is dividends and distributions from the Bank; however, we cannot be assured that the Bank will, in any circumstances, pay dividends to us. Various federal and state statutes, regulations and rules limit, directly or indirectly, the amount of dividends that the Bank may pay to us without regulatory approval. There can be no assurances that we would receive such approval if required. If the Bank fails to make dividend payments to us, and sufficient cash is not otherwise available, we may be unable to make principal and interest payments on the Subordinated Notes (see discussion of the Subordinated Notes in Note 8 to the consolidated financial statements included in this annual report) and our other debt obligations.

Our ability to make payments on and to refinance our indebtedness, including the Subordinated Notes, will depend on our financial and operating performance. We may be unable to maintain a level of cash flows from operating activities sufficient to permit us to pay the principal, premium, if any, and interest on our indebtedness, including the Subordinated Notes. If our cash flows and capital resources, and the dividends we receive from the Bank, are insufficient to fund our debt service obligations, we may be unable to provide new loans, other products or to fund our obligations to existing customers and otherwise implement our business plans. As a result, we may be unable to meet our scheduled debt service obligations. In the absence of sufficient operating results and resources, we could face substantial liquidity issues and we might be required to dispose of material assets or operations to meet our debt service and other obligations, or seek to restructure our indebtedness, including the Subordinated Notes. In such event, there could be no assurance that we would be able to consummate these transactions, and proceeds of such transactions might not be adequate to meet our debt service obligations then due.

If we fail to make interest and principal payments on the Subordinated Notes, the terms of the Subordinated Notes will restrict us from paying dividends to our common shareholders and this may adversely affect the market price of our Common Stock.

If we fail to make payments of principal or interest on the Subordinated Notes or a default occurs under the Subordinated Notes, the Corporation is not permitted to pay or declare dividends or distributions on or redeem, purchase, acquire or make a liquidation payments with respect to our Common Stock.

Further, our ability to pay dividends to our shareholders is always subject to legal and regulatory restrictions. Any payment of dividends in the future will depend, in large part, on the Corporation's earnings, capital requirements, financial condition and other factors considered relevant by the Corporation's Board of Directors. Although we have historically paid cash dividends on our Common Stock, we are not required to do so and our Board of Directors could reduce or eliminate our Common Stock dividend in the future. Our shareholders bear the risk that no dividends will be paid on our Common Stock in future periods or that, if paid, such dividends will be reduced, which may negatively impact the market price of our Common Stock.

Anti-takeover provisions in our Restated Certificate of Incorporation, our Amended and Restated By-Laws and New Jersey law could discourage a change of control that our shareholders may favor, which could negatively affect the market price of our Common Stock.

Provisions in our Restated Certificate of Incorporation and our Amended and Restated By-Laws and applicable provisions of the New Jersey Business Corporation Act may make it more difficult and expensive for a third party to remove our directors and acquire control of us even if a change of control would be beneficial to the interests of our shareholders. These provisions could discourage potential takeover attempts and could adversely affect the market price of our Common Stock. For example, applicable provisions of the New Jersey Business Corporation Act may discourage, delay or prevent a change in control by prohibiting us from engaging in a business combination with an interested shareholder for a period of five years after the person becomes an interested shareholder. Our Restated Certificate of Incorporation provides for staggered terms for our directors and authorizes the issuance of blank check preferred stock that could be issued by our Board of Directors to thwart a takeover attempt and requires super-majority voting by our shareholders to effect amendments to certain provisions of our Restated Certificate of Incorporation. In addition, our Amended and Restated By-Laws limit who may call special meetings of both the board of directors and shareholders and establish advance notice requirements for nominating candidates for election to the Board of Directors or for proposing matters that can be acted upon by shareholders at shareholders' meetings.

Federal banking laws limit the acquisition and ownership of our Common Stock.

Because we are a bank holding company, any purchaser of 5% or more of our Common Stock may be required to file a notice with or obtain the approval of the FRB under the Change in Bank Control Act of 1978, as amended. Specifically, under regulations adopted by the FRB, (1) any other bank holding company may be required to obtain the approval of the FRB before acquiring 5% or more of our Common Stock and (2) any person other than a bank holding company may be required to file a notice with and not be disapproved by the FRB to acquire 10% or more of our Common Stock.

Possible replacement of the LIBOR benchmark interest rate may have an impact on our business, financial condition or results of operations.

On July 27, 2017, the Financial Conduct Authority (FCA), a regulator of financial services firms in the United Kingdom, announced that it intends to stop persuading or compelling banks to submit LIBOR rates after 2021. The FCA and submitting LIBOR banks have indicated they will support the LIBOR indices through 2021 to allow for an orderly transition to an alternative reference rate. In the United States, efforts to identify a set of alternative U.S. dollar reference interest rates include proposals by the Alternative Reference Rates Committee of the Federal Reserve Board. Other financial services regulators and industry groups are evaluating the possible phase-out of LIBOR and the development of alternate reference rate indices or reference rates. Our assets and liabilities that are indexed to LIBOR are very limited. Nevertheless, we are evaluating the potential impact of the possible replacement of the LIBOR benchmark interest rate, but are not able to predict whether LIBOR will cease to be available after 2021, whether the alternative rates the Federal Reserve Board proposes to publish will become market benchmarks in place of LIBOR, or what the impact of such a transition will have on our business, financial condition, or results of operations.

Item 1B. Unresolved Staff Comments

None.

Item 2. Properties

The Corporation conducts its business through its main office located at 630 Godwin Avenue, Midland Park, New Jersey and its current eleven branch offices. The property located at 612 Godwin Avenue is used for administrative offices, primarily for commercial lending functions. The following table sets forth certain information regarding the Corporation's properties as of December 31, 2018:

Location	Leased or Owned	Date of Lease Expiration
612 Godwin Avenue Midland Park, NJ	Owned	---
630 Godwin Avenue Midland Park, NJ	Owned	---
386 Lafayette Avenue Hawthorne, NJ	Owned	---
87 Berdan Avenue Wayne, NJ	Leased	6/30/24
64 Franklin Turnpike Waldwick, NJ	Owned	---
190 Franklin Avenue Ridgewood, NJ	Leased	9/30/22
311 Valley Road Wayne, NJ	Leased	11/30/23
249 Newark Pompton Turnpike Pequannock, NJ	Owned	---
2 Changebridge Road Montville, NJ	Leased	7/31/20
378 Franklin Avenue Wyckoff, NJ	Leased	5/31/26
200 Kinderkamack Road Westwood, NJ	Leased	5/30/26
33 Sicomac Road North Haledon, NJ	Leased	10/31/20
43 S. Park Place Morristown, NJ	Leased	06/30/22

We believe that our properties are in good condition, well maintained and adequate for the present and anticipated needs of our business.

Item 3. Legal Proceedings

The Corporation and the Bank are parties to or otherwise involved in legal proceedings arising in the normal course of business from time to time, such as claims to enforce liens, claims involving the making and servicing of real property loans, and other issues incident to the Bank's business. Management does not believe that there is any pending or threatened proceeding against the Corporation or the Bank which, if determined adversely, would have a material effect on the business or financial position of the Corporation or the Bank.

Item 4. Mine Safety Disclosures

Not applicable.

Part II

Item 5. Market for the Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

The Corporation's Common Stock trades on the Nasdaq Capital Market under the symbol "SSFN". As of March 13, 2019, there were approximately 1,000 shareholders of record of the Common Stock.

During the years ended December 31, 2018 and 2018, the Corporation paid quarterly dividends of $0.03 per share. The amount of future dividends, if any, will be determined by our Board of Directors and will depend on our earnings, most of which are generated by the Bank, our financial condition and other factors considered by our Board of Directors to be relevant.

We rely on the Bank to pay dividends to us to fund our dividend payments to our shareholders. The Bank's ability to pay dividends to us will depend primarily upon its earnings, financial condition, and need for funds, as well as applicable governmental policies. Even if the Bank has earnings in an amount sufficient to distribute cash to us to enable us to pay dividends to our shareholders, the Bank's Board of Directors may determine to retain earnings for the purpose of funding the Bank's growth. The Bank generally pays us a dividend to provide funds for debt service on our outstanding indebtedness, dividends that we pay our shareholders and other expenses.

Under the New Jersey Banking Act, the Bank may not pay a cash dividend unless, following the payment of such dividend, the capital stock of the Bank will be unimpaired and (i) the Bank will have a surplus of no less than 50% of its capital stock or (ii) the payment of such dividend will not reduce the surplus of the Bank. In addition, the Bank cannot pay dividends if doing so would reduce its capital below the regulatory imposed minimums.

As of December 31, 2018, we had $23.6 million aggregate principal amount of indebtedness outstanding, consisting of a subordinated debenture in the principal amount of $7.0 million scheduled to mature in 2033 and $16.6 million aggregate principal amount of 6.75% Fixed-to-Floating Rate Subordinated Notes due in 2025. The agreements under which our indebtedness was issued prohibit us from paying any dividends on our Common Stock or making any other distributions to our shareholders at any time when there shall have occurred and be continuing an event of default under the applicable agreement.

Events of default generally consist of, among other things, our failure to pay any principal or interest on the subordinated debenture or subordinated notes, as applicable, when due, our failure to comply with certain agreements, terms and covenants under the agreement (without curing such default following notice), and certain events of bankruptcy, insolvency or liquidation relating to us.

If an event of default were to occur and we did not cure it, we would be prohibited from paying any dividends or making any other distributions to our shareholders or from redeeming or repurchasing any of our Common Stock, which would likely have a material adverse effect on the market value of our Common Stock. Moreover, without notice to and consent from the holders of our Common Stock, we may enter into additional financing arrangements that may limit our ability to purchase or to pay dividends or distributions on our Common Stock.

We paid cash dividends of $0.12 per share for each of the years ended December 31, 2018 and 2017. We did not repurchase any shares of our Common Stock during the years ended December 31, 2018 and 2017.

Item 6. Selected Financial Data

The following selected consolidated financial data of the Corporation is qualified in its entirety by, and should be read in conjunction with, the consolidated financial statements, including notes, thereto, included elsewhere in this annual report.

STEWARDSHIP FINANCIAL CORPORATION AND SUBSIDIARY CONSOLIDATED
FINANCIAL SUMMARY OF SELECTED FINANCIAL DATA

	December 31,				
	2018	2017	2016	2015	2014
	(Dollars in thousands, except per share amounts)				
Selected Balance Sheet Data at Year End:					
Total assets	$955,630	$928,766	$795,535	$717,888	$693,551
Total interest-earning assets	912,022	886,479	759,805	685,141	661,672
Total investment securities (including FHLB stock)	176,732	169,172	154,428	156,700	183,792
Total loans, net of allowance for loan loss	725,404	702,561	595,952	517,556	467,699
Total deposits	782,091	764,099	658,930	604,753	556,476
Total borrowings	89,082	87,077	82,452	63,186	73,917
Shareholders' equity	80,150	73,665	51,387	47,573	58,969
Earnings Summary:					
Net interest income	$28,163	$26,372	$22,572	$21,783	$21,727
Provision for loan losses	(1,615)	655	(1,350)	(1,375)	(50)
Net interest income after provision for loan losses	29,778	25,717	23,922	23,158	21,777
Noninterest income	3,417	3,307	3,411	3,493	2,960
Noninterest expense	22,145	20,301	19,902	20,179	20,233
Income before income tax expense	11,050	8,723	7,431	6,472	4,504
Income tax expense	3,020	4,776	2,695	2,272	1,419
Net income	8,030	3,947	4,736	4,200	3,085
Dividends on preferred stock and accretion	—	—	—	456	683
Net income available to common shareholders	$8,030	$3,947	$4,736	$3,744	$2,402
Common Share Data:					
Basic and diluted net income	$0.93	$0.50	$0.78	$0.62	$0.40
Cash dividends declared	0.12	0.12	0.11	0.08	0.05
Book value at year end	9.23	8.51	8.39	7.82	7.29
Weighted average shares outstanding (in thousands)	8,673	7,907	6,110	6,078	6,004
Shares outstanding at year end (in thousands)	8,680	8,653	6,121	6,086	6,035
Performance Ratios:					
Return on average assets	0.86%	0.45%	0.63%	0.60%	0.46%
Return on average common shareholders' equity	10.54%	5.86%	9.43%	8.14%	5.77%

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	December 31,				
	2018	2017	2016	2015	2014
	(Dollars in thousands, except per share amounts)				
Net interest margin	3.14 %	3.13 %	3.18 %	3.30 %	3.46 %
Yield on average interest-earning assets	4.02 %	3.83 %	3.81 %	3.87 %	3.96 %
Cost of average interest-bearing liabilities	1.17 %	0.91 %	0.85 %	0.77 %	0.68 %
Net interest spread	2.85 %	2.92 %	2.96 %	3.10 %	3.28 %
Loans to deposits	93.77 %	93.09 %	91.64 %	87.04 %	85.77 %
Asset Quality:					
Total non-accrual loans	$1,544	$1,194	$606	$1,882	$3,628
Other nonperforming assets	$—	$—	$401	$880	$1,308
Allowance for loan loss to total loans	1.08 %	1.23 %	1.31 %	1.68 %	2.01 %
Nonperforming loans to total loans	0.21 %	0.17 %	0.10 %	0.36 %	0.76 %
Nonperforming assets to total assets	0.16 %	0.13 %	0.13 %	0.38 %	0.71 %
Net charge-offs (recoveries) to average loans	(0.11)%	(0.03)%	(0.08)%	(0.12)%	0.06 %
Consolidated Capital Ratios:					
Average shareholders' equity as a percentage of average total assets	8.12 %	7.61 %	6.69 %	7.98 %	8.42 %
Leverage (Tier 1) capital (1)	9.33 %	8.88 %	7.65 %	7.67 %	9.45 %
Tier 1 risk based capital (2)	11.33 %	10.96 %	9.35 %	10.16 %	13.04 %
Total risk based capital (2)	14.39 %	14.29 %	13.10 %	14.34 %	14.30 %
Other Data:					
Number of banking centers (including main branch)	12	12	11	12	12
Full time equivalent employees	133	130	130	134	140

(1) As a percentage of average quarterly assets.
(2) As a percentage of total risk-weighted assets.

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

This section provides an analysis of the Corporation's consolidated financial condition and results of operations for the years ended December 31, 2018 and 2017. The analysis should be read in conjunction with the related audited consolidated financial statements and the accompanying notes presented elsewhere herein.

As used in this annual report, "we", "us" and "our" refer to Stewardship Financial Corporation and its consolidated subsidiary, Atlantic Stewardship Bank, depending on the context.

Introduction

The Corporation's primary business is the ownership and supervision of the Bank and, through the Bank, the Corporation has been, and intends to continue to be, a community-oriented financial institution offering a variety of financial services to meet the needs of the communities it serves. As of December 31, 2018, the Corporation had 12 full service branch offices located in Bergen, Passaic and Morris Counties in New Jersey. The Corporation, through the Bank, conducts a general commercial and retail banking business encompassing a wide range of traditional deposit and lending functions along with other customary banking services. The Corporation earns income and generates cash primarily through the deposit gathering activities of the branch network. These deposits gathered from the general public are then utilized to fund the Corporation's lending and investing activities.

The Corporation has developed a strong deposit base with good franchise value. A mix of a variety of different deposit products and electronic services, along with a strong focus on customer service, is used to attract customers and build depositor relationships. Challenges facing the Corporation include our ability to continue to grow the branch deposit levels, provide adequate technology enhancements to achieve efficiencies, offer a competitive product line, and provide the highest level of customer service.

The Corporation is affected by the overall economic conditions in northern New Jersey, the interest rate and yield curve environment, and, to a lesser extent, the overall national economy. Each of these factors has an impact on our ability to attract specific deposit products, our ability to invest in loan and investment products, and our ability to earn acceptable profits without incurring increased risks.

When evaluating the financial condition and operating performance of the Corporation, management reviews historical trends, peer comparisons, asset and deposit concentrations, interest margin analysis, adequacy of loan loss reserve and loan quality performance, adequacy of capital under current positions as well as to support future expansion, adequacy of liquidity, and overall quality of earnings performance.

The branch network coupled with our online services provides for solid coverage in both existing and new markets in key towns in the three counties in which we operate. The Corporation continually evaluates the need to further develop its infrastructure, including electronic products and services, to enable it to continue to build franchise value and expand its existing and future customer base.

The level of consumers and businesses looking to borrow remained steady in 2018. The managing of credit risk continues to be relatively steady for the Bank and is reflected in our stable asset quality measurements. All new lending opportunities continue to be appropriately evaluated. The Corporation has never engaged in subprime lending.

Competition in the northern New Jersey market remains intense and the challenges of operating in a prolonged, relatively flat interest rate market has continued to make it somewhat difficult to attract deposits when interest rate levels, although rising, are still generally low. In an effort to address the strong competition in attracting deposit balances, the Corporation continues to evaluate product and services offerings. Improvements and upgrades of our electronic / online banking products and services continue to be a priority. Management believes that the Corporation offers the majority of the services that our competitors offer and what today's customers require. Electronic products and services available to our customers include: online banking / cash management, with remote deposit capture services for businesses, applications for smartphones and tablets, mobile deposit capabilities, online deposit account opening, pay other people payment service and Apple Pay. These electronic banking products and services continue to provide our customers with additional means to access their accounts conveniently. Our security for online banking customers includes a multi-factor authentication sign-on. In addition, the Corporation has the technology and procedures to enable instant debit card issuance for new customers and existing customers.

We remained committed to managing our infrastructure and containing costs and expenses while growing the balance sheet. Nevertheless, the Corporation continues to balance the need to control expenses with its focus on quality loan growth and an awareness of the customers' desire for convenient banking – all being addressed while continuing to be compliant with regulations and remaining up-to-date on all levels of security.

During 2019, the Corporation will continue to concentrate its efforts on the origination of loans funded with appropriate deposit growth. In addition, capitalizing on technology and improving efficiencies will remain a focus for 2019.

Recent Accounting Pronouncements

A discussion of recent accounting pronouncements and their effect on the Corporation's Audited Consolidated Financial Statements can be found in Note 1 of the Corporation's Audited Consolidated Financial Statements contained in this Annual Report on Form 10-K.

Critical Accounting Policies and Estimates

"Management's Discussion and Analysis of Financial Condition and Results of Operations," as well as disclosures found elsewhere in this Annual Report on Form 10-K, are based upon the Corporation's Audited Consolidated Financial Statements, which have been prepared in conformity with U.S. generally accepted accounting principles ("GAAP"). The preparation of these financial statements requires the Corporation to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses. Note 1 to the Corporation's Audited Consolidated Financial Statements for the year ended December 31, 2018 contains a summary of the Corporation's significant accounting policies. Management believes the Corporation's policies with respect to the methodology for the determination of the allowance for loan losses involves a higher degree of complexity and requires management to make significant and subjective judgments, which often require assumptions or estimates about highly uncertain matters. Changes in these judgments, assumptions or estimates could materially impact results of operations. This critical policy and its application are periodically reviewed with the Audit Committee and the Board of Directors.

Allowance for Loan Losses. The allowance for loan losses is based upon management's evaluation of the adequacy of the allowance, including an assessment of known and inherent risks in the loan portfolio, giving consideration to the size and composition of the loan portfolio, actual loan loss experience, level of delinquencies, detailed analysis of individual loans for which full collectability may not be assured, the existence and estimated net realizable value of any underlying collateral and guarantees securing the loans, and current economic and market conditions. Although management uses the best information available, the level of the allowance for loan losses remains an estimate, which is subject to significant judgment and short-term change. Various regulatory agencies, as an integral part of their examination process, periodically review the Corporation's allowance for loan losses. Such agencies may require the Corporation to make additional provisions for loan losses based upon information available to them at the time of their examination. Furthermore, the majority of the Corporation's loans are secured by real estate in the State of New Jersey. Accordingly, the collectability of a substantial portion of the carrying value of the Corporation's loan portfolio is susceptible to changes in local market conditions and may be adversely affected should real estate values decline or the northern New Jersey area experience adverse economic changes. Future adjustments to the allowance for loan losses may be necessary due to economic, operating, regulatory and other conditions beyond the Corporation's control.

Earnings Summary

The Corporation reported net income of $8.0 million, or $0.93 per diluted common share, for the year ended December 31, 2018, compared to net income of $3.9 million, or $0.50 per diluted common share, for the year ended December 31, 2017. The results for the year ended December 31, 2017 were impacted by a charge of $1.4 million as a result of the enactment of comprehensive tax legislation commonly referred to as the Tax Cuts and Jobs Act ("Tax Act") on December 22, 2017.

The Tax Act, among other things, reduced the Federal statutory tax rate for corporations from 35% to 21% effective in 2018. While the Tax Act lowered the Corporation's future tax rate, it also required the Corporation to revalue its net deferred tax assets to account for the future impact of the lower corporate tax rate. As a result, for the year ended December 31, 2017, the Corporation recognized a charge of $1.4 million related to the revaluation of the net deferred tax assets. Excluding the impact of the Tax Act, net income for the year ended December 31, 2017 was $5.4 million, or $0.68 per diluted common share.

The reported return on average assets was 0.86% in 2018 compared to 0.45% in 2017. The return on average common equity was 10.54% for 2018 as compared to 5.86% in 2017. Excluding the Tax Act, return on average assets and return on average common equity for the year ended December 31, 2017 were 0.61% and 7.96%, respectively.

Results of Operations

Net Interest Income

The Corporation's principal source of revenue is the net interest income derived from the Bank, which represents the difference between the interest earned on assets and interest paid on funds acquired to support those assets. Net interest income is affected by the balances and mix of interest-earning assets and interest-bearing liabilities, changes in their corresponding yields and costs, and by the volume of interest-earning assets funded by noninterest-bearing deposits. The Corporation's principal interest-earning assets are loans made to businesses and individuals and investment securities.

For the year ended December 31, 2018, net interest income, on a tax equivalent basis, increased to $28.2 million from $26.5 million for the year ended December 31, 2017. The net interest rate spread and net yield on interest-earning assets for the year ended December 31, 2018 were 2.85% and 3.14%, respectively, compared to 2.92% and 3.13% for the year ended December 31, 2017.

In general, the net interest rate spread and net yield on interest-earning assets for the current year is reflective of the balance sheet growth - primarily loan growth funded by deposits.

For the year ended December 31, 2018, total interest income, on a tax equivalent basis, was $36.0 million compared to $32.4 million for the prior year. The increase was due to an increase in the average balance of interest-earning assets coupled with an increase in the overall yield on interest-earning assets. Average interest-earning assets increased $51.4 million in 2018 over the 2017 amount. The change in average interest-earning assets primarily reflects a $45.2 million increase from the comparable prior year in average loans. In addition, 2018 reflects a $6.8 million increase in average investment securities. The year ended December 31, 2018 included approximately $348,000 of interest recoveries and prepayment premiums on loan payoffs compared to $229,000 for the same prior year period. The average rate earned on interest-earning assets increased 0.19% from 3.83% for the year ended December 31, 2017 to 4.02% in the 2018 fiscal year.

Interest expense increased $2.0 million during the year ended December 31, 2018 to $7.8 million. For the year ended December 31, 2018, the average balance of interest-bearing deposits increased $54.2 million and average FHLB-NY borrowings decreased $22.1 million. For the year ended December 31, 2018, the total cost for interest-bearing liabilities was 1.17% compared to 0.91% for the prior year. In December 2018, the FDIC adopted a final rule related to the treatment of reciprocal deposits. The final rule implements Section 202 of the Economic Growth Act to exempt certain reciprocal deposits from being considered as brokered deposits for well-capitalized institutions. At December 31, 2018 and 2017, the Corporation had $37.1 million and $25.9 million, respectively, in aggregate deposits that were classified as brokered deposits by regulatory agencies.

The following table reflects the components of the Corporation's net interest income for the years ended December 31, 2018, 2017 and 2016 including: (1) average assets, liabilities and shareholders' equity based on average daily balances, (2) interest income earned on interest-earning assets and interest expense paid on interest-bearing liabilities, (3) average yields earned on interest-earning assets and average rates paid on interest-bearing liabilities, and (4) net yield on interest-earning assets. Nontaxable income from investment securities and loans is presented on a tax-equivalent basis assuming a statutory tax rate of 21% for 2018 and 34% for both 2017 and 2016. This was accomplished by adjusting non-taxable income upward to make it equivalent to the level of taxable income required to earn the same amount after taxes.

	2018			2017			2016		
	Average Balance	Interest Income/ Expense	Average Rates Earned/ Paid	Average Balance	Interest Income/ Expense	Average Rates Earned/ Paid	Average Balance	Interest Income/ Expense	Average Rates Earned/ Paid
	(Dollars in thousands)								
Assets									
Interest-earning assets:									
Loans (1)	$718,510	$31,532	4.39 %	$673,314	$28,421	4.22 %	$541,918	$23,762	4.38 %
Taxable investment securities	166,249	4,192	2.52 %	156,917	3,485	2.22 %	148,852	2,904	1.95 %
Tax-exempt investment securities (2)	6,003	186	3.10 %	8,574	375	4.37 %	11,229	566	5.04 %
Other interest-earning assets	6,910	138	2.00 %	7,515	106	1.41 %	13,981	79	0.57 %
Total interest-earning assets	897,672	36,048	4.02 %	846,320	32,387	3.83 %	715,980	27,311	3.81 %
Non-interest-earning assets:									
Allowance for loan losses	(8,459)			(8,412)			(8,546)		
Other assets	48,959			47,181			42,751		
Total assets	$938,172			$885,089			$750,185		
Liabilities and Shareholders' Equity									
Interest-bearing liabilities:									
Interest-bearing demand deposits	$310,014	$2,147	0.69 %	$259,637	$709	0.27 %	$234,847	$558	0.24 %
Savings deposits	83,731	84	0.10 %	89,586	92	0.10 %	86,804	90	0.10 %
Time deposits	203,109	3,062	1.51 %	193,397	2,388	1.23 %	149,067	1,644	1.10 %
FHLB-NY borrowings	52,377	968	1.85 %	74,440	1,177	1.58 %	38,288	716	1.87 %
Subordinated Debentures and Subordinated Notes	23,350	1,575	6.75 %	23,285	1,492	6.41 %	23,219	1,505	6.48 %
Total interest-bearing liabilities	672,581	7,836	1.17 %	640,345	5,858	0.91 %	532,225	4,513	0.85 %
Non-interest bearing liabilities:									
Demand deposits	185,406			173,936			165,348		
Other liabilities	4,005			3,413			2,396		
Shareholders' equity	76,180			67,395			50,216		
Total liabilities and Shareholders' equity	$938,172			$885,089			$750,185		
		28,212			26,529			22,798	

Net interest income (taxable equivalent basis)			
Tax equivalent adjustment	(49)	(157)	(226)
Net interest income	$28,163	$26,372	$22,572
Net interest spread (taxable equivalent basis)	2.85 %	2.92 %	2.96 %
Net yield on interest-earning assets (taxable equivalent basis) (3)	3.14 %	3.13 %	3.18 %

(1) For purpose of these calculations, nonaccrual loans are included in the average balance. Fees are included in loan interest.
(2) The tax equivalent adjustments are based on a marginal tax rate of 21% for 2018 and 34% for 2017 and 2016. Loans and total interest-earning assets are net of
unearned income. Securities are included at amortized cost.
(3) Net interest income (taxable equivalent basis) divided by average interest-earning assets.

The following table compares net interest income for the years ended December 31, 2018 and 2017 over the respective prior years in terms of changes from the prior year in the volume of interest-earning assets and interest-bearing liabilities and changes in yields earned and rates paid on such assets and liabilities on a tax-equivalent basis. The table reflects the extent to which changes in the Corporation's interest income and interest expense are attributable to changes in volume (changes in volume multiplied by prior year rate) and changes in rate (changes in rate multiplied by prior year volume). Changes attributable to the combined impact of volume and rate have been allocated proportionately to changes due to volume and changes due to rate.

	2018 Versus 2017			2017 Versus 2016		
	Increase (Decrease) Due to Change in			Increase (Decrease) Due to Change in		
	Volume	Rate	Net	Volume	Rate	Net
	(In thousands)					
Interest income:						
Loans	$1,944	$1,167	$3,111	$5,575	$(916)	$4,659
Taxable investment securities	216	491	707	164	416	580
Tax-exempt investment securities	(96)	(93)	(189)	(122)	(69)	(191)
Other interest-earning assets	2	30	32	(49)	76	27
Total interest-earning assets	2,066	1,595	3,661	5,568	(493)	5,075
Interest expense:						
Interest-bearing demand deposits	159	1,279	1,438	63	88	151
Savings deposits	(8)	—	(8)	3	(1)	2
Time deposits	122	552	674	531	213	744
FHLB borrowings	(388)	179	(209)	586	(125)	461
Subordinated Debentures and Subordinated Notes	4	79	83	4	(17)	(13)
Total interest-bearing liabilities	(111)	2,089	1,978	1,187	158	1,345
Net change in net interest income	$2,177	$(494)	$1,683	$4,381	$(651)	$3,730

Provision for Loan Losses

The Corporation maintains an allowance for loan losses at a level considered by management to be adequate to cover the probable incurred losses associated with its loan portfolio. On an ongoing basis, management analyzes the adequacy of this allowance by considering the nature and volume of the Corporation's loan activity, financial condition of the borrower, fair value of underlying collateral, and changes in general market conditions. Additions to the allowance for loan losses are charged to operations in the appropriate period. Actual loan losses, net of recoveries, reduce the allowance. The appropriate level of the allowance for loan losses is based on estimates, and ultimate losses may vary from current estimates.

The Corporation recorded a negative provision for loan losses of $1.6 million for the year ended December 31, 2018 compared to a provision of $655,000 for the year ended December 31, 2017. While growth in the loan portfolio generally requires the establishment of additional reserves, the negative loan loss provision in the current year reflects net recoveries of previously charged off loan balances of $779,000 for the year ended December 31, 2018. The negative loan loss provision also reflects the continued improvement in the economic conditions and overall real estate climate in the primary business markets in which the Corporation operates. The allowance for loan loss was $7.9 million, or 1.08% of total loans, as of December 31, 2018 compared to $8.8 million, or 1.23% of total loans, a year earlier.

The loan loss provision takes into account any growth or contraction in the loan portfolio and any changes in nonperforming loans as well as the impact of net charge-offs. In determining the level of the allowance for loan loss, the Corporation also considered the types of loans as well as the overall seasoning of loans to determine the risk that was inherent in the portfolio.

Nonperforming loans of $1.5 million at December 31, 2018, or 0.21% of total gross loans, reflected a slight increase from $1.2 million of nonperforming loans, or 0.17% of total gross loans, at December 31, 2017. During the year ended December 31, 2018, the Corporation charged-off $31,000 of loan balances and recovered $810,000 in previously charged-off loans compared to $4,000 and $206,000, respectively, in the prior year. The allowance for loan losses related to the impaired loans increased from $609,000 at December 31, 2017 to $649,000 at December 31, 2018.

In addition to these factors, the Corporation evaluated the economic conditions and overall real estate climate in the primary business markets in which it operates when considering the overall risk of the lending portfolio. Recent years showed improvement in the economy and the real estate market, which is reflected in a reduced level of charge-offs and loan delinquencies. The Corporation monitors its loan portfolio and intends to continue to provide for loan loss reserves based on its ongoing periodic review of the loan portfolio and general market conditions.

See “Asset Quality” section below for further information concerning the allowance for loan losses and nonperforming assets.

Noninterest Income

Noninterest income consists of all income other than interest income and is principally derived from service charges on deposits, income derived from bank-owned life insurance, gains from calls and sales of securities, gains and losses on sales of loans, unrealized gains on equity investments and income derived from debit cards and ATM usage. In addition, gains on sales of other real estate owned (“OREO”) are reflected as noninterest income.

Noninterest income was $3.4 million for the year ended December 31, 2018 as compared to $3.3 million for the prior year. The year ended December 31, 2018 reflected $193,000 of gains from the sale of the guaranteed portion of newly originated Small Business Administration ("SBA") loans. The year ended December 31, 2018 also included a positive $80,000 mark to market adjustment of a Community Reinvestment Act ("CRA") investment which is classified as an equity security. Such security has been owned for years for CRA purposes, but in connection with the adoption of ASU 2016-01, equity securities now require a quarterly mark to market through the income statement. Offsetting these increases, for the year ended December 31, 2018, the Corporation realized a $186,000 loss on calls and sales of securities primarily due to the sale of approximately $2.0 million of the CRA investment which is classified as an equity security. In addition, gain on sales of mortgage loans were $70,000 for the year ended December 31, 2018 compared to gains of $178,000 realized in the prior year. Finally, the year ended December 31, 2018 included no gains on sales of OREO compared to $13,000 of gains during the year ended December 31, 2017.

Noninterest Expense

For the years ended December 31, 2018 and 2017, total noninterest expense was $22.1 million and $20.3 million, respectively. The Corporation continues to appropriately control expenses. Increases in various expenses were offset by decreases in other expenses. The Corporation's largest expense is salaries and employee benefits, which increased $1.2 million. Such increase represented an increase in staff to support the Corporation's operations and continued growth, including costs associated with the establishment of of an SBA Lending Department in late 2017.

Income Taxes

Income tax expense totaled $3.0 million and $4.8 million for the years ended December 31, 2018 and 2017, respectively, representing effective tax rates of 27.3% and 54.8%. For the year ended December 31, 2017, tax expense reflects the previously discussed one-time charge related to the revaluation of the net deferred tax assets resulting from the enactment of the Tax Act.

Financial Condition

Total assets at December 31, 2018 were $955.6 million, an increase of $26.8 million, or 2.9%, over the $928.8 million at December 31, 2017. Securities available-for-sale were relatively unchanged while securities held-to-maturity increased $9.9 million to $62.3 million. Net loans increased $22.8 million to $725.4 million at December 31, 2018 compared to $702.6 million at December 31, 2017, reflecting continued improvement in loan demand. There were no loans held for sale at December 31, 2018 compared to $370,000 at December 31, 2017.

Loan Portfolio

The Corporation's loan portfolio at December 31, 2018, net of allowance for loan losses, totaled $725.4 million, an increase of $22.8 million, or a 3.3% increase over the $702.6 million at December 31, 2017. Residential real estate mortgages increased $3.3 million. Although certain residential real estate loans were placed into the portfolio to partially compensate for payoffs and normal amortization, the Corporation continued its policy of selling the majority of its residential real estate loans in the secondary market. Of the loans sold in 2018, all but $2.3 million of loans have been sold with servicing of the loan transferring to the purchaser. Commercial real estate mortgage loans consisting of $520.9 million, or 71.0% of the total portfolio, represent the largest portion of the loan portfolio. These loans reflected an increase of $16.8 million from $504.0 million, or 70.8% of the total loan portfolio, at December 31, 2017. Commercial loans increased $4.7 million to $93.8 million, representing 12.8% of the total loan portfolio. Consumer installment loans and home equity loans increased $3.8 million to $36.5 million.

The Corporation's lending activities are concentrated in loans secured by real estate located in northern New Jersey. Accordingly, the collectability of a substantial portion of the Corporation's loan portfolio is susceptible to changes in real estate market conditions in northern New Jersey. The Corporation has not made loans to borrowers outside the United States.

At December 31, 2018, aside from the real estate concentration described above, there were no concentrations of loans exceeding 10% of total loans outstanding. Loan concentrations are considered to exist when there are amounts loaned to a multiple number of borrowers engaged in similar activities which would cause them to be similarly impacted by economic or other related conditions.

The following table sets forth the classification of the Corporation's loans by major category at the end of each of the last five years:

	December 31,				
	2018	2017	2016	2015	2014
	(In thousands)				
Real estate mortgage:					
Residential	$82,491	$85,760	$84,321	$82,955	$77,836
Commercial (1)	520,868	504,028	407,226	348,724	295,278
Commercial loans	93,755	89,056	82,065	64,860	75,852
Consumer loans:					
Installment (2)	17,799	15,089	10,713	10,262	12,174
Home equity	18,685	17,548	19,566	19,425	15,950
Other	189	239	192	251	230
Total gross loans	733,787	711,720	604,083	526,477	477,320
Less: Allowance for loan losses	7,926	8,762	7,905	8,823	9,602
Deferred loan costs (fees)	457	397	226	98	19
Net loans	$725,404	$702,561	$595,952	$517,556	$467,699

(1) Includes construction loans and Government Guaranteed loans - guaranteed portion.
(2) Includes automobile, home improvement, second mortgages, and unsecured loans.

The following table sets forth certain categories of gross loans as of December 31, 2018 by contractual maturity. Borrowers may have the right to prepay obligations with or without prepayment penalties. This might cause actual maturities to differ from the contractual maturities summarized below.

	Within 1 Year	After 1 Year But Within 5 Years	After 5 Years	Total
	(In thousands)			
Real estate mortgage	$15,589	$43,423	$544,347	$603,359
Commercial	43,701	26,449	23,605	93,755
Consumer	151	1,610	34,912	36,673
Total gross loans	$59,441	$71,482	$602,864	$733,787

The following table sets forth the dollar amount of all gross loans due one year or more after December 31, 2018, which have predetermined interest rates or floating or adjustable interest rates:

	Predetermined Rates	Adjustable Rates	Total
	(In thousands)		
Real estate mortgage	$132,057	$455,713	$587,770
Commercial	15,144	34,910	50,054
Consumer	17,804	18,718	36,522
Total gross loans	$165,005	$509,341	$674,346

Asset Quality

The Corporation's principal earning asset is its loan portfolio. Inherent in the lending function is the risk of deterioration in a borrower's ability to repay loans under existing loan agreements. The Corporation manages this risk by maintaining reserves to absorb probable incurred loan losses. In determining the adequacy of the allowance for loan losses, management considers the risks inherent in its loan portfolio and changes in the nature and volume of its loan activities, along with general economic and real estate market conditions. Although management endeavors to establish a reserve sufficient to offset probable incurred losses in the portfolio, changes in economic conditions, regulatory policies and borrower's performance could require future changes to the allowance.

In establishing the allowance for loan losses, the Corporation utilizes a two-tiered approach by (1) identifying problem loans and allocating specific loss allowances to such loans and (2) establishing a general loan loss allowance on the remainder of its loan portfolio. The Corporation maintains a loan review system that allows for a periodic review of its loan portfolio and the early identification of potential problem loans. Such a system takes into consideration, among other things, delinquency status, size of loans, type of collateral and financial condition of the borrowers.

Allocations of specific loan loss allowances are established for identified loans based on a review of various information including appraisals of underlying collateral. Appraisals are performed by independent licensed appraisers to determine the value of impaired, collateral-dependent loans. Appraisals are periodically updated to ascertain any further decline in value. General loan loss allowances are based upon a combination of factors including, but not limited to, actual loss experience, composition of the loan portfolio, current economic conditions and management's judgment.

Management continually reviews and makes enhancements, as appropriate, to its process over measuring the general portion of the allowance for loan losses. In connection with its periodic risk assessment and monitoring process, the Corporation evaluates a number of assumptions supporting the methodology, including the look-back period used to evaluate the historical loss factors for its portfolios, as well as performing a study of its loss emergence period data. Given these evaluations, management reassesses its qualitative and environmental factors to align with the model assumptions. These reviews had no material impact on the overall allowance.

The Corporation's accounting policies are set forth in Note 1 to the Corporation's Audited Consolidated Financial Statements. The application of some of these policies requires significant management judgment and the utilization of estimates. Actual results could differ from these judgments and estimates resulting in a significant impact on the financial statements. A critical accounting policy for the Corporation is the policy utilized in determining the adequacy of the allowance for loan losses. Although management uses the best information available, the level of the allowance for loan losses remains an estimate which is subject to significant judgment and changes. Various regulatory agencies, as an integral part of their examination process, periodically review the Corporation's allowance for loan losses. Such agencies may require the Corporation to make additional provisions for loan losses based upon information available to them at the time of their examination. Furthermore, the Corporation's lending activities are concentrated in loans secured by real estate located in northern New Jersey. Accordingly, the collectability of a substantial portion of the Corporation's loan portfolio is susceptible to changes in real estate market conditions in northern New Jersey. Future adjustments to the allowance may be necessary due to economic, operating, regulatory, and other conditions beyond the Corporation's control. In management's opinion, the allowance for loan losses totaling $7.9 million is adequate to cover probable incurred losses inherent in the portfolio at December 31, 2018.

Nonperforming Assets

Risk elements include nonaccrual loans, past due and restructured loans, potential problem loans, loan concentrations and other real estate owned (i.e., property acquired through foreclosure or deed in lieu of foreclosure). The Corporation's loans are generally placed on a nonaccrual status when they become past due in excess of 90 days as to payment of principal and interest or earlier if collection of principal or interest is considered doubtful. Interest previously accrued on these loans and not yet paid is reversed against income during the current period. Interest earned thereafter may only be included in income to the extent that it is received in cash. Loans past due 90 days or more and accruing represent those loans which are in the process of collection, adequately collateralized and management believes all interest and principal owed will be collected. Restructured loans are loans that have been renegotiated to permit a borrower, who has incurred adverse financial circumstances, to continue to perform. Management can make concessions to the terms of the loan or reduce the contractual interest rates to below market rates in order for the borrower to continue to make payments.

The following table sets forth certain information regarding the Corporation's nonperforming assets as of December 31 of each of the preceding five years:

	December 31,				
	2018	2017	2016	2015	2014
	(Dollars in thousands)				
Nonaccrual loans (1):					
Residential real estate	$576	$295	$—	$—	$96
Commercial real estate	574	701	528	484	1,284
Commercial	394	136	—	1,314	1,923
Consumer	—	62	78	84	325
Total nonaccrual loans	1,544	1,194	606	1,882	3,628
Total nonperforming loans	1,544	1,194	606	1,882	3,628
Other real estate owned	—	—	401	880	1,308
Total nonperforming assets (2)	$1,544	$1,194	$1,007	$2,762	$4,936
Allowance for loan losses	$7,926	$8,762	$7,905	$8,823	$9,602
Nonperforming loans to total gross loans	0.21 %	0.17 %	0.10 %	0.36 %	0.76 %
Nonperforming assets to total assets	0.16 %	0.13 %	0.13 %	0.38 %	0.71 %
Allowance for loan losses to total gross loans	1.08 %	1.23 %	1.31 %	1.68 %	2.01 %

(1) Restructured loans classified in the nonaccrual category totaled $509,000, $610,000, $528,000, $552,000, and $824,000 for the years ended December 31, 2018, 2017, 2016, 2015, and 2014, respectively.
(2) There were no loans past due ninety days or more and accruing for any years presented.

A loan is generally placed on nonaccrual when, based on current information and events, it is probable that the Corporation will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. The identification of nonaccrual loans reflects careful monitoring of the loan portfolio. The Corporation is focused on resolving nonperforming loans and mitigating future losses in the portfolio. All delinquent loans continue to be reviewed by management.

At December 31, 2018, the balance of nonaccrual loans were comprised of two residential real estate loans, two commercial real estate loans and two commercial loans. During the year ended December 31, 2018, nonaccrual loans have increased $350,000 to $1,544,000. The increase reflects the addition of two loans to nonaccrual status partially offset by the payoff of two nonaccrual loans, one charge-off, one loan returning to accruing status and principal payments received.

Evaluation of all nonperforming loans includes the updating of appraisals and specific evaluation of such loans to determine estimated cash flows from business and/or collateral. We have assessed these loans for collectability and considered, among other things, the borrower's ability to repay, the value of the underlying collateral, and other market conditions to ensure the allowance for loan losses is adequate to absorb probable losses to be incurred. All of our nonperforming loans at December 31, 2018 are secured by real estate collateral. We have continued to record appropriate charge-offs and the existing underlying collateral coverage for the nonperforming loans currently supports the collection of our remaining principal.

For loans not included in nonperforming loans, at December 31, 2018, the level of loans past due 30-89 days increased to $2,251,000 from $704,000 at December 31, 2017, primarily due to one loan which was brought current in January 2019. We will continue to monitor delinquencies for early identification of new problem loans.

The Corporation maintains an allowance for loan losses at a level considered by management to be adequate to cover the probable losses to be incurred associated with its loan portfolio. The Corporation's policy with respect to the methodology for the determination of the allowance for loan losses involves a high degree of complexity and requires management to make difficult and subjective judgments.

The adequacy of the allowance for loan losses is based upon management's evaluation of the known and inherent risks in the portfolio, consideration of the size and composition of the loan portfolio, actual loan loss experience, the level of delinquencies, detailed analysis of individual loans for which full collectability may not be assured, the existence and estimated net realizable value of any underlying collateral and guarantees securing the loans, and current economic and market conditions.

The allowance for loan losses contains an unallocated reserve amount to cover inherent imprecision of the overall loss estimation process. Due to the complexity in determining the estimated amount of allowance for loan losses, these unallocated reserves reflect management's attempt to ensure that the overall allowance reflects an appropriate level of reserves. The Corporation continues to refine and enhance, as appropriate, its assessment of the adequacy of the allowance by reviewing the look-back periods, updating the loss emergence periods, and enhancing the analysis of qualitative factors. These refinements have increased the level of precision in the allowance and the unallocated portion has declined. During the year ended December 31, 2018, the Corporation increased its unallocated allowance for loan losses by $4,000 to $11,000. Management believes that the increase in unallocated reserves at December 31, 2018 is appropriate as, in addition to the above discussion, the Corporation has demonstrated a sustained level of performance in the loan portfolio.

For the year ended December 31, 2018, a negative provision for loan loss was recorded in the amount of $1.6 million compared to a provision for loan loss of $655,000 for the year ended December 31, 2017. The total allowance for loan losses of $7.9 million represented 1.08% of total gross loans at December 31, 2018 compared to $8.8 million, or a ratio of 1.23%, at December 31, 2017.

At December 31, 2018 and 2017, the Corporation had $6.3 million and $6.6 million, respectively, of loans whose terms have been modified in troubled debt restructurings. Of these loans, $5.7 million and $5.9 million had demonstrated a reasonable period of performance in accordance with their new terms at December 31, 2018 and 2017, respectively, and not included in the preceding table. The remaining troubled debt restructurings are reported as nonaccrual loans. Specific reserves of $649,000 and $582,000 have been allocated for the troubled debt restructurings at December 31, 2018 and 2017, respectively. As of December 31, 2018 and 2017, the Corporation had no additional funds committed to these borrowers. The balance in performing restructured loans also includes loans that are current under their restructured terms, but because of the below market rate of interest and other forbearance agreements, continue to be reflected as restructured loans and impaired loans in accordance with accounting practices. For the year ended December 31, 2018, gross interest income which would have been recorded had the restructured and non-accruing loans been current in accordance with their original terms amounted to $345,000, of which $292,000 was included in interest income for the year ended December 31, 2018.

When management expects that some portion or all of a loan balance will not be collected, that amount is charged-off as a loss against the allowance for loan losses. The net charge-offs reflect partial or full charge-offs on nonaccrual loans due to the initial and ongoing evaluations of market values of the underlying real estate collateral in accordance with Accounting Standards Codification ("ASC") 310-40. While regular monthly payments continue to be made on many of the nonaccrual loans, certain charge-offs result, nevertheless, from the borrowers' inability to provide adequate documentation evidencing their ability to continue to service their debt. Management believes the charge-off of these loan balances against reserves provides a clearer indication of the recoverable value of nonaccrual loans. Regardless of our actions of recording partial and full charge-offs on loans, we continue to aggressively pursue collection, including legal action.

As of December 31, 2018 and 2017, there were $10.8 and $12.1 million, respectively, of other loans not included in the preceding table or discussion of troubled debt restructurings, where credit conditions of borrowers, including real estate tax delinquencies, caused management to have concerns about the possibility of the borrowers not complying with the present terms and conditions of repayment and which may result in disclosure of such loans as nonperforming loans at a future date. Management continues to monitor performance and credit conditions.

The following table sets forth, for each of the preceding five years, the historical relationships among the amount of loans outstanding, the allowance for loan losses, the provision for loan losses, the amount of loans charged-off and the amount of loan recoveries:

	December 31, 2018	2017	2016	2015	2014
	(Dollars in thousands)				
Allowance for loan losses:					
Balance at beginning of period	$8,762	$7,905	$8,823	$9,602	$9,915
Loans charged-off:					
Residential real estate	—	—	—	—	7
Commercial real estate	—	—	96	—	1,110
Commercial	29	3	72	600	262
Consumer and other	2	1	14	2	6
Total loans charged-off	31	4	182	602	1,385
Recoveries of loans previously charged-off:					
Construction	—	—	—	552	48
Residential real estate	—	—	—	26	—
Commercial real estate	665	100	162	151	858
Commercial	142	97	446	465	216
Consumer and other	3	9	6	4	—
Total recoveries of loans previously charged-off	810	206	614	1,198	1,122
Net loans charged-off (recovered)	(779)	(202)	(432)	(596)	263
Provisions charged (credited) to operations	(1,615)	655	(1,350)	(1,375)	(50)
Balance at end of period	$7,926	$8,762	$7,905	$8,823	$9,602
Net charge-offs (recoveries) during the period to average loans outstanding during the period	(0.11)%	(0.03)%	(0.08)%	(0.12)%	0.06 %
Balance of allowance for loan losses at the end of year to gross year end loans	1.08 %	1.23 %	1.31 %	1.68 %	2.01 %

The following table sets forth the allocation of the allowance for loan losses, for each of the preceding five years, as indicated by loan categories:

	2018		2017		2016		2015		2014	
	Amount	Percent to Total (1)	Amount	Percent to Total (1)	Amount	Percent to Total (1)	Amount	Percent to Total (1)	Amount	Percent to Total (1)
	(Dollars in thousands)									
Real estate - residential	$65	11.2 %	$68	12.1 %	$66	14.0 %	$109	15.8 %	$142	16.3 %
Real estate - commercial	5,078	71.0 %	5,564	70.8 %	5,089	67.4 %	4,774	66.2 %	5,167	61.9 %
Commercial	2,703	12.8 %	3,058	12.5 %	2,663	13.6 %	3,698	12.3 %	3,704	15.9 %
Consumer	69	5.0 %	65	4.6 %	75	5.0 %	121	5.7 %	191	5.9 %
Unallocated	11	— %	7	— %	12	— %	121	— %	398	— %
Total allowance for loan losses	$7,926	100.0%	$8,762	100.0%	$7,905	100.0%	$8,823	100.0%	$9,602	100.0%

(1) Represents percentage of loan balance in category to total gross loans.

Investment Portfolio

The Corporation maintains an investment portfolio to enhance its yields and to provide a secondary source of liquidity. The portfolio is currently comprised of U.S. Treasury, U.S. government and agency obligations, state and political subdivision obligations, mortgage-backed securities, asset-backed securities and corporate debt securities, and has been classified as held-to-maturity or available-for-sale. Investments in debt securities that the Corporation has the intention and the ability to hold to maturity are classified as held-to-maturity securities and reported at amortized cost. All other securities are classified as available-for-sale securities and reported at fair value, with unrealized gains or losses reported in a separate component of shareholders' equity. Securities in the available-for-sale category may be held for indefinite periods of time and include securities that management intends to use as part of its Asset/Liability strategy or that may be sold in response to changes in interest rates, changes in prepayment risks, the need to provide liquidity, the need to increase regulatory capital or similar factors. Securities available-for-sale decreased to $108.8 million at December 31, 2018, from $109.3 million at December 31, 2017, a decrease of $0.5 million, or 0.4%. Securities held-to-maturity increased $9.9 million, or 18.8%, to $62.3 million at December 31, 2018 from $52.4 million at December 31, 2017.

The following table sets forth the classification of the Corporation's investment securities by major category at the end of the last three years:

	December 31,					
	2018		2017		2016	
	Carrying Value	Percent	Carrying Value	Percent	Carrying Value	Percent
	(Dollars in thousands)					
Securities available-for-sale:						
U.S. government-sponsored agencies	$25,749	23.7 %	$21,333	19.5 %	$17,445	18.4 %
Obligation of state and political subdivisions	3,121	2.9 %	3,165	2.9 %	3,096	3.3 %
Mortgage-backed securities	62,163	57.1 %	63,834	58.5 %	52,046	54.8 %
Asset-backed securities (a)	4,922	4.5 %	6,698	6.1 %	8,267	8.7 %
Corporate debt (b)	12,856	11.8 %	14,229	13.0 %	14,037	14.8 %
Total	$108,811	100.0%	$109,259	100.0%	$94,891	100.0%
Securities held-to-maturity:						
U.S. Treasury	$999	1.6 %	$999	1.9 %	$999	1.9 %
U.S. government-sponsored agencies	35,565	57.1 %	27,075	51.6 %	19,162	36.6 %
Obligations of state and political subdivisions	2,358	3.8 %	4,057	7.8 %	7,102	13.6 %
Mortgage-backed securities	23,386	37.5 %	20,311	38.7 %	25,067	47.9 %
Total	$62,308	100.0%	$52,442	100.0%	$52,330	100.0%

(a) Collateralized by student loans.
(b) Corporate debt securities are primarily in financial institutions.

The following table sets forth the maturity distribution and weighted average yields (calculated on the basis of stated yields to maturity, considering applicable premium or discount) of the Corporation's debt securities available-for-sale as of December 31, 2018. Issuers may have the right to call or prepay obligations with or without call or prepayment penalties. This might cause actual maturities to differ from contractual maturities. Non-debt securities and securities not due at a single maturity date, such as mortgage-backed securities and asset-backed securities, are not reflected in the table below.

	Within 1 Year	After 1 Year Through 5 Years	After 5 Years Through 10 Years	After 10 Years	Total
	(Dollars in thousands)				
U.S. government-sponsored agencies:					
Amortized cost	$1,147	$9,387	$11,631	$4,067	$26,232
Yield	1.37 %	2.41 %	3.04 %	1.96 %	2.58 %
Obligations of state and political subdivisions:					
Amortized cost	396	985	1,524	300	3,205
Yield	1.35 %	1.79 %	1.68 %	2.75 %	1.77 %
Corporate debt:					
Amortized cost	—	2,546	10,823	—	13,369
Yield	0.00 %	2.73 %	3.60 %	0.00 %	3.44 %
Total amortized cost	$1,543	$12,918	$23,978	$4,367	$42,806
Weighted average yield	1.36 %	2.43 %	3.21 %	2.01 %	2.79 %

The following table sets forth the maturity distribution and weighted average yields (calculated on the basis of stated yields to maturity, considering applicable premium or discount) of the Corporation's debt securities held-to-maturity as of December 31, 2018. Issuers may have the right to call or prepay obligations with or without call or prepayment penalties. This might cause actual maturities to differ from contractual maturities.

	Within 1 Year	After 1 Year Through 5 Years	After 5 Years Through 10 Years	After 10 Years	Total
	(Dollars in thousands)				
U.S. Treasury:					
Carrying value	$—	$999	$—	$—	$999
Yield	0.00 %	1.41 %	0.00 %	0.00 %	1.41 %
U.S. government-sponsored agencies:					
Carrying value	—	15,498	20,067	—	35,565
Yield	0.00 %	2.26 %	2.62 %	0.00 %	2.46 %
Obligations of state and political subdivisions:					
Carrying value	335	1,535	—	488	2,358
Yield	3.71 %	4.01 %	0.00 %	1.70 %	3.49 %
Total carrying value	$335	$18,032	$20,067	$488	$38,922
Weighted average yield	3.71 %	2.36 %	2.62 %	1.70 %	2.50 %

Deposits

The Corporation had deposits at December 31, 2018 totaling $782.1 million, an increase of $18.0 million, or 2.4%, over the comparable period of 2017, when deposits totaled $764.1 million. The Corporation relied on its branch network and current competitive products and services to grow deposits during 2018. Included in deposit balances were $37.1 million of brokered certificates of deposit at December 31, 2018 compared to $25.9 million at

December 31, 2017.

The following table sets forth the classification of the Corporation's deposits by major category as of December 31 of each of the three preceding years:

	December 31,					
	2018		2017		2016	
	Amount	Percent	Amount	Percent	Amount	Percent
	(Dollars in thousands)					
Non-interest bearing demand	$174,717	22.3 %	$172,861	22.6 %	$169,306	25.7 %
Interest-bearing demand	325,151	41.6 %	307,180	40.2 %	242,278	36.8 %
Savings deposits	76,745	9.8 %	83,114	10.9 %	90,677	13.7 %
Certificates of deposit	205,478	26.3 %	200,944	26.3 %	156,669	23.8 %
Total	$782,091	100.0%	$764,099	100.0%	$658,930	100.0%

As of December 31, 2018, the aggregate amount of outstanding time deposits issued in amounts of $100,000 or more, broken down by time remaining to maturity, was as follows:

	Balances (In thousands)
Three months or less	$ 20,843
Four months through six months	34,691
Seven months through twelve months	16,701
Over twelve months	41,236
	$ 113,471

Borrowings

Although deposits with the Bank are the Corporation's primary source of funds, the Corporation's policy has been to utilize borrowings to the extent that they are a less costly source of funds, when the Corporation desires additional capacity to fund loan demand, or to extend the life of its liabilities as a means of managing exposure to interest rate risk. The Corporation's borrowings are a combination of advances from the Federal Home Loan Bank of New York ("FHLB-NY"), including overnight repricing lines of credit and, to a lesser extent, securities sold under agreements to repurchase.

Interest Rate Sensitivity

Interest rate movements have made managing the Corporation's interest rate sensitivity increasingly important. The Corporation attempts to maintain stable net interest margins by generally matching the volume of interest-earning assets and interest-bearing liabilities maturing, or subject to repricing, by adjusting interest rates to market conditions, and by developing new products. One method of measuring the Corporation's exposure to changes in interest rates is the maturity and repricing gap analysis. The difference or mismatch between the amount of assets and liabilities that mature or reprice in a given period is defined as the interest rate sensitivity gap. A "negative" gap results when the amount of interest-bearing liabilities maturing or repricing within a specified time period exceeds the amount of interest-earning assets maturing or repricing within the same period of time. Conversely, a "positive" gap results when the amount of interest-earning assets maturing or repricing exceed the amount of interest-bearing liabilities maturing or repricing in the same given time frame. The smaller the gap, the less the effect of the market volatility on net interest income. During a period of rising interest rates, an institution with a negative gap position would not be in as favorable a position, as compared to an institution with a positive gap, to invest in higher yielding assets. This may result in yields on its assets increasing at a slower rate than the increase in its costs of interest-bearing liabilities than if it had a positive gap. During a period of falling interest rates, an institution with a negative gap would experience a repricing of its assets at a slower rate than its interest-bearing liabilities, which consequently may result in its net interest income growing at a faster rate than an institution with a positive gap position.

The following table sets forth estimated maturity/repricing structure of the Corporation’s interest-earning assets and interest-bearing liabilities as of December 31, 2018. The amounts of assets or liabilities shown which reprice or mature during a particular period were determined in accordance with the contractual terms of each asset or liability and adjusted for prepayment assumptions where applicable. The table does not necessarily indicate the impact of general interest rate movements on the Corporation’s net interest income because the repricing of certain categories of assets and liabilities, for example, prepayments of loans and withdrawal of deposits, is beyond the Corporation’s control. As a result, certain assets and liabilities indicated as repricing within a period may in fact reprice at different times and at different rate levels.

	Three Months or Less	More than Three Months Through One Year	After One Year	Noninterest Sensitive	Total
	(In thousands)				
Assets:					
Loans:					
Real estate Mortgage	$37,992	$61,791	$503,576	$—	$603,359
Commercial	58,727	7,521	27,507	—	93,755
Consumer	12,026	2,154	22,493	—	36,673
Investment securities (1)	22,711	23,188	130,833	—	176,732
Other assets	483	—	—	44,628	45,111
Total assets	$131,939	$94,654	$684,409	$44,628	$955,630
Source of funds:					
Interest-bearing demand	$325,151	$—	$—	$—	$325,151
Savings	76,745	—	—	—	76,745
Certificates of deposit	34,293	81,254	89,931	—	205,478
FHLB-NY advances	12,700	33,000	20,000	—	65,700
Subordinated Debentures	—	—	23,382	—	23,382
Other liabilities (including non-interest bearing deposits)	—	—	—	179,024	179,024
Shareholders' equity	—	—	—	80,150	80,150
Total source of funds	$448,889	$114,254	$133,313	$259,174	$955,630
Interest rate sensitivity gap	$(316,950)	$(19,600)	$551,096	$(214,546)	
Cumulative interest rate sensitivity gap	$(316,950)	$(336,550)	$214,546	$—	

(1) Includes securities held-to-maturity, securities available-for sale,other equity investments and FHLB-NY Stock.

The Corporation also uses a simulation model to analyze the sensitivity of net interest income to movements in interest rates. The simulation model projects net interest income, net income, net interest margin, and capital to asset ratios based on various interest rate scenarios over a twelve-month period. The model is based on the actual maturity and repricing characteristics of all rate sensitive assets and liabilities. Management incorporates into the model certain assumptions regarding prepayments of certain assets and liabilities. Assumptions have been built into the model for prepayments for assets and decay rates for nonmaturity deposits such as savings and interest bearing demand. The model assumes an immediate rate shock to interest rates without management’s ability to proactively change the mix of assets or liabilities. Based on the reports generated for December 31, 2018, an immediate interest rate increase of 200 basis points would have resulted in a decrease in net interest income of 10.9%, or $3.3 million, and an immediate interest rate decrease of 200 basis points would have resulted in a decrease in net interest income of 1.3% or $387,000.

Management cannot provide any assurance about the actual effect of changes in interest rates on the Corporation’s net interest income.

Liquidity

The Corporation's primary sources of funds are deposits, amortization and prepayments of loans and mortgage-backed securities, maturities of investment securities and funds provided by operations. While scheduled loan and mortgage-backed securities amortization and maturities of investment securities are a relatively predictable source of funds, deposit flow and prepayments on loans and mortgage-backed securities are greatly influenced by market interest rates, economic conditions, and competition.

The Corporation's liquidity, represented by cash and cash equivalents, is a product of its operating, investing and financing activities. These activities are summarized below:

	Years Ended December 31,	
	2018	2017
	(In thousands)	
Cash and cash equivalents - beginning	$21,270	$11,680
Operating activities:		
Net income	8,030	3,947
Adjustments to reconcile net income to net cash provided by (used in) operating activities	(598)	4,583
Net cash provided by operating activities	7,432	8,530
Net cash used in investing activities	(30,884)	(126,730)
Net cash provided by financing activities	19,005	127,790
Net increase (decrease) in cash and cash equivalents	(4,447)	9,590
Cash and cash equivalents - ending	$16,823	$21,270

Cash was generated by operating activities in each of the above periods. The primary source of cash from operating activities during each period was operating income. Net cash provided by financing activities at December 31, 2017 included proceeds from the issuance of common stock.

On April 17, 2017, the Corporation closed an underwritten public offering of 2,509,090 shares of the Corporation's common stock, which included 327,272 shares issued pursuant to the full exercise of the underwriter's over-allotment option, at a price to the public of $8.25 per share, for aggregate gross proceeds of $20.7 million. The net proceeds to the Corporation, after deducting the underwriting discount and offering expenses, were $18.9 million. The Corporation is using the net proceeds of the offering to support organic growth and other general corporate purposes.

Liquidity management is both a daily and long-term function of business management. Excess liquidity is generally invested in short-term investments, such as federal funds sold.

The Corporation enters into commitments to extend credit, such as letters of credit, which are not reflected in the Corporation's Audited Consolidated Statements of Financial Condition.

The Corporation has various contractual obligations that may require future cash payments. The following table summarizes the Corporation’s contractual obligations at December 31, 2018 and the effect such obligations are expected to have on our liquidity and cash flows in future periods.

		Payment Due By Period			
	Total	Less than 1 Year	1 - 3 Years	3 - 5 Years	After 5 Years
	(In thousands)				
Contractual obligations					
Operating lease obligations	$3,357	$718	$1,140	$833	$666
Total contracted cost obligations	$3,357	$718	$1,140	$833	$666
Other long-term liabilities/long-term debt					
Time deposits	$205,478	$115,418	$80,394	$9,666	$—
Federal Home Loan Bank advances (1)	68,049	46,084	10,360	11,605	—
Subordinated Debentures (1)	13,316	414	829	829	11,244
Subordinated Notes (1)	23,439	1,091	2,182	2,182	17,984
Supplemental Executive Retirement Plan	1,853	53	114	114	1,572
Total other long-term liabilities/long-term debt	$312,135	$163,060	$93,879	$24,396	$30,800
Other commitments - off balance sheet					
Letters of credit	$2,514	$2,368	$—	$146	$—
Commitments to extend credit	8,037	8,037	—	—	—
Unused lines of credit	124,738	124,738	—	—	—
Total off balance sheet arrangements and contractual obligations	$135,289	$135,143	$—	$146	$—

(1) Includes interest contractually due.

Management believes that a significant portion of the time deposits will remain with the Corporation. In addition, management does not believe that all of the unused lines of credit will be exercised. We anticipate that the Corporation will have sufficient funds available to meet its current contractual commitments. Should we need temporary funding, the Corporation has the ability to borrow overnight with the FHLB-NY. The overall borrowing capacity is contingent on available collateral to secure borrowings and the ability to purchase additional activity-based capital stock of the FHLB-NY. The Corporation may also borrow from the Discount Window of the Federal Reserve Bank of New York based on the market value of collateral pledged. At December 31, 2018 and 2017, the borrowing capacity at the Discount Window was $3.3 million and $4.7 million, respectively. In addition, the Corporation had available overnight variable repricing lines of credit with other correspondent banks totaling $38 million on an unsecured basis. There were no borrowings under these lines of credit at December 31, 2018 and 2017.

The Corporation's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit and standby letters of credit is represented by the contractual notional amount of those instruments. The Corporation uses the same credit policies in making commitments and conditional obligations as it does for on-balance sheet instruments.

Of the $2.5 million in commitments under standby and commercial letters of credit, approximately $2.4 million expire within one year. Should any letter of credit be drawn on, the interest rate charged on the resulting note would fluctuate with the Corporation's base rate. Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments may expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The

Corporation evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Corporation upon extension of credit, is based on management's credit evaluation of the counter-

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party. Collateral held varies, but may include accounts receivable, inventory, property, plant and equipment, and income-producing commercial properties.

Standby and commercial letters of credit are irrevocable conditional commitments issued by the Corporation to guarantee payment or performance of a customer to a third party. Those guarantees are primarily issued to support public and private borrowing arrangements, including commercial paper, bond financing and similar transactions. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. The Corporation obtains collateral supporting those commitments for which collateral is deemed necessary.

At December 31, 2018, the Corporation had no residential mortgage commitments to extend credit. Commercial, construction, and home equity loan commitments of approximately $7.3 million were extended with variable rates averaging 5.43% and approximately $780,000 extended at fixed rates averaging 4.36%. Generally, commitments were due to expire within approximately 90 days.

The unused lines of credit consist of $31.8 million relating to a home equity line of credit program and an unsecured line of credit program, $3.9 million relating to an unsecured overdraft protection program, and $89.0 million relating to commercial and construction lines of credit. Amounts drawn on the unused lines of credit are predominantly assessed interest at rates which fluctuate with the base rate.

Capital
Capital Adequacy

The Corporation is subject to capital adequacy guidelines promulgated by the FRB. The Bank is subject to somewhat comparable but different capital adequacy requirements imposed by the FDIC. The federal banking agencies have adopted risk-based capital guidelines for banks and bank holding companies. The risk-based capital guidelines are designed to make regulatory capital requirements more sensitive to differences in risk profiles among banks and bank holding companies, to account for off-balance sheet exposure, and to minimize disincentives for holding liquid assets. Under these guidelines, assets and off-balance sheet items are assigned to broad risk categories, each with appropriate weights. The resulting capital ratios represent capital as a percentage of total risk-weighted assets and off-balance sheet items.

Federal banking regulators have also adopted leverage capital guidelines to supplement the risk-based measures. Leverage capital to average total assets is determined by dividing Tier 1 Capital as defined under the risk-based capital guidelines by average total assets (non-risk adjusted).

Guidelines for Banks

In December 2010 and January 2011, the Basel Committee published the final texts of reforms on capital and liquidity, which are generally referred to as “Basel III”. The Basel Committee is a committee of central banks and bank supervisors and regulators from the major industrialized countries that develops broad policy guidelines for the regulation of banks and bank holding companies. In July 2013, the FDIC and the other federal bank regulatory agencies adopted final rules (the “Basel Rules”) to implement certain provisions of Basel III and the Dodd-Frank Wall Street Reform and Consumer Protection Act. The Basel Rules revised the leverage and risk-based capital requirements and the methods for calculating risk-weighted assets. The Basel Rules apply to all depository institutions, top-tier bank holding companies with total consolidated assets of $1 billion or more and top-tier savings and loan holding companies.

Among other things, the Basel Rules (a) established a CET1 to risk-weighted assets ratio minimum of 4.5% of risk-weighted assets, (b) raised the minimum Tier 1 Capital to risk-based assets requirement (“Tier 1 Capital Ratio) from 4% to 6% of risk-weighted assets and (c) assigned a higher risk weight of 150% to exposures that are more than 90 days past due or are on nonaccrual status and to certain commercial real estate facilities. The minimum ratio of Total Capital to risk-weighted assets (including certain off-balance sheet activities, such as standby letters of credit) is 8%. At least 6% of the Total Capital is required to be “Tier 1 Capital”, which consists of common shareholders’ equity and certain preferred stock, less certain items and other intangible assets. The remainder, “Tier 2 Capital,” may consist of (a) the allowance for loan losses of up to 1.25% of risk-weighted assets, (b) excess of qualifying preferred stock, (c) hybrid capital instruments, (d) debt, (e) mandatory convertible securities and (f) qualifying subordinated debt. “Total Capital” is the sum of Tier 1 Capital and Tier 2 Capital less reciprocal holdings of other banking organizations’ capital instruments, investments in unconsolidated subsidiaries and any other deductions as determined by the federal banking regulatory agencies on a case-by-case basis or as a matter of policy after formal rule-making. A small bank holding company that has the highest regulatory examination rating and is not contemplating significant growth or expansion must maintain a minimum level of Tier 1 Capital to average total consolidated assets leverage ratio of at least 3%. All other bank holding companies are expected to maintain a leverage ratio of at least 100 to 200 basis points above the stated minimum.

The Basel Rules also require unrealized gains and losses on certain available-for-sale securities to be included for purposes of calculating regulatory capital unless a one-time opt-out was exercised. Additional constraints are also imposed on the inclusion in regulatory capital of mortgage-servicing assets and deferred tax assets. The Basel Rules limit a banking organization’s capital distributions and certain discretionary bonus payments if the banking organization does not hold a “capital conservation buffer” consisting of 2.5% of CET1 to risk-weighted assets in addition to the amount necessary to meet a minimum risk-based capital requirement. The purpose of the capital conservation buffer is to ensure that banking organizations conserve capital when it is needed most, allowing them to weather periods of economic stress. Banking institutions with a CET1 Ratio, Tier 1 Capital Ratio or Total Capital Ratio above the minimum capital ratios but below the minimum capital ratios plus the capital conservation buffer will face constraints on their ability to pay dividends, repurchase equity and pay discretionary bonuses to executive officers based on the amount of the shortfall. The Basel Rules became effective for the Bank on January 1, 2015. The capital conservation buffer requirement of 0.625% became effective January 1, 2016 and was phased in annually through January 1, 2019, when the full capital conservation buffer requirement of 2.50% became effective. At December 31, 2018, the Bank's capital conservation buffer requirement was 1.875%, and the actual capital conservation buffer was 5.54%.

Bank assets are given risk-weights of 0%, 20%, 50%, 100%, and 150%. In addition, certain off-balance sheet items are given similar credit conversion factors to convert them to asset equivalent amounts to which an appropriate risk-weight will apply. These computations result in the total risk-weighted assets. Most loans are assigned to the 100% risk category, except for performing first mortgage loans fully secured by residential property which carry a 50% risk-weighting. Loan exposures past due 90 days or more or on nonaccrual are assigned a risk-weighting of at least 100%. High volatility commercial real estate ("HVCRE") loan exposures are assigned to the 150% category; provided, however, Section 214 of the Economic Growth Act, prohibits federal banking agencies from requiring the financial institution to assign heightened risk weights to HVCRE loans unless the loan is related to real estate acquisition, development and construction (“HVCRE ADC”). Under the Basel III capital rules, HVCRE ADC loans are assigned a higher risk weight than other commercial real estate loans. Most investment securities (including, primarily, general obligation claims of states or other political subdivisions of the United States) are assigned to the 20% category, except for municipal or state revenue bonds, which have a 50% risk-weight, and direct obligations of the U.S. Treasury or obligations backed by the full faith and credit of the U.S. government, which have a 0% risk-weight. In converting off-balance sheet items, direct credit substitutes, including general guarantees and standby letters of credit backing nonfinancial obligations, and undrawn commitments (including commercial credit lines with an initial maturity of more than one year) have a 50% risk-weighting. Short-term undrawn commitments and commercial letters of credit with an initial maturity of under one year have a 50% risk-weighting and certain short-term unconditionally cancelable commitments are not risk-weighted.

Community Bank Leverage Ratio

The recently enacted Economic Growth Act requires federal banking agencies to develop a “community bank leverage ratio” (the ratio of a bank’s tangible equity capital to average total consolidated assets) for financial institutions with assets of less than $10 billion. A “qualifying community bank” that exceeds this ratio will be deemed to be in compliance with all other capital and leverage requirements, including the capital requirements to be considered “well capitalized" under prompt corrective action rules. The federal banking agencies may consider an institution's risk profile when evaluating whether it qualifies as a community bank for purposes of the capital ratio requirement. The minimum capital for the new community bank leverage ratio must be set at not less than 8% and not more than 10%. A financial institution can elect to be subject to this new definition. The Economic Growth Act requires the federal banking agencies to consult with state banking regulators and notify the applicable state banking regulator of any qualifying community bank that exceeds or no longer exceeds the Community Bank Leverage Ratio.

Guidelines for Small Bank Holding Companies

The Dodd-Frank Act required the FRB to establish for all bank and savings and loan holding companies minimum consolidated capital requirements that are as stringent as those required for the insured depository subsidiaries. The FRB has updated and amended its Small Bank Holding Company Policy Statement to extend to bank and savings and loan holding companies the applicability of the "Small Bank Holding Company" exception to its consolidated capital requirements and, as a result of the Economic Growth Act, increased the threshold for the exception from $1.0 billion in consolidated assets to $3.0 billion in consolidated assets. As a result of the revised Small Bank Holding Company Policy Statement, Basel III capital rules and reporting requirements do not apply to small bank holding companies ("SBHC"), such as the Corporation, that have total consolidated assets of less than $3 billion unless otherwise advised by the FRB. The minimum risk-based capital requirements for a SBHC to be considered adequately capitalized are 4% for Tier 1 Capital and 8% for Total Capital to risk-weighted assets.

The regulations for SBHCs classify risk-based capital into two categories: "Tier 1 Capital" which consists of common and qualifying perpetual preferred shareholders' equity less goodwill and other intangibles and "Tier 2 Capital" which consists of (a) the allowance for loan losses of up to 1.25% of risk-weighted assets, (b) the excess of qualifying preferred stock, (c) hybrid capital instruments, (d) debt, (e) mandatory convertible securities and (f) qualifying subordinated debt. Total qualifying capital consists of Tier 1 Capital and Tier 2 Capital less reciprocal holdings of other banking organizations' capital instruments, investments in unconsolidated subsidiaries and any other deductions as determined by the FRB on a case-by-case basis or as a matter of policy after formal rule-making. However, the amount of Tier 2 Capital may not exceed the amount of Tier 1 Capital. The Corporation must maintain a minimum level of Tier 1 Capital to average total consolidated assets leverage ratio of 3%, which is the leverage ratio reserved for top-tier bank holding companies having the highest regulatory examination rating and not contemplating significant growth or expansion.

Bank holding company assets are given risk-weights of 0%, 20%, 50%, and 100%. In addition, certain off-balance sheet items are given similar credit conversion factors to convert them to asset equivalent amounts to which an appropriate risk-weight will apply. These computations result in the total risk-weighted assets.

The following table summarizes the capital ratios for the Corporation and the Bank at December 31, 2018.

	Actual	Required for Capital Adequacy Purposes	To Be Well-Capitalized Under Prompt Corrective Action Regulations
Tier 1 Leverage ratio			
Corporation	9.33 %	4.00 %	N/A
Bank	10.49%	4.00 %	5.00 %
Risk-based capital:			
Common Equity Tier 1			
Corporation	N/A	N/A	N/A
Bank	12.54%	4.50 %	6.50 %
Tier 1			
Corporation	11.33%	4.00 %	N/A
Bank	12.54%	6.00 %	8.00 %
Total			

Corporation	14.39%	8.00 %	N/A
Bank	13.54%	8.00 %	10.00 %

As discussed in further detail in Note 8 to the Audited Consolidated Financial Statements contained in this Annual Report on Form 10-K, on August 28, 2015, the Corporation completed a private placement of Subordinated Notes.

The Subordinated Notes have a maturity date of August 28, 2025 and bear interest at the rate of 6.75% per annum, payable semiannually, over their term. The Subordinated Notes have been structured to qualify as Tier 2 capital for regulatory purposes.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk

Not applicable to smaller reporting companies.

Item 8. Financial Statements and Supplementary Data

Report of Independent Registered Public Accounting Firm

To the Shareholders and Board of Directors
Stewardship Financial Corporation
Midland Park, NJ

Opinion on the Consolidated Financial Statements

We have audited the accompanying consolidated statement of financial condition of Stewardship Financial Corporation and Subsidiary (the "Corporation") as of December 31, 2018, the related consolidated statement of income, comprehensive income, changes in shareholders' equity, and cash flows for the year then ended, and the related notes (collectively referred to as the "consolidated financial statements"). In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Corporation at December 31, 2018, and the results of their operations and their cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) ("PCAOB"), the Corporation's internal control over financial reporting as of December 31, 2018, based on criteria established in Internal Control - Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO") and our report dated March 15, 2019 expressed an unqualified opinion thereon.

Basis for Opinion

These consolidated financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on the Corporation's consolidated financial statements based on our audit. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Corporation in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audit 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 consolidated financial statements are free of material misstatement, whether due to error or fraud.

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

/s/ BDO USA, LLP

We have served as the Corporation's auditor since 2018.

New York, New York
March 15, 2019

Report of Independent Registered Public Accounting Firm

To the Shareholders and Board of Directors
Stewardship Financial Corporation
Midland Park, NJ

Opinion on Internal Control over Financial Reporting

We have audited Stewardship Financial Corporation and Subsidiary’s (the “Corporation’s”) internal control over financial reporting as of December 31, 2018, based on criteria established in Internal Control - Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (the “COSO criteria”). In our opinion, the Corporation maintained, in all material respects, effective internal control over financial reporting as of December 31, 2018, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (“PCAOB”), the consolidated statement of financial condition of the Corporation as of December 31, 2018, the related consolidated statement of income, comprehensive income, changes in shareholders’ equity, and cash flows for the year then ended, and the related notes and our report dated March 15, 2019 expressed an unqualified opinion thereon.

Basis for Opinion

The Corporation’s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Item 9A, Management’s Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Corporation’s internal control over financial reporting based on our audit. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Corporation 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 audit of internal control over financial reporting in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

Definition and Limitations of Internal Control over Financial Reporting

A corporation's internal control over financial reporting is a process 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. A corporation's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the corporation; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the corporation are being made only in accordance with authorizations of management and directors of the corporation; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the corporation's assets that could have a material effect on the financial statements.

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.

/s/ BDO USA, LLP

New York, New York
March 15, 2019

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Report of Independent Registered Public Accounting Firm

To the Shareholders and Board of Directors
Stewardship Financial Corporation:

Opinion on the Consolidated Financial Statements
We have audited the accompanying consolidated statement of financial condition of Stewardship Financial Corporation and Subsidiary (the Corporation) as of December 31, 2017, the related consolidated statements of income, comprehensive income, changes in shareholders' equity, and cash flows for the year then ended, and the related notes (collectively, the consolidated financial statements). In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Corporation as of December 31, 2017, and the results of its operations and its cash flows for the year then ended, in conformity with U.S. generally accepted accounting principles.
Basis for Opinion
These consolidated financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit. 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 Corporation in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.
We conducted our audit 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 consolidated financial statements are free of material misstatement, whether due to error or fraud.
Our audit included performing procedures to assess the risks of material misstatement of the consolidated financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the consolidated financial statements. Our audit also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. We believe that our audit provides a reasonable basis for our opinion.

/s/ KPMG LLP

We served as the Corporation's auditor from 2013 to 2017.
Short Hills, New Jersey
March 23, 2018

Stewardship Financial Corporation and Subsidiary
Consolidated Statements of Financial Condition

	December 31, 2018	2017
	(Dollars in thousands)	
Assets		
Cash and due from banks	$16,340	$20,558
Other short-term interest-earning assets	483	712
Cash and cash equivalents	16,823	21,270
Securities available-for-sale	108,811	109,259
Securities held-to-maturity; estimated fair value of $60,997 (2018) and $51,551 (2017)	62,308	52,442
Other equity investments, at fair value (2018) and available-for-sale (2017)	1,648	3,756
Federal Home Loan Bank of New York stock, at cost	3,965	3,715
Loans held for sale	—	370
Loans, net of allowance for loan losses of $7,926 (2018) and $8,762 (2017)	725,404	702,561
Premises and equipment, net	7,007	6,909
Accrued interest receivable	2,696	2,566
Bank owned life insurance	21,636	21,084
Other assets	5,332	4,834
Total assets	$955,630	$928,766
Liabilities and Shareholders' equity		
Liabilities		
Deposits:		
Noninterest-bearing	$174,717	$172,861
Interest-bearing	607,374	591,238
Total deposits	782,091	764,099
Federal Home Loan Bank of New York advances	65,700	63,760
Subordinated Debentures and Subordinated Notes	23,382	23,317
Accrued interest payable	1,106	1,116
Accrued expenses and other liabilities	3,201	2,809
Total liabilities	875,480	855,101
Shareholders' equity		
Common stock, no par value; 20,000,000 and 20,000,000 shares authorized; 8,680,388 and 8,652,804 shares issued and outstanding at December 31, 2018, and 2017, respectively	61,030	60,742
Retained earnings	21,056	14,307
Accumulated other comprehensive loss, net	(1,936)	(1,384)
Total Shareholders' equity	80,150	73,665
Total liabilities and Shareholders' equity	$955,630	$928,766

See accompanying notes to consolidated financial statements.

Stewardship Financial Corporation and Subsidiary
Consolidated Statements of Income

	Years Ended December 31,	
	2018	2017
	(Dollars in thousands, except per share amounts)	
Interest income:		
Loans	$31,514	$ 28,385
Securities held-to-maturity:		
Taxable	1,247	990
Nontaxable	98	197
Securities available-for-sale:		
Taxable	2,618	2,196
Nontaxable	57	57
Other equity investments	99	96
FHLB dividends	228	203
Other interest-earning assets	138	106
Total interest income	35,999	32,230
Interest expense:		
Deposits	5,293	3,189
FHLB-NY borrowings	968	1,177
Subordinated Debentures and Subordinated Notes	1,575	1,492
Total interest expense	7,836	5,858
Net interest income before provision for loan losses	28,163	26,372
Provision for loan losses	(1,615)	655
Net interest income after provision for loan losses	29,778	25,717
Noninterest income:		
Fees and service charges	2,228	2,111
Bank owned life insurance	552	526
Gain (loss) on calls and sales of securities, net	(186)	1
Gain on sales of mortgage loans	70	178
Gain on sale of other real estate owned	—	13
Gain on sales of SBA loans	193	—
Gain on equity investments	80	—
Miscellaneous	480	478
Total noninterest income	3,417	3,307
Noninterest expenses:		
Salaries and employee benefits	12,636	11,455
Occupancy, net	1,701	1,630
Equipment	746	673
Data processing	1,947	1,811
Advertising	715	700
FDIC insurance premium	277	322
Charitable contributions	910	615
Bank-card related services	533	551

Other real estate owned, net	—	24
Miscellaneous	2,680	2,520
Total noninterest expenses	22,145	20,301
Income before income tax expense	11,050	8,723
Income tax expense	3,020	4,776
Net income	$ 8,030	$ 3,947
Basic and diluted earnings per common share	$ 0.93	$ 0.50
Weighted average number of basic and diluted common shares outstanding	8,672,840	7,906,791

See accompanying notes to consolidated financial statements.

Stewardship Financial Corporation and Subsidiary
Consolidated Statements of Comprehensive Income

	Years Ended December 31,	
	2018	2017
	(In thousands)	
Net income	$8,030	$3,947
Other comprehensive income (loss), net of tax:		
Change in unrealized holding gains (losses) on securities available-for-sale during the period	(677)	150
Reclassification adjustment for securities available for sale (gains) losses in net income	(4)	(1)
Accretion of unrealized loss on securities reclassified to held-to-maturity	22	28
Change in fair value of interest rate swap in a cash flow hedging relationship	(88)	(19)
Reclassification adjustment for interest rate swap interest expense in net income	32	2
Total other comprehensive income (loss)	(715)	160
Total comprehensive income	$7,315	$4,107

See accompanying notes to consolidated financial statements.

Stewardship Financial Corporation and Subsidiary
Consolidated Statements of Changes in Shareholders' Equity

	Years Ended December 31, 2018 and 2017				
	Common Stock		Retained	Accumulated Other Comprehensive Income	
	Shares	Amount	Earnings	(Loss), Net	Total
	(Dollars in thousands, except per share amounts)				
Balance – January 1, 2017	6,121,329	$41,626	$11,082	$ (1,321)	$51,387
Issuance of common stock, net of costs	2,509,090	18,860	—	—	18,860
Cash dividends declared ($0.12 per share)	—	—	(961)	—	(961)
Payment of discount on dividend reinvestment plan	—	(5)	—	—	(5)
Common stock issued under dividend reinvestment plan	10,031	90	—	—	90
Common stock issued under stock plans	8,025	77	—	—	77
Issuance of restricted stock	20,876	185	(185)	—	—
Amortization of restricted stock	—	—	184	—	184
Tax benefit from restricted stock vesting	—	48	—	—	48
Restricted stock forfeited	(16,547)	(139)	17	—	(122)
Net income	—	—	3,947	—	3,947
Other comprehensive (loss)	—	—	—	160	160
Reclassification due to the adoption of ASU 2018-02	—	—	223	(223)	—
Balance – December 31, 2017	8,652,804	60,742	14,307	(1,384)	73,665
Cash dividends declared ($0.12 per share)	—	—	(1,040)	—	(1,040)
Payment of discount on dividend reinvestment plan	—	(4)	—	—	(4)
Common stock issued under dividend reinvestment plan	8,386	87	—	—	87
Common stock issued under stock plans	2,943	30	—	—	30
Issuance of restricted stock	28,221	301	(301)	—	—
Compensation expense on restricted stock	—	—	206	—	206
Restricted stock forfeited	(11,966)	(126)	17	—	(109)
Net income	—	—	8,030	—	8,030
Other comprehensive (loss)	—	—	—	(715)	(715)
Reclassification due to the adoption of ASU 2016-01	—	—	(163)	163	—
Balance – December 31, 2018	8,680,388	$61,030	$21,056	$ (1,936)	$80,150

See accompanying notes to consolidated financial statements.

Stewardship Financial Corporation and Subsidiary
Consolidated Statements of Cash Flows

	Years Ended December 31,	
	2018	2017
	(In thousands)	
Cash flows from operating activities:		
Net income	$8,030	$3,947
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization of premises and equipment	475	399
Amortization of premiums and accretion of discounts, net	465	533
Compensation expense on restricted stock, net of forfeitures	201	62
Amortization of Subordinated Notes issuance cost	65	65
Accretion of deferred loan fees	147	145
Fair value adjustment for equity securities	(80)	—
Provision for loan losses	(1,615)	655
Originations of mortgage loans held for sale	(4,666)	(10,316)
Proceeds from sale of mortgage loans	5,106	10,897
Gain on sale of SBA loans	(193)	—
Gain on sales of mortgage loans	(70)	(178)
(Gain) loss on sales and calls of securities	186	(1)
Gain on sale of other real estate owned	—	(13)
Deferred income tax expense	(3)	1,419
Excess tax benefit from restricted stock vesting	—	48
Increase in accrued interest receivable	(130)	(433)
Increase (decrease) in accrued interest payable	(10)	322
Earnings on bank owned life insurance	(552)	(526)
Increase (decrease) in other assets	(155)	686
Increase in other liabilities	335	819
Net cash provided by operating activities	7,536	8,530
Cash flows from investing activities:		
Purchase of securities available-for-sale	(17,160)	(29,201)
Proceeds from maturities and principal repayments on securities available-for-sale	15,212	14,096
Proceeds from sales and calls on securities available-for-sale	1,007	500
Purchase of securities held-to-maturity	(15,828)	(8,173)
Proceeds from maturities and principal repayments on securities held-to-maturity	5,614	6,665
Proceeds from calls on securities held-to-maturity	280	1,320
Purchase of equity securities	(41)	—
Proceeds from sales of equity securities	2,037	—
Purchase of FHLB-NY stock	(6,671)	(11,650)
Redemption of FHLB-NY stock	6,421	11,450
Net increase in loans	(21,182)	(107,409)
Proceeds from sale of other real estate owned	—	414
Purchase of bank owned life insurance	—	(4,000)
Additions to premises and equipment	(573)	(742)
Net cash used in investing activities	(30,884)	(126,730)
Cash flows from financing activities:		
Net increase in noninterest-bearing deposits	1,856	3,555
Net increase in interest-bearing deposits	16,136	101,614
Increase in long term borrowings	10,000	25,000

Repayment of long term borrowings	(20,760)	(15,000)
Net increase (decrease) in short term borrowings	12,700	(5,440)
Proceeds from issuance of common stock, net of costs	—	18,860
Cash dividends paid on common stock	(1,040)	(961)
Payment of discount on dividend reinvestment plan	(4)	(5)
Taxes paid related to net share settlement of restricted stock	(104)	—
Issuance of common stock	117	167
Net cash provided by financing activities	18,901	127,790
Net increase (decrease) in cash and cash equivalents	(4,447)	9,590
Cash and cash equivalents - beginning	21,270	11,680
Cash and cash equivalents - ending	$16,823	$21,270

Stewardship Financial Corporation and Subsidiary
Consolidated Statements of Cash Flows, continued

	Years Ended December 31,	
	2018	2017
	(In thousands)	
Supplemental disclosures of cash flow information:		
Cash paid during the year for interest	$7,846	$5,536
Cash paid during the year for income taxes	$3,928	$2,322

See accompanying notes to consolidated financial statements.

Stewardship Financial Corporation and Subsidiary
Notes to Consolidated Financial Statements

Note 1. SIGNIFICANT ACCOUNTING POLICIES

Nature of operations and principles of consolidation

The consolidated financial statements include the accounts of Stewardship Financial Corporation and its wholly owned subsidiary, Atlantic Stewardship Bank ("the Bank"), together referred to as "the Corporation". The Bank includes its wholly-owned subsidiaries, Stewardship Investment Corporation (whose primary business is to own and manage an investment portfolio), Stewardship Realty LLC (whose primary business is to own and manage property at 612 Godwin Avenue, Midland Park, New Jersey), Atlantic Stewardship Insurance Company, LLC (whose primary business is insurance) and several other subsidiaries formed to hold title to properties acquired through foreclosure or deed in lieu of foreclosure. The Bank's subsidiaries have an insignificant impact on the daily operations. All intercompany accounts and transactions are eliminated in the consolidated financial statements. Certain prior period amounts have been reclassified to conform with the current year presentation.

The Corporation provides financial services through the Bank's offices in Bergen, Passaic, and Morris Counties, New Jersey. Its primary deposit products are checking, savings, and term certificate accounts, and its primary lending products are commercial, residential mortgage and installment loans. Substantially all loans are secured by specific items of collateral including business assets, consumer assets, and commercial and residential real estate. Commercial loans are expected to be repaid from cash flow generated from the operations of businesses. There are no significant concentrations of loans to any one industry or customer. The Corporation's lending activities are concentrated in loans secured by real estate located in northern New Jersey and, therefore, collectability of the loan portfolio is susceptible to changes in real estate market conditions in the northern New Jersey market. The Corporation has not made loans to borrowers outside the United States.

Basis of consolidated financial statements presentation

The consolidated financial statements of the Corporation have been prepared in conformity with U.S. generally accepted accounting principles ("GAAP"). In preparing the financial statements, management is required to make estimates and assumptions, based on available information, that affect the amounts reported in the financial statements and the disclosures provided. The estimate of the allowance for loan losses and the valuation of deferred tax assets are particularly critical because they involve a higher degree of complexity and subjectivity and require estimates and assumptions about highly uncertain matters. Actual results may differ from those estimates and assumptions. The current economic environment has increased the degree of uncertainty inherent in these material estimates.

Cash flows

Cash and cash equivalents include cash and deposits with other financial institutions and interest-bearing deposits in other banks with original maturities under 90 days. Net cash flows are reported for customer loan and deposit transactions, and short term borrowings and securities sold under agreement to repurchase.

Securities available-for-sale and held-to-maturity

The Corporation classifies its securities as held-to-maturity or available-for-sale. Investments in debt securities that the Corporation has the positive intent and ability to hold to maturity are classified as securities held-to-maturity and are carried at amortized cost. All other securities are classified as securities available-for-sale. Securities available-for-sale may be sold prior to maturity in response to changes in interest rates or prepayment risk, for asset/liability management purposes, or other similar factors. These securities are carried at fair value with unrealized holding gains or losses reported in a separate component of shareholders' equity, net of the related tax effects.

Interest income includes amortization of purchase premium or discount. Premiums and discounts on securities are amortized on the level-yield method without anticipating prepayments except for mortgage-backed securities where prepayments are anticipated. Gains and losses on sales are recorded on the trade date and determined using the specific identification method.

Management evaluates securities for other-than-temporary impairment ("OTTI") on at least a quarterly basis, and more frequently when economic or market conditions warrant such an evaluation. For securities in an unrealized loss position, management considers the extent and duration of the unrealized loss, and the financial condition and near-term prospects of the issuer. Management also assesses whether it intends to sell, or it is more likely than not that it will be required to sell, a security in an unrealized loss position before recovery of its amortized cost basis. If either of the criteria regarding intent or requirement to sell is met, the entire difference between amortized cost and fair value is recognized as impairment through earnings. For debt securities that do not meet the aforementioned criteria, the amount of impairment is split into two components as follows: (1) OTTI related to credit loss, which must be recognized in the income statement and (2) OTTI related to other factors, which is recognized in other comprehensive income. The credit loss is defined as the difference between the present value of the cash flows expected to be collected and the amortized cost basis.

Other Equity Investments

The Corporation carried other equity investments at fair value with unrealized holding gains or losses reported through the Consolidated Statement of Income beginning January 1, 2018 with the adoption of ASU No. 2016-01, "Financial Instruments - Overall: Recognition and Measurement of Financial Assets and Liabilities. Prior to the adoption of ASU No. 2016-01, the unrealized holding gains or losses reported in a component of shareholders' equity, net of the related tax effects. Cash dividends are reported as income when declared.

Federal Home Loan Bank ("FHLB") Stock

The Bank is a member of the FHLB system. Members are required to own a certain amount of FHLB stock based on their level of borrowings and other factors. FHLB stock is carried at cost, classified as a restricted security, and periodically evaluated for impairment based on the ultimate recovery of par value. Cash dividends are reported as income when declared.

Loans held for sale

Loans held for sale generally represent mortgage loans originated and intended for sale in the secondary market, which are carried at the lower of cost or fair value on an aggregate basis. Mortgage loans held for sale are carried net of deferred fees, which are recognized as income at the time the loans are sold to permanent investors. Gains or losses on the sale of mortgage loans held for sale are recognized at the settlement date and are determined by the difference between the net proceeds and the carrying value. All loans are generally sold with loan servicing rights released to the buyer.

Loans

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are reported at the principal amount outstanding, net of deferred loan fees and costs and an allowance for loan losses. Interest income is accrued on the unpaid principal balance. Loan origination fees, net of certain direct origination costs, are deferred and recognized in interest income using the level-yield method without anticipating prepayments. The recorded investment in loans represents the outstanding principal balance after charge-offs and does not include accrued interest receivable as the inclusion is not significant to the reported amounts.

Interest income on loans is discontinued at the time the loan is 90 days delinquent unless the loan is well secured and in process of collection. Past due status is based on the contractual terms of the loan. In all cases, loans are placed on nonaccrual or are charged-off at an earlier date if collection of principal or interest is considered doubtful. Nonaccrual loans and loans past due 90 days still on accrual include both smaller balance homogeneous loans that are collectively evaluated for impairment and individually classified impaired loans.

All interest accrued but not received for loans placed on nonaccrual is reversed against interest income. Interest received on such loans is accounted for on the cash-basis or cost-recovery method, until qualifying for return to accrual. Loans are returned to an accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

Allowance for loan losses

The allowance for loan losses is a valuation allowance for probable incurred credit losses. Loan losses are charged against the allowance when management believes the collectability of the full loan balance is in doubt. Subsequent recoveries, if any, are credited to the allowance. Management estimates the allowance balance required using past loan loss experience, the nature and volume of the portfolio, information about specific borrower situations and estimated collateral values, economic conditions and other factors. Allocations of the allowance may be made for specific loans, but the entire allowance is available for any loan that, in management's judgment, should be charged-off.

The allowance consists of specific and general components. The specific component relates to loans that are individually classified as impaired. In addition, the allowance contains an unallocated reserve amount to cover inherent imprecision of the overall loss estimation process. Due to the complexity in determining the estimated amount of allowance for loan losses, these unallocated reserves reflect management's attempt to ensure that the overall allowance reflects an appropriate level of reserves.

A loan is considered impaired when, based on current information and events, it is probable that the Corporation will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Loans for which the terms have been modified and for which the borrower is experiencing financial difficulties are considered troubled debt restructuring and classified as impaired. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed. Impairment is measured on a loan by loan basis by either the present value of expected future cash flows discounted at the loan's effective interest rate, the fair value of the note, or the fair value of the collateral if the loan is collateral-dependent. Large groups of smaller balance homogeneous loans, such as consumer and residential real estate loans are collectively evaluated for impairment and, accordingly, they are not separately identified for impairment disclosures. Troubled debt restructurings are separately identified for impairment disclosures and are measured at the present value of estimated future cash flows using the loan's effective rate at inception. If a troubled debt restructuring is considered to be a collateral dependent loan, the loan is reported, net, at the lower of the recorded investment or fair value of the collateral. For troubled debt restructurings that subsequently default, the Corporation determines the amount of reserve in accordance with the accounting policy for the allowance for loan losses.

The general component of the allowance is based on historical loss experience, including an appropriate loss emergence period, adjusted for qualitative factors. The historical loss experience is determined for each portfolio segment and class, and is based on the actual loss history experienced by the Corporation over the most recent five years. The Bank prepares an analysis for each portfolio segment, which examines the historical loss experience as well as the loss emergence period. The analysis is updated quarterly for the purpose of determining the assigned allocation factors which are essential components of the allowance for loan losses calculation. This actual loss experience is supplemented with other qualitative factors based on the risks present for each portfolio segment or class. These qualitative factors include consideration of the following: levels of and trends in charge-offs; levels of and trends in delinquencies and impaired loans; levels and trends in loan size; levels of real estate concentrations; national and local economic trends and conditions; the depth and experience of lending management and staff; and other changes in lending policies, procedures, and practices.

For purposes of determining the allowance for loan losses, loans in the portfolio are segregated by type into the following segments: commercial, commercial real estate, construction, residential real estate, consumer and other. The

Corporation also sub-divides these segments into classes based on the associated risks within those segments. Commercial loans are divided into the following two classes: secured by real estate and other. Construction loans are divided into the following two classes: commercial and residential. Consumer loans are divided into two classes: secured by real estate and other. The models and assumptions used to determine the allowance require management's judgment. Assumptions, data and computations are appropriately reviewed and properly documented.

The risk characteristics of each of the identified portfolio segments are as follows:

Commercial – Commercial loans are generally of higher risk and typically are made on the basis of the borrower's ability to make repayment from the cash flow of the borrower's business. As a result, the availability of funds for the repayment of commercial loans may depend substantially on the success of the business itself. Furthermore, any collateral securing such loans may depreciate over time, may be difficult to appraise and may fluctuate in value.

Commercial Real Estate – Commercial real estate loans are secured by multi-family and nonresidential real estate and generally have larger balances and generally are considered to involve a greater degree of risk than residential real estate loans. Commercial real estate loans depend on the global cash flow analysis of the borrower and the net operating income of the property, the borrower's expertise, credit history and profitability, and the value of the underlying property. Of primary concern in commercial real estate lending is the borrower's creditworthiness and the cash flow from the property. Payments on loans secured by income producing properties often depend on successful operation and management of the properties. As a result, repayment of such loans may be subject, to a greater extent than residential real estate loans, to adverse conditions in the real estate market or the economy. Commercial real estate is also subject to adverse market conditions that cause a decrease in market value or lease rates, obsolescence in location or function and market conditions associated with oversupply of units in a specific region.

Construction – Construction financing is generally considered to involve a higher degree of risk of loss than long-term financing on improved, occupied real estate. Risk of loss on a construction loan depends largely upon the accuracy of the initial estimate of the property's value at completion of construction and the estimated cost of construction. During the construction phase, a number of factors could result in delays and cost overruns. If the estimate of construction costs proves to be inaccurate, additional funds may be required to be advanced in excess of the amount originally committed to permit completion of the building. If the estimate of value proves to be inaccurate, the value of the building may be insufficient to assure full repayment if liquidation is required. If foreclosure is required on a building before or at completion due to a default, there can be no assurance that all of the unpaid balance of, and accrued interest on, the loan as well as related foreclosure and holding costs will be recovered.

Residential Real Estate – Residential real estate loans are generally made on the basis of the borrower's ability to make repayment from his or her employment income or other income, and which are secured by real property whose value tends to be more easily ascertainable. Repayment of residential real estate loans is subject to adverse employment conditions in the local economy leading to increased default rate and decreased market values from oversupply in a geographic area. In general, residential real estate loans depend on the borrower's continuing financial stability and, therefore, are likely to be adversely affected by various factors, including job loss, divorce, illness or personal bankruptcy. Furthermore, the application of various federal and state laws, including federal and state bankruptcy and insolvency laws, may limit the amount that can be recovered on such loans.

Consumer loans – Consumer loans secured by real estate may entail greater risk than residential mortgage loans due to a lower lien position. In addition, other consumer loans, particularly loans secured by assets that depreciate rapidly, such as motor vehicles, are subject to greater risk. In all cases, collateral for a defaulted consumer loan may not provide an adequate source of repayment for the outstanding loan and a small remaining deficiency often does not warrant further substantial collection efforts against the borrower. Consumer loan collections depend on the borrower's continuing financial stability and, therefore, are likely to be adversely affected by various factors, including job loss, divorce, illness or personal bankruptcy. Furthermore, the application of various federal and state laws, including federal and state bankruptcy and insolvency laws, may limit the amount that can be recovered on such loans.

Generally, when it is probable that some portion or all of a loan balance will not be collected, regardless of portfolio segment, that amount is charged-off as a loss against the allowance for loan losses. On loans secured by real estate, the charge-offs reflect partial writedowns due to the initial valuation of market values of the underlying real estate collateral in accordance with Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") 310-40. Consumer loans are generally charged-off in full when they reach 90 – 120 days past due.

Transfers of Financial Assets

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

Premises and equipment

Land is stated at cost. Buildings and improvements and furniture, fixtures and equipment are stated at cost, less accumulated depreciation computed on the straight-line method over the estimated lives of each type of asset. Estimated useful lives are three to forty years for buildings and improvements and three to twenty-five years for furniture, fixtures and equipment. Leasehold improvements are stated at cost less accumulated amortization computed on the straight-line method over the shorter of the term of the lease or useful life.

Long-Term Assets

Premises and equipment and other long-term assets are reviewed for impairment when events indicate their carrying amount may not be recovered from future undiscounted cash flows. If impaired, the assets are recorded at fair value.

Bank owned life insurance

The Corporation has purchased life insurance policies on certain key officers. Bank owned life insurance is recorded at the amount that can be realized under the insurance contract at the balance sheet date, which is the cash surrender value adjusted for other charges or other amounts due that are probable at settlement.

Dividend Reinvestment Plan

The Corporation offers shareholders the opportunity to participate in a dividend reinvestment plan. Plan participants may reinvest cash dividends to purchase new shares of stock at 95% of the market value, based on the most recent trades. Cash dividends due to the plan participants are utilized to acquire shares from either, or a combination of, the issuance of authorized shares or purchases of shares in the open market through an approved broker. The Corporation reimburses the broker for the 5% discount when the purchase of the Corporation's stock is completed. The plan is considered to be non-compensatory.

Stock-based compensation

Stock-based compensation cost is based on the fair value of the awards at the date of grant. The fair value of restricted stock awards is based upon the average of the high and low sale price reported for the Corporation's common stock on the date of grant. Compensation cost is recognized for restricted stock over the required service period, generally defined as the vesting period. Restricted shares may be forfeited if the vesting requirements are not met. Forfeitures are recognized when they occur.

Advertising Costs

The Corporation expenses advertising costs as incurred.

Income taxes

The Corporation records income taxes in accordance with ASC 740, Income Taxes, as amended, using the asset and liability method. Accordingly, deferred tax assets and liabilities: (i) are recognized for the expected future tax consequences of events that have been recognized in the financial statements or tax returns; (ii) are attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases; and (iii) are measured using enacted tax rates expected to apply in the years when those temporary differences are expected to be recovered or settled. Where applicable, deferred tax assets are reduced by a valuation allowance for any portions determined not likely to be realized. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income tax expense in the period of enactment. The valuation allowance is adjusted, by a charge or credit to income tax expense, as changes in facts and circumstances warrant. Deferred tax assets and liabilities are reported as a component of other assets on the consolidated statements of financial condition.

A tax position is recognized as a benefit only if it is “more likely than not” that the tax position would be sustained in a tax examination, with a tax examination being presumed to occur. The amount recognized is the largest amount of tax benefit that is greater than 50% likely of being realized on examination. For tax positions not meeting the “more likely than not” test, no tax benefit is recorded. The Corporation recognizes interest and/or penalties related to income tax matters in income tax expense.

Comprehensive income

Comprehensive income consists of net income and other comprehensive income (loss). Other comprehensive income includes unrealized gains and losses on securities available-for-sale, accretion of losses related to securities transferred from available-for-sale to held to maturity, and unrealized gains or losses on cash flow hedges, net of tax, which are also recognized as separate components of equity.

Earnings per common share

Basic earnings per common share is calculated by dividing net income available to common shareholders by the weighted average number of common shares outstanding during the period. Common stock equivalents are not included in the calculation.

Diluted earnings per share is computed similar to that of the basic earnings per share except that the denominator is increased to include the number of additional common shares that would have been outstanding if all potential dilutive common shares were issued.

Loan Commitments and Related Financial Instruments

Financial instruments include off-balance sheet credit instruments, such as commitments to make loans and commercial letters of credit, issued to meet customer financing needs. The face amount for these items represents the exposure to loss, before considering customer collateral or ability to repay. Such financial instruments are recorded when they are funded.

Loss contingencies

Loss contingencies, including claims and legal actions arising in the ordinary course of business, are recorded as liabilities when the likelihood of loss is probable and an amount or range of loss can be reasonably estimated. Management does not believe there are such matters that will have a material effect on the financial statements.

Dividend restriction

Banking regulations require maintaining certain capital levels and may limit the dividends paid by the Bank to the Corporation or by the Corporation to its shareholders. The Corporation's ability to pay cash dividends is based, among other things, on its ability to receive cash from the Bank. Banking regulations limit the amount of dividends that may be paid without prior approval of regulatory agencies. Under these regulations, the amount of dividends that may be paid in any calendar year is limited to the current year's profits, combined with the retained net profits of the preceding two years. At December 31, 2018 the Bank could have paid dividends totaling approximately $13.8 million. At December 31, 2018, this restriction did not result in any effective limitation in the manner in which the Corporation is currently operating.

Derivatives

Derivative financial instruments are recognized as assets or liabilities at fair value. The Corporation’s only free standing derivatives consist of interest rate swap agreements, which are used as part of its asset liability management strategy to help manage interest rate risk related to its deposits and Subordinated Debentures (see Note 8 to the Consolidated Financial Statements). The Corporation does not use derivatives for trading purposes.

The Corporation designated the interest rate swaps as cash flow hedges, which is a hedge of a forecasted transaction or the variability of cash flows to be received or paid related to a recognized asset or liability. For a cash flow hedge, the change in the fair value on the derivative is reported in other comprehensive income (loss) and is reclassified into earnings in the same periods during which the hedged transaction affects earnings. Net cash settlements on these interest rate swaps that qualify for hedge accounting are recorded in interest expense. 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 items are recognized immediately in current earnings.

The Corporation formally documented the risk-management objective and the strategy for undertaking the hedge transaction at the inception of the hedging relationship. The documentation includes linking the fair value of the cash flow hedge to the deposit or Subordinated Debentures on the balance sheet. The Corporation formally assessed, both at the hedge’s inception and on an ongoing basis, whether the interest rate swaps are highly effective in offsetting changes in cash flows of the deposits and Subordinated Debentures.

When a cash flow hedge is discontinued but the hedged cash flows or forecasted transactions are still expected to occur, gains or losses that would be accumulated in other comprehensive income are amortized into earnings over the same periods in which the hedged transactions will affect earnings.

Fair value of financial instruments

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

Segment Reporting

The Corporation acts as an independent community financial services provider and offers traditional banking and related financial services to individual, business and government customer. Through its branches, automated teller machine networks, and internet banking services, the Corporation offers a full array of commercial and retail financial service, including time, savings and demand deposits; the making of commercial, consumer and mortgage loans; and the providing of other financial services. Management does not separately allocate expense, including the cost of funding loan demand, between the commercial, retail, mortgage and consumer banking operation of the Corporation. Accordingly, all significant operating decisions are based upon analysis of the Bank as one segment or unit.

Subsequent Events

The Corporation has evaluated events and transactions occurring subsequent to the balance sheet date of December 31, 2018 for items that should potentially be recognized or disclosed in these financial statements.

Adoption of New Accounting Standards

In May 2014, the Financial Accounting Standards Board (the “FASB”) issued Accounting Standards Update (“ASU”) No. 2014-09, "Revenue from Contracts with Customers (Topic 606)". The objective of this amendment is to clarify the principles for recognizing revenue and to develop a common revenue standard for U.S. GAAP and International Financial Reporting Standards. This update affects any entity that either enters into contracts with customers to transfer goods or services or enters into contracts for the transfer of nonfinancial assets unless those contracts are in the scope of other standards. The ASU is effective for public business entities for financial statements issued for fiscal years beginning after December 15, 2017, and early adoption is permitted. Subsequently, the FASB issued the following standards related to ASU 2014-09: ASU 2016-08, “Revenue from Contracts with Customers (Topic 606): Principal versus Agent Considerations;” ASU 2016-10, “Revenue from Contracts with Customers (Topic 606): Identifying Performance Obligations and Licensing;” ASU 2016-11, “Revenue Recognition (Topic 605) and Derivatives and Hedging (Topic 815): Rescission of SEC Guidance Because of Accounting Standards Updates 2014-09 and 2014-16 Pursuant to Staff Announcements at the March 3, 2016 EITF Meeting;” ASU 2016-12, “Revenue from Contracts with Customers (Topic 606): Narrow-Scope Improvements and Practical Expedients;” ASU 2016-20, "Technical Corrections and Improvements to Topic 606, Revenue Contracts with Customers;" ASU 2017-13, "Revenue Recognition (Topic 605), Revenue from Contracts with Customers (Topic 606), Leases (Topic 840), and Leases (Topic 842): Amendments to SEC Paragraphs Pursuant to the Staff Announcement at the July 20, 2017 EITF Meeting and Rescission of Prior SEC Staff Announcements and Observer Comments;" and ASU 2017-14, "Income Statement - Reporting Comprehensive Income (Topic 220), Revenue Recognition (Topic 605), and Revenue from Contracts with Customers (Topic 606): Amendments to SEC Paragraphs Pursuant to Staff Accounting Bulletin No. 116 and SEC Release No. 33-10403." These amendments are intended to improve and clarify the implementation guidance of ASU 2014-09 and have the same effective date as the original standard. The Corporation’s implementation efforts include the identification of revenue within the scope of the guidance, as well as the evaluation of revenue contracts and the respective performance obligations within those contracts. We have evaluated the nature of our contracts with customers and determined that further disaggregation of revenue from contracts with customers into more granular categories beyond what is presented in the Condensed Consolidated Statement of Income was not necessary. We generally satisfy our performance obligations on contracts with customers as services are rendered, and the transaction prices are typically fixed and charged either on a periodic basis or based on activity. Because performance obligations are satisfied as services are rendered and the transaction prices are fixed, there is little judgment involved in applying this ASU that significantly affect the determination of the amount and timing of the revenue from contracts with customers. The Corporation has completed its evaluation and adopted this ASU effective January 1, 2018 using the modified retrospective approach. Adoption of ASU 2014-09 did not have a material impact on our Consolidated Financial Statements and related disclosures as our primary sources of revenues are derived from interest and dividends earned on loans, securities and other financial instruments that are not within the scope of the new standard. Our revenue recognition pattern for revenue streams within the scope of the new standard, including but not limited to service charges on deposit accounts and debit card interchange, did not change significantly from prior practice. The modified retrospective method requires application of ASU 2014-09 to uncompleted contracts at the date of adoption, however, periods prior to the date of adoption have not been retrospectively revised as the impact of the new standard on uncompleted contracts as of the date of adoption was not material. As such, a cumulative effective adjustment to opening retained earnings was not deemed necessary. Additional disclosures required have been included in Note 19 - Revenue Recognition.

In January 2016, the FASB issued ASU No. 2016-01, "Financial Instruments - Overall: Recognition and Measurement of Financial Assets and Liabilities." This ASU addresses certain aspects of recognition, measurement, presentation, and disclosure of financial instruments. This amendment supersedes the guidance to classify equity securities with readily determinable fair values into different categories, requires equity securities to be measured at fair value with changes in the fair value recognized through net income, and simplifies the impairment assessment of equity investments without readily determinable fair values. The amendment requires public business entities that are required to disclose the fair value of financial instruments measured at amortized cost on the balance sheet to measure that fair value using the exit price notion. The amendment requires an entity to present separately in other comprehensive income the portion of the total change in the fair value of a liability resulting from a change in the instrument-specific credit risk when the entity has elected to measure the liability at fair value in accordance with the fair value option. The amendment requires separate presentation of financial assets and financial liabilities by measurement category and form of financial asset on the balance sheet or in the accompanying notes to the financial statements. The amendment reduces diversity in current practice by clarifying that an entity should evaluate the need for a valuation allowance on a deferred tax asset related to available for sale securities in combination with the entity's other deferred tax assets. This amendment is effective for fiscal years, including interim periods, beginning after December 15, 2017. Entities should apply the amendment by means of a cumulative-effect adjustment as of the beginning of the fiscal year of adoption, with the exception of the amendment related to equity securities without readily determinable fair values, which should be applied prospectively to equity investments that exist as of the date of adoption. The Corporation's adoption of the guidance on January 1, 2018 resulted in the reclassification from accumulated other comprehensive income (loss) to retained earnings of $163,000, reflected in the Consolidated Statements of Changes in Shareholders' Equity. In addition, the fair value of loans has been estimated using the exit price notion as described in Note 16 to the Consolidated Financial Statements.

In February 2016, the FASB issued ASU 2016-02, "Leases (Subtopic 842)." This ASU requires all lessees to recognize a lease liability and a right-of-use asset, measured at the present value of the future minimum lease payments, at the lease commencement date. Lessor accounting remains largely unchanged under the new guidance. The amendments in ASU 2016-02 are effective for fiscal years, including interim periods, beginning after December 15, 2018. Early adoption of ASU 2016-02 is permitted. Subsequently, the FASB issued the following standards related to ASU 2016-02: ASU 2017-13, "Revenue Recognition (Topic 605), Revenue from Contracts with Customers (Topic 606), Leases (Topic 840), and Leases (Topic 842): Amendments to SEC Paragraphs Pursuant to the Staff Announcement at the July 20, 2017 EITF Meeting and Rescission of Prior SEC Staff Announcements and Observer Comments;" ASU 2018-1, "Leases (Topic 842): Land Easement Practical Expedient for Transition to Topic 842; ASU 2018-10, "Codification Improvements to Topic 842, Leases;" and ASU 2018-11, "Leases (Topic 842): Targeted Improvements." Based on the current lease portfolio, upon adoption of the new accounting standard, the Corporation anticipates recognizing a lease liability and related right-of-use asset on the Consolidated Statements of Financial Condition. Management is continuing to evaluate the Corporation's outstanding inventory of leases and determining the effect of recognizing operating leases on the Consolidated Statements of Financial Condition. The Corporation plans to adopt the modified retrospective approach under ASU 2018-11 in the first quarter of 2019. Based on the current composition of leases, at adoption, the Corporation is expected to record an estimated $3.3 million lease liability with a corresponding right-of-use asset on the Consolidated Statements of Financial Condition.

In June 2016, the FASB issued ASU 2016-13, "Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments." The main objective of this ASU is to provide financial statement users with more decision-useful information about the expected credit losses on financial instruments by a reporting entity at each reporting date. The amendments in this ASU require financial assets measured at amortized cost to be presented at the net amount expected to be collected. The allowance for credit losses would represent a valuation account that would be deducted from the amortized cost basis of the financial asset(s) to present the net carrying value at the amount expected to be collected on the financial asset. The income statement would reflect the measurement of credit losses for newly recognized financial assets, as well as the expected increases or decreases of expected credit losses that have taken place during the period. The measurement of expected credit losses would be based on relevant information about past events, including historical experience, current conditions, and reasonable and supportable forecasts that affect the collectability of the reported amount. An entity will be required to use judgment in determining the relevant information and estimation methods that are appropriate in its circumstances. The amendments in ASU 2016-13 are effective for fiscal years, including interim periods, beginning after December 15, 2019. Early adoption of this ASU is permitted for fiscal years beginning after December 15, 2018. The Corporation is currently evaluating the potential impact of ASU 2016-13 on the Corporation's consolidated financial statements. The Corporation has formed a working group, under the direction of the Chief Financial Officer, which is currently developing an implementation plan to include assessment of processes, portfolio segmentation, model development, system requirements and the identification of data and resource needs, among other things. Also, the Corporation is currently evaluating third-party vendor solutions to assist in the application of ASU 2016-13. The adoption of ASU 2016-13 may result in an increase in the allowance for loan losses due to 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. Furthermore, ASU 2016-13 will necessitate establishing an allowance for expected credit losses on debt securities. The Corporation has reviewed available historical data, preliminarily identified the appropriate loan pools and is in the process of reviewing loss rates. The completion of shadow calculations are expected in 2019. The Corporation is currently unable to reasonably estimate the impact of adopting ASU 2016-13, and it is expected that the impact of adoption will be significantly influenced by the composition, characteristics and quality of our loan and securities portfolios as well as the prevailing economic conditions and forecasts as of the adoption date.

In August 2016, the FASB issued ASU 2016-15, "Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments." ASU 2016-15 addresses changes to reduce the presentation diversity of certain cash receipts and cash payments in the statement of cash flows, including debt prepayment or extinguishment costs, settlement of certain debt instruments, contingent consideration payments made after a business combination, proceeds from the settlement of insurance claims, and distributions received from equity method investees. The guidance became effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years, with early adoption permitted. The new standard should be applied retrospectively, but may be applied prospectively if retrospective application would be impracticable. The Company adopted this ASU on January 1, 2018 and the impact was not material on the financial statements.

In March 2017, the FASB issued ASU 2017-08, "Premium Amortization on Purchased Callable Debt Securities (Subtopic 310-20)." The update shortens the amortization period for premiums on purchased callable debt securities to the earliest call date. The amendment will apply only to callable debt securities with explicit, noncontingent call features that are callable at fixed prices and on preset dates, apply to all premiums on callable debt securities, regardless of how they were generated, and require companies to reset the effective yield using the payment terms of the debt security if the call option is not exercised on the earliest call date. ASU 2017-08 does not require an accounting change for securities held at a discount. The discount continues to be amortized to maturity and does not apply when the investor has already incorporated prepayments into the calculation of its effective yield under other GAAP. The amendments in ASU 2017-08 are effective for public business entities for fiscal years beginning after December 15, 2018, including interim periods within those years. Early adoption is permitted, including adoption in an interim period. As the Corporation already amortizes these premiums to the call date, the adoption of this ASU will not have any impact on the Corporation's consolidated financial statements.

In August 2017, the FASB issued ASU No. 2017-12, "Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities", with the objective of improving the financial reporting of hedging relationships to better portray the economic results of an entity’s risk management activities in its financial statements. The amendments in ASU 2017-12 expand and refine hedge accounting for both nonfinancial and financial risk components and align the recognition and presentation of the effects of the hedging instrument and the hedged item in the financial statements. This ASU will be effective for interim and annual periods beginning after December 15, 2018. Early adoption of ASU 2017-12 is permitted. As of December 31, 2018, the Corporation has early adopted ASU 2017-12 with no material impact to the Corporation's consolidated financial statements.

Note 2. SECURITIES

The fair value of the available-for-sale securities and the related gross unrealized gains and losses recognized in accumulated other comprehensive income (loss) were as follows:

	December 31, 2018			
	Amortized	Gross Unrealized		Fair
	Cost	Gains	Losses	Value
	(In thousands)			
U.S. government-sponsored agencies	$26,232	$15	$(498)	$25,749
Obligations of state and political subdivisions	3,205	—	(84)	3,121
Mortgage-backed securities	63,659	68	(1,564)	62,163
Asset-backed securities (a)	4,916	6	—	4,922
Corporate debt (b)	13,369	48	(561)	12,856
Total	$111,381	$137	$(2,707)	$108,811

	December 31, 2017			
	Amortized	Gross Unrealized		Fair
	Cost	Gains	Losses	Value
	(In thousands)			
U.S. government-sponsored agencies	$21,699	$30	$(396)	$21,333
Obligations of state and political subdivisions	3,221	—	(56)	3,165
Mortgage-backed securities	64,775	70	(1,011)	63,834
Asset-backed securities (a)	6,672	30	(4)	6,698
Corporate debt (b)	14,437	94	(302)	14,229
Total	$110,804	$224	$(1,769)	$109,259

(a) Collateralized by student loans.
(b) Corporate debt securities are primarily in financial institutions.

Cash proceeds realized from sales and calls of securities available-for-sale for the years ended December 31, 2018 and 2017 were $1,007,000 and $500,000, respectively. There were gross gains totaling $6,000 and no gross losses realized on sales or calls during the year ended December 31, 2018. There were gross gains totaling $1,000 and no gross losses realized on sales or calls during the year ended December 31, 2017.

The fair value of available-for-sale securities pledged to secure public deposits for the years ended December 31, 2018 and 2017 was $988,000 and $990,000, respectively. See also Note 7 to the Consolidated Financial Statements regarding securities pledged as collateral for Federal Home Loan Bank of New York advances.

The following is a summary of the held-to-maturity securities and related gross unrealized gains and losses:

	December 31, 2018			
	Amortized	Gross Unrealized		Fair
	Cost	Gains	Losses	Value
	(In thousands)			
U.S. Treasury	$999	$—	$(14)	$985
U.S. government-sponsored agencies	35,565	20	(976)	34,609
Obligations of state and political subdivisions	2,358	14	(27)	2,345
Mortgage-backed securities	23,386	47	(375)	23,058
Total	$62,308	$81	$(1,392)	$60,997

	December 31, 2017			
	Amortized	Gross Unrealized		Fair
	Cost	Gains	Losses	Value
	(In thousands)			
U.S. Treasury	$999	$—	$(11)	$988
U.S. government-sponsored agencies	27,075	4	(760)	26,319
Obligations of state and political subdivisions	4,057	21	(23)	4,055
Mortgage-backed securities	20,311	76	(198)	20,189
Total	$52,442	$101	$(992)	$51,551

Cash proceeds realized from calls of securities held-to-maturity for the years ended December 31, 2018 and 2017 were $280,000 and $1,320,000, respectively. There were no gross gains and no gross losses realized from calls during the years ended December 31, 2018 and 2017.

The fair value of held-to-maturity securities pledged to secure public deposits for the years ended December 31, 2018 and 2017 was $626,000 and $789,000, respectively. See also Note 7 to the Consolidated Financial Statements regarding securities pledged as collateral for Federal Home Loan Bank of New York advances.

Issuers may have the right to call or prepay obligations with or without call or prepayment penalties. This might cause actual maturities to differ from the contractual maturities.

Mortgage-backed securities are a type of asset-backed security secured by a mortgage or collection of mortgages, purchased by government agencies such as the Government National Mortgage Association and government sponsored agencies such as the Federal National Mortgage Association ("FNMA") and the Federal Home Loan Mortgage Corporation, which then issue securities that represent claims on the principal and interest payments made by borrowers on the loans in the pool. At year-end 2018 and 2017, the Corporation had no holdings of securities of any one issuer other than the U.S. government and its agencies in an amount greater than 10% of shareholders' equity.

The following table presents the amortized cost and fair value of the debt securities portfolio by contractual maturity. As issuers may have the right to call or prepay obligations with or without call or prepayment premiums, the actual maturities may differ from contractual maturities. Securities not due at a single maturity date, such as mortgage-backed securities and asset-backed securities, are shown separately.

	December 31, 2018	
	Amortized Cost	Fair Value
	(In thousands)	
Available-for-sale		
Within one year	$1,543	$1,528
After one year, but within five years	12,918	12,734
After five years, but within ten years	23,978	23,260
After ten years	4,367	4,204
Mortgage-backed securities	63,659	62,163
Asset-backed securities	4,916	4,922
Total	$111,381	$108,811
Held-to-maturity		
Within one year	$335	$336
After one year, but within five years	18,032	17,738
After five years, but within ten years	20,067	19,404
After ten years	488	461
Mortgage-backed securities	23,386	23,058
Total	$62,308	$60,997

The following tables summarize the fair value and unrealized losses of those investment securities which reported an unrealized loss at December 31, 2018 and 2017, and if the unrealized loss position was continuous for the twelve months prior to December 31, 2018 and 2017.

Available-for-sale

December 31, 2018	Less than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
	(In thousands)					
U.S. government-sponsored agencies	$—	$ —	$17,432	$ (498)	$17,432	$ (498)
Obligations of state and political subdivisions	—	—	3,121	(84)	3,121	(84)
Mortgage-backed securities	4,177	(19)	47,479	(1,545)	51,656	(1,564)
Asset-backed securities	2,892	—	—	—	2,892	—
Corporate debt	—	—	8,808	(561)	8,808	(561)
Total temporarily impaired securities	$7,069	$ (19)	$76,840	$ (2,688)	$83,909	$ (2,707)

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Available-for-sale

December 31, 2017	Less than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
	(In thousands)					
U.S. government-sponsored agencies	$8,260	$ (70)	$11,174	$ (326)	$19,434	$ (396)
Obligations of state and political subdivisions	1,384	(7)	1,781	(49)	3,165	(56)
Mortgage-backed securities	30,575	(201)	26,809	(810)	57,384	(1,011)
Asset-backed securities	—	—	3,013	(4)	3,013	(4)
Corporate debt	—	—	9,135	(302)	9,135	(302)
Total temporarily impaired securities	$40,219	$ (278)	$51,912	$ (1,491)	$92,131	$ (1,769)

Held-to-maturity

December 31, 2018	Less than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
	(In thousands)					
U.S. Treasury	$—	$ —	$985	$ (14)	$985	$ (14)
U.S. government-sponsored agencies	2,496	(9)	24,595	(967)	27,091	(976)
Obligations of state and political subdivisions	—	—	461	(27)	461	(27)
Mortgage-backed securities	5,885	(67)	11,081	(308)	16,966	(375)
Total temporarily impaired securities	$8,381	$ (76)	$37,122	$ (1,316)	$45,503	$ (1,392)

Held-to-maturity

December 31, 2017	Less than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
	(In thousands)					
U.S. Treasury	$988	$ (11)	$—	$ —	$988	$ (11)
U.S. government-sponsored agencies	10,032	(139)	15,265	(621)	25,297	(760)
Obligations of state and political subdivisions	—	—	474	(23)	474	(23)
Mortgage-backed securities	9,531	(114)	3,896	(84)	13,427	(198)
Total temporarily impaired securities	$20,551	$ (264)	$19,635	$ (728)	$40,186	$ (992)

Equity securities consist solely of a Community Reinvestment Act ("CRA") mutual fund. During 2018, the Corporation adopted Accounting Standards Update No. 2016-01, "Financial Instruments - Overall: Recognition and

Measurement of Financial Assets and Liabilities. As a result of adoption, this fund was transferred from available for sale and reclassified into other equity investments on the Consolidated Statements of Financial Condition. In addition, the Corporation recorded an cumulative effect adjustment of $163,000 as a reclassification from accumulated other comprehensive loss to retained earnings. All future unrealized gains and losses are recognized in the Consolidated Statements of Income.

Other-Than-Temporary-Impairment

At December 31, 2018, there were available-for-sale investments comprising twenty-one U.S. government-sponsored agency securities, seven obligations of state and political subdivision securities, seventy-three mortgage-backed securities, and nine corporate debt securities in a continuous loss position for twelve months or longer. At December 31, 2018, there were held-to-maturity investments comprising one U.S. treasury, twenty-six U.S. government-sponsored agency securities, one obligation of state and political subdivision security, and twenty-seven mortgage-backed securities in a continuous loss position for twelve months or longer. Management has assessed the securities that were in an unrealized loss position at December 31, 2018 and 2017 and determined that any decline in fair value below amortized cost primarily relate to changes in interest rates and market spreads and was temporary.

In making this determination management considered the following factors: the period of time the securities were in an unrealized loss position; the percentage decline in comparison to the securities' amortized cost; any adverse conditions specifically related to the security, an industry or a geographic area; the rating or changes to the rating by a credit rating agency; the financial condition of the issuer and guarantor and any recoveries or additional declines in fair value subsequent to the balance sheet date.

Management does not intend to sell securities in an unrealized loss position and it is not more likely than not that the Corporation will be required to sell these securities before the recovery of their amortized cost bases, which may be at maturity.

Note 3. LOANS AND ALLOWANCE FOR LOAN LOSSES

At December 31, 2018 and 2017, respectively, the loan portfolio consisted of the following:

	December 31,	
	2018	2017
	(In thousands)	
Commercial:		
Secured by real estate	$28,790	$31,684
Other	64,965	57,372
Commercial real estate	504,522	493,542
Commercial construction	9,787	2,152
Residential real estate	82,491	85,760
Consumer:		
Secured by real estate	36,120	32,207
Other	455	563
Government Guaranteed Loans - guaranteed portion	6,559	8,334
Other	98	106
Total gross loans	733,787	711,720
Less: Deferred loan costs, net	457	397
Allowance for loan losses	7,926	8,762
	8,383	9,159
Loans, net	$725,404	$702,561

Included in Commercial - Other and Commercial real estate were $170,000 and $3,561,000, respectively, of Small Business Administration ("SBA") loans originated during 2018. The guaranteed portion of these loans were sold during the year ended December 31, 2018.

In addition to the origination of SBA loans, prior to 2017, the Corporation purchased the guaranteed portion of several Government Guaranteed loans. These loans are listed separately in the table above. Due to the guarantee of the principal amount of these loans, no allowance for loan losses is established for these loans.

The Corporation has entered into lending transactions with directors, executive officers and principal shareholders of the Corporation and their affiliates. At December 31, 2018 and 2017, these loans aggregated approximately $3,038,000 and $3,248,000, respectively. During the year ended December 31, 2018, new loans totaling $2,126,000 were granted and repayments totaled approximately $1,461,000. Additionally, one loan relationship in the amount of $874,000 is no longer included in the December 31, 2018 balance as the director is no longer affiliated with this borrower as they had been previously. The loans, at December 31, 2018 and 2017, were current as to principal and interest payments.

Excluded from the above table are $14.3 million and $11.4 million of unpaid principal balances of loans serviced for others at December 31, 2018 and 2017, respectively.

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

	Year Ended December 31, 2018				
	Balance beginning of period	Provision charged to operations	Loans charged-off	Recoveries of loans charged-off	Balance end of period
	(In thousands)				
Commercial	$3,058	$(468)	$(29)	$142	$2,703
Commercial real estate	5,531	(1,249)	—	665	4,947
Commercial construction	33	98	—	—	131
Residential real estate	68	(3)	—	—	65
Consumer	64	2	—	2	68
Other	1	1	(2)	1	1
Unallocated	7	4	—	—	11
Balance, ending	$8,762	$(1,615)	$(31)	$810	$7,926

	Year Ended December 31, 2017				
	Balance beginning of period	Provision charged to operations	Loans charged-off	Recoveries of loans charged-off	Balance end of period
	(In thousands)				
Commercial	$2,663	$301	$(3)	$97	$3,058
Commercial real estate	4,734	697	—	100	5,531
Commercial construction	355	(322)	—	—	33
Residential real estate	66	2	—	—	68
Consumer	75	(19)	—	8	64
Other	—	1	(1)	1	1
Unallocated	12	(5)	—	—	7
Balance, ending	$7,905	$655	$(4)	$206	$8,762

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The following tables present the balance in the allowance for loan losses and the recorded investment in loans by portfolio segment and based on the impairment method as of December 31, 2018 and 2017:

	December 31, 2018								
	Commercial	Commercial Real Estate	Commercial Construction	Residential Real Estate	Consumer	Government Guaranteed	Other Loans	Unallocated	Total
	(In thousands)								
Allowance for loan losses:									
Ending allowance balance attributable to loans									
Individually evaluated for impairment	$88	$561	$—	$—	$—	$—	$—	$—	$649
Collectively evaluated for impairment	2,615	4,386	131	65	68	—	1	11	7,277
Total ending allowance balance	$2,703	$4,947	$131	$65	$68	$—	$1	$11	$7,926
Loans:									
Loans individually evaluated for impairment	$633	$6,079	$—	$576	$—	$—	$—	$—	$7,288
Loans collectively evaluated for impairment	93,122	498,443	9,787	81,915	36,575	6,559	98	—	726,499
Total ending loan balance	$93,755	$504,522	$9,787	$82,491	$36,575	$6,559	$98	$—	$733,787

	December 31, 2017								
	Commercial	Commercial Real Estate	Commercial Construction	Residential Real Estate	Consumer	Government Guaranteed	Other Loans	Unallocated	Total
	(In thousands)								
Allowance for loan losses:									
Ending allowance balance attributable to loans									
Individually evaluated for impairment	$34	$575	$—	$—	$—	$—	$—	$ —	$609
Collectively evaluated for impairment	3,024	4,956	33	68	64	—	1	7	8,153
Total ending allowance balance	$3,058	$5,531	$33	$68	$64	$—	$1	$ 7	$8,762
Loans:									
Loans individually evaluated for impairment	$549	$6,236	$—	$295	$62	$—	$—	$ —	$7,142
Loans collectively evaluated for impairment	88,507	487,306	2,152	85,465	32,708	8,334	106	—	704,578
Total ending loan balance	$89,056	$493,542	$2,152	$85,760	$32,770	$8,334	$106	$ —	$711,720

The following table presents the recorded investment in nonaccrual loans at the dates indicated:

	December 31,	
	2018	2017
	(In thousands)	
Commercial:		
Secured by real estate	$394	$136
Commercial real estate	574	701
Residential real estate	576	295
Consumer:		
Secured by real estate	—	62
Total nonaccrual loans	$1,544	$1,194

At December 31, 2018 and 2017 there were no loans that were past due 90 days and still accruing.

The following table presents loans individually evaluated for impairment by class of loans at and for the periods indicated:

	At And For The Year Ended December 31, 2018				
	Unpaid Principal Balance	Recorded Investment	Allowance for Loan Losses Allocated	Average Recorded Investment	Interest Income Recognized
	(In thousands)				
With no related allowance recorded:					
Commercial:					
Secured by real estate	$447	$ 416		$ 455	$ 11
Commercial real estate	3,329	3,001		3,061	108
Residential real estate	587	576		343	—
Consumer:					
Secured by real estate	—	—		28	—
With an allowance recorded:					
Commercial:					
Secured by real estate	95	95	$ 83	65	3
Other	122	122	5	125	9
Commercial real estate	3,078	3,078	561	3,095	161
Total impaired loans	$7,658	$ 7,288	$ 649	$ 7,172	$ 292

During the year ended December 31, 2018, no interest income was recognized on a cash basis.

	At And For The Year Ended December 31, 2017				
	Unpaid Principal Balance	Recorded Investment	Allowance for Loan Losses Allocated	Average Recorded Investment	Interest Income Recognized
	(In thousands)				
With no related allowance recorded:					
Commercial:					
Secured by real estate	$389	$ 389		$ 964	$ 70
Commercial real estate	3,442	3,124		3,148	121
Residential real estate	295	295		59	—
Consumer:					
Secured by real estate	71	62		70	—
With an allowance recorded:					
Commercial:					
Secured by real estate	33	32	$ 27	45	—
Other	128	128	7	171	12
Commercial real estate	3,112	3,112	575	3,144	128
Total impaired loans	$7,470	$ 7,142	$ 609	$ 7,601	$ 331

During the year ended December 31, 2017, no interest income was recognized on a cash basis.

The following table presents the aging of the recorded investment in past due loans by class of loans as of December 31, 2018 and 2017. Nonaccrual loans are included in the disclosure by payment status:

	December 31, 2018					
	30-59 Days Past Due	60-89 Days Past Due	Greater than 90 Days Past Due	Total Past Due	Loans Not Past Due	Total
	(In thousands)					
Commercial:						
Secured by real estate	$—	$ —	$394	$394	$28,396	$28,790
Other	6	—	—	6	64,959	64,965
Commercial real estate	2,155	—	509	2,664	501,858	504,522
Commercial construction	—	—	—	—	9,787	9,787
Residential real estate	112	42	308	462	82,029	82,491
Consumer:						
Secured by real estate	—	—	—	—	36,120	36,120
Other	1	—	—	1	454	455
Government Guaranteed Loans	—	—	—	—	6,559	6,559
Other	—	—	—	—	98	98
Total	$2,274	$ 42	$1,211	$3,527	$730,260	$733,787

	December 31, 2017					
	30-59 Days Past Due	60-89 Days Past Due	Greater than 90 Days Past Due	Total Past Due	Loans Not Past Due	Total
	(In thousands)					
Commercial:						
Secured by real estate	$186	$ —	$ —	$186	$31,498	$31,684
Other	8	—	—	8	57,364	57,372
Commercial real estate	300	—	599	899	492,643	493,542
Commercial construction	—	—	—	—	2,152	2,152
Residential real estate	314	—	—	314	85,446	85,760
Consumer:						
Secured by real estate	—	—	28	28	32,179	32,207
Other	—	—	—	—	563	563
Government Guaranteed Loans	—	—	—	—	8,334	8,334
Other	—	—	—	—	106	106
Total	$808	$ —	$ 627	$1,435	$710,285	$711,720

Troubled Debt Restructurings

In order to determine whether a borrower is experiencing financial difficulty necessitating a restructuring, an evaluation is performed of the probability that the borrower will be in payment default on any of its debt in the foreseeable future without the modification. This evaluation is performed in accordance with the Corporation's internal underwriting policy. A loan is considered to be in payment default once it is contractually 90 days past due.

At December 31, 2018 and 2017, the Corporation had $6.3 million and $6.6 million, respectively, of loans whose terms have been modified in troubled debt restructurings. Of these loans, $5.7 million and $5.9 million had demonstrated a reasonable period of performance in accordance with their new terms at December 31, 2018 and 2017, respectively, and are, therefore, accruing loans. The remaining troubled debt restructurings are reported as nonaccrual loans. Specific reserves of $649,000 and $582,000 have been recorded for the troubled debt restructurings at December 31, 2018 and 2017, respectively, and are included in the table above. As of December 31, 2018 and December 31, 2017, there were no additional funds committed to these borrowers.

The following table presents the number of loans and their recorded investment immediately prior to the modification date and immediately after the modification date by class that were modified as troubled debt restructurings during the year ended December 31, 2018:

	December 31, 2018		
	Number of Loans	Pre-Modification Recorded Investment	Post-Modification Recorded Investment
	(Dollars in thousands)		
Commercial:			
Secured by real estate	1	$ 95	$ 95
Total	1	$ 95	$ 95

During the year ended December 31, 2018, there was one loan modified as a troubled debt restructuring. The modification of the terms of the commercial - secured by real estate loan represented the term out of the remaining balance of a line of credit.

For the year ended December 31, 2018, the troubled debt restructuring described above resulted in an increase in the allowance for loan losses of $83,000. There were no charge-offs during the twelve months ended December 31, 2018 related to this troubled debt restructuring.

There were no new loans classified as troubled debt restructuring during the year ended December 31, 2017.

For the years ended December 31, 2018 and 2017, there was a net increase in the allowance for loan losses of $67,000 and decrease of $28,000, respectively, related to troubled debt restructurings. There were no charge-offs in 2018 or 2017 related to these troubled debt restructurings.

There were no loans modified as TDRs within the previous 12 months from both December 31, 2018 and 2017, which had a payment default (90 days or more past due) during the years ended December 31, 2018 and 2017.

TDRs that subsequently default are considered collateral dependent impaired loans and are evaluated for impairment based on the estimated fair value of the underlying collateral less expected selling costs.

Credit Quality Indicators

The Corporation categorizes loans into risk categories based on relevant information about the ability of the borrowers to service their debt such as: current financial information, historical payment experience, credit documentation, public information, and current economic trends, among other factors. The Corporation analyzes loans individually by classifying the loans as to credit risk. This analysis includes non-homogeneous loans, such as commercial, commercial real estate and commercial construction loans. This analysis is performed at the time the loan is originated and annually thereafter. The Corporation uses the following definitions for risk ratings.

Special Mention – A Special Mention asset has potential weaknesses that deserve management's close attention, which, if left uncorrected, may result in deterioration of the repayment prospects for the asset or the Bank's credit position at some future date. Special Mention assets are not adversely classified and do not expose the Bank to sufficient risk to warrant adverse classification.

Substandard – Substandard loans are inadequately protected by the current net worth and paying capacity of the borrower or by the collateral pledged, if any. Loans so classified must have a well-defined weakness or weaknesses that jeopardize the repayment and liquidation of the debt. These loans are characterized by the distinct possibility that the Bank will sustain some loss if the deficiencies are not corrected.

Doubtful – A Doubtful loan has all of the weaknesses inherent in those classified as Substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently known facts, conditions, and values, highly questionable or improbable. The likelihood of loss is extremely high, but because of certain important and reasonably specific factors, an estimated loss is deferred until a more exact status can be determined.

Loss – A loan classified Loss is considered uncollectible and of such little value that its continuance as an asset is not warranted. This classification does not necessarily mean that an asset has absolutely no recovery or salvage value, but rather it is not practical or desirable to defer writing off a basically worthless asset even though partial recovery may be affected in the future.

Loans not meeting the criteria above that are analyzed individually as part of the above described process are considered to be pass rated loans. As of December 31, 2018 and 2017, and based on the most recent analysis performed at those times, the risk category of loans by class is as follows:

	December 31, 2018					
	Pass	Special Mention	Substandard	Doubtful	Loss	Total
	(In thousands)					
Commercial:						
Secured by real estate	$26,879	$1,234	$677	$—	$—	$28,790
Other	63,438	181	1,346	—	—	64,965
Commercial real estate	490,661	7,086	6,775	—	—	504,522
Commercial construction	9,787	—	—	—	—	9,787
Government Guaranteed Loans guaranteed portion	6,559	—	—	—	—	6,559
Total	$597,324	$8,501	$8,798	$—	$—	$614,623

	December 31, 2017					
	Pass	Special Mention	Substandard	Doubtful	Loss	Total
	(In thousands)					
Commercial:						
Secured by real estate	$29,025	$2,153	$ 506	$ —	$ —	$31,684
Other	56,632	216	524	—	—	57,372
Commercial real estate	481,443	10,023	2,076	—	—	493,542
Commercial construction	2,152	—	—	—	—	2,152
Government Guaranteed						
Loans guaranteed portion	8,334	—	—	—	—	8,334
Total	$577,586	$12,392	$ 3,106	$ —	$ —	$593,084

The Corporation considers the historical and projected performance of the loan portfolio and its impact on the allowance for loan losses. For residential real estate and consumer loan segments, the Corporation evaluates credit quality primarily based on payment activity and historical loss data. The following table presents the recorded investment in residential real estate and consumer loans based on payment activity as of December 31, 2018 and 2017.

	December 31, 2018		
	Current	30+ Days Past Due or Nonaccrual	Total
	(In thousands)		
Residential real estate	$81,761	$ 730	$82,491
Consumer:			
Secured by real estate	36,120	—	36,120
Other	454	1	455
Total	$118,335	$ 731	$119,066

	December 31, 2017		
	Current	30+ Days Past Due or Nonaccrual	Total
	(In thousands)		
Residential real estate	$85,446	$ 314	$85,760
Consumer:			
Secured by real estate	32,179	28	32,207
Other	563	—	563
Total	$118,188	$ 342	$118,530

Note 4. PREMISES AND EQUIPMENT, NET

The balance of premises and equipment consists of the following at December 31, 2018 and 2017:

	Years Ended December 31,	
	2018	2017
	(In thousands)	
Land	$3,240	$3,240
Buildings and improvements	4,654	4,505
Leasehold improvements	1,925	1,923
Furniture, fixtures, and equipment	2,027	1,605
	11,846	11,273
Less: accumulated depreciation and amortization	4,839	4,364
Total premises & equipment, net	$7,007	$6,909

Amounts charged to net occupancy expense for depreciation and amortization of banking premises and equipment amounted to $475,000 and $399,000 in 2018 and 2017, respectively.

Note 5. OTHER REAL ESTATE OWNED

There was no other real estate owned at the years ended December 31, 2018 and 2017.

There was no activity in the allowance for losses on other real estate owned for the year ended December 31, 2018. Activity in the allowance for losses on other real estate owned for the year ended December 31, 2017 was as follows:

	Year Ended December 31, 2017 (In thousands)
Beginning of year	$ 3
Additions charged to expense	—
Reductions from sales of other real estate owned	(3)
End of year	$ —

There was no gain on sale of other real estate owned for the year ended December 31, 2018. Net gain on sale of other real estate owned totaled $13,000 for the year ended December 31, 2017.

There were no other real estate owned expenses for the year ended December 31, 2018. Expenses related to other real estate owned for the year ended December 31, 2017 include:

Year
Ended
December
31, 2017
(In
thousands)

Provision for unrealized losses	$	—
Operating expenses, net of rental income	24	
End of year	$	24

75

Note 6. DEPOSITS

The following table presents deposits at December 31, 2018 and 2017:

	December 31,	
	2018	2017
	(In thousands)	
Noninterest-bearing demand	$174,717	$172,861
Interest-bearing checking accounts	175,215	196,924
Money market accounts	149,936	110,256
Total interest-bearing demand	325,151	307,180
Statement savings and clubs	71,472	77,284
Business savings	5,273	5,830
Total savings	76,745	83,114
IRA investment and variable rate savings	31,876	33,236
Brokered certificates	37,063	25,944
Money market certificates	136,539	141,764
Total certificates of deposit	205,478	200,944
Total interest-bearing deposits	607,374	591,238
Total deposits	$782,091	$764,099

Certificates of deposit with balances of $250,000 or more at December 31, 2018 and 2017, totaled $59,421,000 and $42,810,000, respectively.

The scheduled maturities of certificates of deposit were as follows:

Year Ended December 31,	Balances (In thousands)
2019	$ 115,418
2020	45,973
2021	34,421
2022	7,132
2023	2,534
	$ 205,478

The following table presents interest expense on deposits at December 31, 2018 and 2017 summarized as follows:

	December 31, 2018	December 31, 2017
	(In thousands)	
Total interest bearing demand	$2,147	$709
Total savings	83	91
Total certificates of deposit	3,063	2,389
Total interest expense	$5,293	$3,189

Deposits from executive officers and directors at December 31, 2018 and 2017 were $3,627,000 and $3,793,000, respectively.

Note 7. BORROWINGS

Federal Home Loan Bank of New York Advances

The following table presents Federal Home Loan Bank of New York ("FHLB-NY") advances by maturity date:

Advances Maturing	December 31, 2018 Amount	Weighted Average Rate		December 31, 2017 Amount	Weighted Average Rate	
	(Dollars in thousands)					
Within one year	$45,700	1.99	%	$20,760	1.59	%
After one year, but within two years	5,000	1.88	%	33,000	1.76	%
After two years, but within three years	5,000	1.68	%	5,000	1.88	%
After three years, but within four years	—	—	%	5,000	1.68	%
After four years, but within five years	10,000	3.25	%	—	—	%
Total advances maturing	$65,700	2.15	%	$63,760	1.71	%

During 2018 and 2017, the maximum amount of FHLB-NY advances outstanding at any month end was $65.8 million and $93.8 million, respectively. The average amount of advances outstanding during the years ended December 31, 2018 and 2017 was $52.4 million and $74.4 million, respectively.

Advances from the FHLB-NY are all fixed rate borrowings and are secured by a blanket assignment of the Corporation's unpledged, qualifying residential first mortgage loans, by select commercial real estate loans and by certain securities. The loans remain under the control of the Corporation. Securities are maintained in safekeeping with the FHLB-NY. As of December 31, 2018 and 2017, the advances were collateralized by $68.2 million and $73.0 million, respectively, of residential first mortgage loans under the blanket lien arrangement and by $44.1 million and $49.3 million of investment securities, respectively. Additionally, as of December 31, 2018, the advances were collateralized by $37.8 million of select commercial real estate loans pledged to the FHLB-NY. Based on the collateral, the Corporation was eligible to borrow up to a total of $150.2 million at December 31, 2018 and $122.3 million at December 31, 2017.

The Corporation has the ability to borrow overnight with the FHLB-NY. As of December 31, 2018, overnight borrowings with the FHLB-NY were $12.7 million. There were no overnight borrowings with the FHLB-NY as of December 31, 2017. The overall borrowing capacity is contingent on available collateral to secure borrowings and the ability to purchase additional activity-based capital stock of the FHLB-NY.

The Corporation may also borrow from the Discount Window of the Federal Reserve Bank of New York based on the market value of collateral pledged. At December 31, 2018 and 2017, the Corporation’s borrowing capacity at the Discount Window was $3.3 million and $4.7 million, respectively. In addition, at both December 31, 2018 and 2017 the Corporation had available overnight variable repricing lines of credit with other correspondent banks totaling $38.0 million, on an unsecured basis. There were no borrowings under these lines of credit at December 31, 2018 and 2017.

Note 8. SUBORDINATED DEBENTURES AND SUBORDINATED NOTES

Issue	Maturity	Rate	Carrying Amount December 31, 2018	2017
			(In thousands)	
9/17/2003	9/17/2033	Fixed / Floating Rate Junior Subordinated Debentures	$7,217	$7,217
8/28/2015	8/25/2025	Fixed Rate Subordinated Notes	16,165	16,100
		Total	$23,382	$23,317

In 2003, the Corporation formed Stewardship Statutory Trust I (the "Trust"), a statutory business trust, which on September 17, 2003 issued $7.0 million Fixed/Floating Rate Capital Securities ("Capital Securities"). The Trust used the proceeds of the Capital Securities to purchase from the Corporation, $7,217,000 of Fixed/Floating Rate Junior Subordinated Deferrable Interest Debentures (the "Subordinated Debentures") maturing September 17, 2033. The Trust is obligated to distribute all proceeds of a redemption whether voluntary or upon maturity, to holders of the Capital Securities. The Corporation's obligation with respect to the Capital Securities and the Subordinated Debentures, when taken together, provide a full and unconditional guarantee on a subordinated basis by the Corporation of the Trust's obligations to pay amounts when due on the Capital Securities. The Corporation is not considered the primary beneficiary of the Trust (variable interest entity); therefore, the Trust is not consolidated in the Corporation's consolidated financial statements, but rather the Subordinated Debentures are shown as a liability. Prior to September 17, 2008, the Capital Securities and the Subordinated Debentures both had a fixed interest rate of 6.75%. Beginning September 17, 2008, the rate floats quarterly at a rate of three month LIBOR plus 2.95%. At December 31, 2018 and 2017, the rate on both the Capital Securities and the Subordinated Debentures was 5.74% and 4.55%, respectively. The Corporation has the right to defer payments of interest on the Subordinated Debentures by extending the interest payment period for up to 20 consecutive quarterly periods. The Subordinated Debentures may be included in Tier 1 capital (with certain limitations applicable) under current regulatory guidelines and interpretations.

On August 28, 2015, the Corporation completed a private placement of $16.6 million in aggregate principal amount of fixed rate subordinated notes (the "Subordinated Notes") to certain institutional accredited investors pursuant to a Subordinated Note Purchase Agreement dated August 28, 2015 between the Corporation and such investors. The Subordinated Notes have a maturity date of August 28, 2025 and bear interest at the rate of 6.75% per annum, payable semi-annually, in arrears, on March 1 and September 1 of each year during the time that the Subordinated Notes remain outstanding. The Subordinated Notes include a right of prepayment, without penalty, on or after August 28, 2020 and, in certain limited circumstances, before that date. The indebtedness evidenced by the Subordinated Notes, including principal and interest, is unsecured and subordinate and junior in right of the Corporation's payment to general and secured creditors and depositors of the Bank. The Subordinated Notes have been structured to qualify as Tier 2 capital for regulatory purposes. The Subordinated Notes totaled $16.2 million and $16.1 million at December 31, 2018 and 2017, respectively, which includes $435,000 and $500,000, respectively, of remaining unamortized debt issuance costs. The debt issuance costs are being amortized over the expected life of the issue.

Note 9. REGULATORY CAPITAL REQUIREMENTS

The Corporation is subject to capital adequacy guidelines promulgated by the Board of Governors of the Federal Reserve System ("FRB Board"). The Bank is subject to somewhat comparable but different capital adequacy requirements imposed by the Federal Deposit Insurance Corporation (the "FDIC"). The federal banking agencies have adopted risk-based capital guidelines for banks and bank holding companies. The risk-based capital guidelines are designed to make regulatory capital requirements more sensitive to differences in risk profiles among banks and bank holding companies, to account for off-balance sheet exposure, and to minimize disincentives for holding liquid assets. Under these guidelines, assets and off-balance sheet items are assigned to broad risk categories, each with appropriate weights. The resulting capital ratios represent capital as a percentage of total risk-weighted assets and off-balance sheet items.

Federal banking regulators have also adopted leverage capital guidelines to supplement the risk-based measures. Leverage capital to average total assets is determined by dividing Tier 1 Capital as defined under the risk-based capital guidelines by average total assets (non-risk adjusted).

Guidelines for Banks

In December 2010 and January 2011, the Basel Committee on Banking Supervision (the "Basel Committee") published the final texts of reforms on capital and liquidity, which are generally referred to as "Basel III". The Basel Committee is a committee of central banks and bank supervisors and regulators from the major industrialized countries that develops broad policy guidelines for the regulation of banks and bank holding companies. In July 2013, the FDIC and the other federal bank regulatory agencies adopted final rules (the "Basel Rules") to implement certain provisions of Basel III and the Dodd-Frank Wall Street Reform and Consumer Protection Act. The Basel Rules revised the leverage and risk-based capital requirements and the methods for calculating risk-weighted assets. The Basel Rules apply to all depository institutions, top-tier bank holding companies with total consolidated assets of $1 billion or more and top-tier savings and loan holding companies.

Among other things, the Basel Rules (a) established a new common equity Tier 1 Capital ("CET1") to risk-weighted assets ratio minimum of 4.5% of risk-weighted assets, (b) raised the minimum Tier 1 Capital to risk-based assets requirement ("Tier 1 Capital Ratio) from 4% to 6% of risk-weighted assets and (c) assigned a higher risk weight of 150% to exposures that are more than 90 days past due or are on nonaccrual status and to certain commercial real estate facilities. The minimum ratio of Total Capital to risk-weighted assets (including certain off-balance sheet activities, such as standby letters of credit) is 8%. At least 6% of the Total Capital is required to be "Tier 1 Capital", which consists of common shareholders' equity and certain preferred stock, less certain items and other intangible assets. The remainder, "Tier 2 Capital," may consist of (a) the allowance for loan losses of up to 1.25% of risk-weighted assets, (b) excess of qualifying preferred stock, (c) hybrid capital instruments, (d) debt, (e) mandatory convertible securities and (f) qualifying subordinated debt. "Total Capital" is the sum of Tier 1 Capital and Tier 2 Capital less reciprocal holdings of other banking organizations' capital instruments, investments in unconsolidated subsidiaries and any other deductions as determined by the federal banking regulatory agencies on a case-by-case basis or as a matter of policy after formal rule-making. A small bank holding company that has the highest regulatory examination rating and is not contemplating significant growth or expansion must maintain a minimum level of Tier 1 Capital to average total consolidated assets leverage ratio of at least 3%. All other bank holding companies are expected to maintain a leverage ratio of at least 100 to 200 basis points above the stated minimum.

The Basel Rules also require unrealized gains and losses on certain available-for-sale securities to be included for purposes of calculating regulatory capital unless a one-time opt-out was exercised. Additional constraints are also imposed on the inclusion in regulatory capital of mortgage-servicing assets and deferred tax assets. The Basel Rules limit a banking organization's capital distributions and certain discretionary bonus payments if the banking organization does not hold a "capital conservation buffer" consisting of 2.5% of CET1 to risk-weighted assets in addition to the amount necessary to meet a minimum risk-based capital requirement. The purpose of the capital conservation buffer is to ensure that banking organizations conserve capital when it is needed most, allowing them to weather periods of economic stress. Banking institutions with a CET1 Ratio, Tier 1 Capital Ratio or Total Capital Ratio above the minimum capital ratios but below the minimum capital ratios plus the capital conservation buffer will face constraints on their ability to pay dividends, repurchase equity and pay discretionary bonuses to executive officers based on the amount of the shortfall. The Basel Rules became effective for the Bank on January 1, 2015. The capital conservation buffer requirement of 0.625% became effective January 1, 2016 and was phased in annually through January 1, 2019, when the full capital conservation buffer requirement of 2.50% became effective. At December 31, 2018, the Bank's capital conservation buffer requirement was 1.875% and the actual capital conservation buffer was 5.54%.

Bank assets are given risk-weights of 0%, 20%, 50%, 100%, and 150%. In addition, certain off-balance sheet items are given similar credit conversion factors to convert them to asset equivalent amounts to which an appropriate risk-weight will apply. These computations result in the total risk-weighted assets. Most loans are assigned to the 100% risk category, except for performing first mortgage loans fully secured by residential property which carry a 50% risk-weighting. Loan exposures past due 90 days or more or on nonaccrual are assigned a risk-weighting of at least 100%. High volatility commercial real estate ("HVCRE") loan exposures are assigned to the 150% category; provided, however, Section 214 of the Economic Growth Act, prohibits federal banking agencies from requiring the financial institution to assign heightened risk weights to HVCRE loans unless the loan is related to real estate acquisition, development and construction ("HVCRE ADC"). Under the Basel III capital rules, HVCRE ADC loans are assigned a higher risk weight than other commercial real estate loans. Most investment securities (including, primarily, general obligation claims of states or other political subdivisions of the United States) are assigned to the 20% category, except for municipal or state revenue bonds, which have a 50% risk-weight, and direct obligations of the U.S. Treasury or obligations backed by the full faith and credit of the U.S. government, which have a 0% risk-weight. In converting off-balance sheet items, direct credit substitutes, including general guarantees and standby letters of credit backing nonfinancial obligations, and undrawn commitments (including commercial credit lines with an initial maturity of more than one year) have a 50% risk-weighting. Short-term undrawn commitments and commercial letters of credit with an initial maturity of under one year have a 50% risk-weighting and certain short-term unconditionally cancelable commitments are not risk-weighted.

Community Bank Leverage Ratio

The recently enacted Economic Growth Act requires federal banking agencies to develop a "community bank leverage ratio" (the ratio of a bank's tangible equity capital to average total consolidated assets) for financial institutions with assets of less than $10 billion. A "qualifying community bank" that exceeds this ratio will be deemed to be in compliance with all other capital and leverage requirements, including the capital requirements to be considered "well capitalized" under prompt corrective action rules. The federal banking agencies may consider an institution's risk profile when evaluating whether it qualifies as a community bank for purposes of the capital ratio requirement. The minimum capital for the new community bank leverage ratio must be set at not less than 8% and not more than 10%. A financial institution can elect to be subject to this new definition. The Economic Growth Act requires the federal banking agencies to consult with state banking regulators and notify the applicable state banking regulator of any qualifying community bank that exceeds or no longer exceeds the Community Bank Leverage Ratio.

Guidelines for Small Bank Holding Companies

The Dodd-Frank Act required the FRB to establish for all bank and savings and loan holding companies minimum consolidated capital requirements that are as stringent as those required for the insured depository subsidiaries. The FRB has updated and amended its Small Bank Holding Company Policy Statement to extend to bank and savings and loan holding companies the applicability of the "Small Bank Holding Company" exception to its consolidated capital requirements and, as a result of the Economic Growth Act, increased the threshold for the exception from $1.0 billion in consolidated assets to $3.0 billion in consolidated assets. As a result of the revised Small Bank Holding Company Policy Statement, Basel III capital rules and reporting requirements do not apply to small bank holding companies ("SBHC"), such as the Corporation, that have total consolidated assets of less than $3 billion unless otherwise advised by the FRB. The minimum risk-based capital requirements for a SBHC to be considered adequately capitalized are 4% for Tier 1 Capital and 8% for Total Capital to risk-weighted assets.

The regulations for SBHCs classify risk-based capital into two categories: "Tier 1 Capital" which consists of common and qualifying perpetual preferred shareholders' equity less goodwill and other intangibles and "Tier 2 Capital" which consists of (a) the allowance for loan losses of up to 1.25% of risk-weighted assets, (b) the excess of qualifying preferred stock, (c) hybrid capital instruments, (d) debt, (e) mandatory convertible securities and (f) qualifying subordinated debt. Total qualifying capital consists of Tier 1 Capital and Tier 2 Capital less reciprocal holdings of other banking organizations' capital instruments, investments in unconsolidated subsidiaries and any other deductions as determined by the FRB on a case-by-case basis or as a matter of policy after formal rule-making. However, the amount of Tier 2 Capital may not exceed the amount of Tier 1 Capital. The Corporation must maintain a minimum level of Tier 1 Capital to average total consolidated assets leverage ratio of 3%, which is the leverage ratio reserved for top-tier bank holding companies having the highest regulatory examination rating and not contemplating significant growth or expansion.

Bank holding company assets are given risk-weights of 0%, 20%, 50%, and 100%. In addition, certain off-balance sheet items are given similar credit conversion factors to convert them to asset equivalent amounts to which an appropriate risk-weight will apply. These computations result in the total risk-weighted assets.

	Actual		Required for Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Corrective Action Regulations	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
	(Dollars in thousands)					
December 31, 2018						
Tier 1 Leverage ratio						
Corporation	$89,086	9.33 %	$38,213	4.00%	N/A	N/A
Bank	99,761	10.49%	38,032	4.00%	$47,540	5.00 %
Risk-based capital:						
Common Equity Tier 1						
Corporation	N/A	N/A	N/A	N/A	N/A	N/A
Bank	99,761	12.54%	35,798	4.50%	51,708	6.50 %
Tier 1						
Corporation	89,086	11.33%	31,461	4.00%	N/A	N/A
Bank	99,761	12.54%	47,731	6.00%	63,641	8.00 %
Total						
Corporation	113,178	14.39%	62,922	8.00%	N/A	N/A
Bank	107,687	13.54%	63,641	8.00%	79,551	10.00%
December 31, 2017						
Tier 1 Leverage ratio						
Corporation	$81,886	8.88 %	$36,867	4.00%	N/A	N/A
Bank	92,824	10.12%	36,698	4.00%	$45,872	5.00 %
Risk-based capital:						
Common Equity Tier 1						
Corporation	N/A	N/A	N/A	N/A	N/A	N/A
Bank	92,824	12.24%	34,113	4.50%	49,274	6.50 %
Tier 1						
Corporation	81,886	10.96%	29,889	4.00%	N/A	N/A
Bank	92,824	12.24%	45,484	6.00%	60,645	8.00 %
Total						
Corporation	106,748	14.29%	59,777	8.00%	N/A	N/A
Bank	101,586	13.40%	60,645	8.00%	75,807	10.00%

As presented above, at December 31, 2018 and 2017, the Bank’s regulatory capital ratios exceeded the established minimum capital requirements.

The Subordinated Notes have been structured to qualify as Tier 2 capital for regulatory purposes.

Note 10. BENEFIT PLANS

The Corporation has a 401(k) plan which covers all eligible employees. Participants may elect to contribute a percentage, up to 100%, of their salaries, not to exceed the applicable limitations as per the Internal Revenue Code. The Corporation's matching contribution is determined on an annual basis. For the year ended ended December 31, 2018 and 2017, the Corporation matched 50% of the participant's first 7% contribution. Total 401(k) expense for the years ended December 31, 2018 and 2017 amounted to approximately $213,000 and $173,000, respectively.

The Corporation offers an Employee Stock Purchase Plan which allows all eligible employees to authorize a specific payroll deduction from his or her base compensation for the purchase of the Corporation's Common Stock. Total stock purchases amounted to 2,863 and 2,724 shares during 2018 and 2017, respectively. At December 31, 2018, the Corporation had 165,706 shares reserved for issuance under this plan.

During 2017, the Corporation introduced a Supplemental Executive Retirement Plan ("SERP") for the President / Chief Executive Officer of the Corporation. In 2018 this plan was expanded to include the Executive Vice President / Chief Financial Officer and the Executive Vice President / Chief Lending Officer. The SERP provides a supplemental retirement income benefit upon the attainment of age 66 or separation of service. SERP benefits are payable in equal monthly installments for 180 months. Benefits are also payable upon death. The estimated present value of future benefits is accrued over the period from the effective date of the agreement until the expected retirement date. The Corporation recorded SERP expense of $444,000 and $258,000 for the years ended December 31, 2018 and 2017, respectively. The benefits accrued under the SERP included in Accrued Expenses and Other Liabilities totaled $702,000 and $258,000 at December 31, 2018 and 2017, respectively, and are unfunded.

Note 11. STOCK-BASED COMPENSATION

At December 31, 2018, the Corporation maintained the following stock award programs.

Director Stock Plan

The Director Stock Plan permits members of the Board of Directors of the Bank to receive their monthly Board of Directors' fees in shares of the Corporation's Common Stock, rather than in cash. Shares are purchased for directors in the open market and resulted in purchases of 2,644 and 2,855 shares for the years ended December 31, 2018 and 2017, respectively. At December 31, 2018, the Corporation had 512,005 shares authorized but unissued for this plan.

Stock Incentive Plan

The 2010 Stock Incentive Plan covers both employees and directors. The purpose of the plan is to promote the long-term growth and profitability of the Corporation by (i) providing key people with incentives to improve shareholder value and to contribute to the growth and financial success of the Corporation, and (ii) enabling the Corporation to attract, retain and reward the best available persons. The plan permits the granting of stock (including incentive stock options qualifying under Internal Revenue Code section 422 and nonqualified options), stock appreciation rights, restricted or unrestricted stock awards, phantom stock, performance awards or other stock-based awards.

Restricted shares granted under the plan generally vest over a three year service period with compensation expenses recognized on a straight-line basis. The value of restricted shares is based upon an average of the high and low closing price of the Corporation's common stock on the date of grant.

Changes in nonvested restricted shares were as follows:

	2018		2017	
	Number of Shares	Weighted Average Grant Date Fair Value	Number of Shares	Weighted Average Grant Date Fair Value

Balance January 1	51,528	$ 6.91	68,586	$ 5.52
Granted	28,221	10.65	20,876	8.88
Vested (1)	(28,066)	4.39	(34,675)	5.40
Forfeited	(2,131)	9.82	(3,259)	6.41
Balance December 31	49,552	$ 10.34	51,528	$ 6.91

(1) Includes 9,835 and 13,288 shares in 2018 and 2017, respectively, that vested but were immediately forfeited to cover taxes.

Stock based compensation expense related to stock grants to associates was $97,000 and $62,000 for the years ended December 31, 2018 and 2017, respectively. As of December 31, 2018, there was approximately $282,000 of unrecognized compensation cost related to non-vested stock grants that will be recognized over the next 26 months.

There were no unrestricted stock awards granted during the years ended December 31, 2018. There were 5,000 unrestricted stock awards granted to the members of the Board of Directors during the year ended December 31, 2017. Expense related to stock grants to directors was $50,000 for the year ended December 31, 2017 .

At December 31, 2018 the Corporation had 64,528 shares authorized but unissued for this plan.

Note 12. EARNINGS PER COMMON SHARE

The following reconciles the income available to common shareholders (numerator) and the weighted average common stock outstanding (denominator) for both basic and diluted earnings per share:

	Years Ended December 31,	
	2018	2017
	(Dollars in thousands, except per share amounts)	
Net income available to common shareholders	$8,030	$ 3,947
Weighted average common shares outstanding - basic and diluted	8,672,840	7,906,791
Basic and diluted earnings per common share	$0.93	$ 0.50

There were no stock options to purchase shares of common stock for the years ended December 31, 2018 or 2017.

Note 13. INCOME TAXES

The Tax Cuts and Jobs Act ("Tax Act) was signed into law on December 22, 2017. Included as part of the law was a permanent reduction in the Federal corporate income tax rate from 35% to 21% effective January 1, 2018. Based upon the change in the tax rate, the Corporation revalued its net deferred tax asset at December 31, 2017. As a result of the enactment of the Tax Act, the Corporation recognized an additional tax expense of $1.4 million for the year ended December 31, 2017.

The components of income tax expense are summarized as follows:

	Years Ended December 31,	
	2018	2017
	(In thousands)	
Current tax expense		
Federal	$1,865	$2,438
State	1,158	919
	3,023	3,357
Deferred tax expense		
Federal	100	1,555
State	(101)	(128)

Valuation allowance	(2)	(8)
	(3)	1,419
Total	$3,020	$4,776

The following table presents a reconciliation between the reported income taxes and the income taxes which would be computed by applying the normal federal income tax rate (21% and 34% for the year ended December 31, 2018 and 2017, respectively) to income before income taxes:

	Years Ended December 31,	
	2018	2017
	(In thousands)	
Federal income tax	$2,320	$2,966
Add (deduct) effect of:		
State income taxes, net of federal income tax effect	835	606
Nontaxable interest income	(47)	(129)
Effect of change in Federal statutory tax rate	33	1,420
Bank owned life insurance	(116)	(198)
Nondeductible expenses	(14)	(31)
Change in valuation reserve	(2)	(8)
Out of period adjustment for state fixed asset basis	—	150
Other	11	—
Effective federal income taxes	$3,020	$4,776

The tax effects of existing temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities are as follows:

	December 31,	
	2018	2017
	(In thousands)	
Deferred tax assets:		
Allowance for loan losses	$2,285	$2,455
Accrued compensation	109	91
Nonaccrual loan interest	30	12
Depreciation	94	202
Contribution carry forward	—	2
Mortgage servicing rights	(22)	(5)
Accrued contributions	249	167
Unrealized loss on securities available-for-sale	836	498
SERP	202	—
	3,783	3,422
Valuation reserve	—	(2)
Net deferred tax assets	$3,783	$3,420

At December 31, 2018, the Corporation provided a valuation allowance relating to a state tax benefit of contribution carryforwards. Management had determined that it was more likely than not that it would not be able to realize this deferred tax benefit.

There were no unrecognized tax benefits during the years or at the years ended December 31, 2018 and 2017 and management does not expect a significant change in unrecognized benefits in the next twelve months. There were no tax interest and penalties recorded in the income statement for the years ended December 31, 2018 and 2017. There were no tax interest and penalties accrued for the years ended December 31, 2018 and 2017.

The Corporation and its subsidiaries are subject to U.S. federal income tax as well as income tax of the States of New Jersey and New York.

The Corporation is no longer subject to examination by taxing authorities for years before 2015.

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Note 14. COMMITMENTS AND CONTINGENCIES

Loan Commitments

The Corporation 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. Those instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the consolidated financial statements. The contract or notional amounts of those instruments reflect the extent of involvement the Corporation has in particular classes of financial instruments.

The Corporation's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit and standby letters of credit is represented by the contractual notional amount of those instruments. The Corporation uses the same credit policies in making commitments and conditional obligations as it does for on-balance sheet instruments.

At December 31, 2018, the Corporation had no residential mortgage commitments to extend credit. Commercial, construction, and home equity loan commitments of approximately $7.3 million were extended with variable rates averaging 5.43% and approximately $780,000 extended at fixed rates averaging 4.36%. Generally, commitments were due to expire within approximately 90 days.

Additionally, at December 31, 2018, the Corporation was committed for approximately $124.7 million of unused lines of credit, consisting of $31.8 million relating to a home equity line of credit program and an unsecured line of credit program, $3.9 million relating to an unsecured overdraft protection program, and $89.0 million relating to commercial and construction lines of credit. Amounts drawn on the unused lines of credit are predominantly assessed interest at rates which fluctuate with the base rate.

Commitments under standby letters of credit were approximately $2.5 million at December 31, 2018, of which $2.4 million expire within one year. Should any letter of credit be drawn on, the interest rate charged on the resulting note would fluctuate with the Corporation's base rate. Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments may expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Corporation evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Corporation upon extension of credit, is based on management's credit evaluation of the borrower. Collateral held varies, but may include accounts receivable, inventory, property, plant and equipment, and income-producing commercial properties.

Standby letters of credit are conditional commitments issued by the Corporation to guarantee payment or performance of a customer to a third party. Those guarantees are primarily issued to support public and private borrowing arrangements, including commercial paper, bond financing and similar transactions. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. The Corporation obtains collateral supporting those commitments for which collateral is deemed necessary.

Lease Commitments

At December 31, 2018, the minimum rental commitments on the noncancellable leases with an initial term of one year and expiring thereafter are as follows:

Year Ended December 31,	Minimum Rent (In thousands)
2019	$ 718
2020	657
2021	483
2022	454
2023	379
Thereafter	666
	$ 3,357

Rental expense under long-term operating leases for branch offices amounted to approximately $888,000 and $873,000 during the years ended December 31, 2018 and 2017, respectively. Rental income was approximately $36,000 and $36,000 for the years ended December 31, 2018 and 2017, respectively.

Contingencies

The Corporation is also subject to litigation which arises primarily in the ordinary course of business. In the opinion of management the ultimate disposition of such litigation should not have a material adverse effect on the financial position of the Corporation.

Note 15. INTEREST RATE SWAP

The Corporation utilizes interest rate swap agreements as part of its asset liability management strategy to help manage its interest rate risk position. The notional amount of the interest rate swap does not represent an amount exchanged by the parties. The amount exchanged is determined by reference to the notional amount and the other terms of the individual interest rate swap agreements.

Interest Rate Swap Designated as Cash Flow Hedge:

During the second quarter of 2017, the Corporation entered into a forward-starting interest rate swap with an effective date of December 18, 2017 and a notional amount of $7.0 million. This swap was designated as a cash flow hedge of the Subordinated Debentures (See Note 8 to the Consolidated Financial Statements). In addition, during the second quarter of 2018, the Corporation entered into two forward-starting interest rate swaps with an effective date of September 1, 2018 and notional amount of $10.0 million each. These swaps were designated as cash flow hedges of money market deposit accounts whose interest rate is tied to the Effective Federal Funds Rate. All of the swaps were determined to be highly effective during the years ended December 31, 2018 and 2017. As such, no amount of ineffectiveness has been included in net income per ASU 2017-12. Therefore, the aggregate fair value of the swaps is recorded in other assets (liabilities) with changes in fair value recorded in other comprehensive income (loss). The amount included in accumulated other comprehensive income (loss) would be reclassified to current earnings should the hedge no longer be considered effective. In addition, interest expense on the swaps is reclassified and reported as a component of interest expense as incurred.

Summary information as of December 31, 2018 and 2017 about the interest swaps designated as cash flow hedges are as follows:

	As of December 31, 2018				
	Notional Amount	Unrealized Gain / (Loss)	Fixed Pay Rate	Floating Receive Rate	Maturity Date
	(Dollars in thousands)				
Interest rate swaps by effective date					
December 18, 2017	$7,000	$ 134	5.323 %	3 month LIBOR plus 2.95%	June 17, 2027
September 1, 2018	10,000	(84)	2.607 %	Federal Funds Rate	August 31, 2021
September 1, 2018	10,000	(162)	2.615 %	Federal Funds Rate	August 31, 2023
	$27,000	$ (112)			

	As of December 31, 2017				
	Notional Amount	Unrealized Loss	Fixed Pay Rate	Floating Receive Rate	Maturity Date
	(Dollars in thousands)				
Interest rate swaps by effective date					
December 18, 2017	$7,000	$ (29)	5.323 %	3 month LIBOR plus 2.95%	June 17, 2027
	$7,000	$ (29)			

The Corporation has secured the interest rate swaps by pledging investment securities with a fair value of $170,000 at both December 31, 2018 and 2017.

The net expense recorded on the swap transactions totaled $46,000 and $2,000 for the years ended December 31, 2018 and 2017, respectively, and is reported as a component of interest expense on Deposits and Subordinated Debentures and Subordinated Notes, as appropriate. There are no netting arrangements for any of the interest rate swaps.

The fair value of the interest rate swaps in the amount of $134,000 were included in other assets on the Consolidated Statements of Financial Condition at December 31, 2018. The fair value of the interest rate swap in the amount of ($246,000) and ($29,000) at December 31, 2018 and 2017, respectively, were included in accrued expenses and other liabilities on the Consolidated Statements of Financial Condition.

The following table presents the after tax net gains recorded in accumulated other comprehensive income and the Consolidated Statements of Income relating to the cash flow derivative instruments for the periods indicated.

	Year Ended December 31, 2018		
	Amount of Gain (Loss) Recognized in OCI (Effective Portion)	Amount of Gain (Loss) Reclassified from OCI to Interest Expense	Amount of Gain (Loss) Recognized in Other Noninterest Income (Ineffective Portion)
	(In thousands)		
Interest rate swaps by effective date			
December 18, 2017	$119	$ (16)	$ —
September 1, 2018	(60)	(15)	—
September 1, 2018	(115)	(15)	—
Total	$(56)	$ (46)	$ —

	Year Ended December 31, 2017		
	Amount of Gain (Loss) Recognized in OCI (Effective Portion)	Amount of Gain (Loss) Reclassified from OCI to Interest Expense	Amount of Gain (Loss) Recognized in Other Noninterest Income (Ineffective Portion)
	(In thousands)		
Interest rate swaps by effective date			
December 18, 2017	$ (21)	$ —	$ —
Total	$ (21)	$ —	$ —

Note 16. FAIR VALUE OF FINANCIAL INSTRUMENTS

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

Level 1: Quoted prices (unadjusted) or identical assets or liabilities in active markets that the entity has the ability to access as of the measurement date.

Level 2: Significant other observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.

Level 3: Significant unobservable inputs that reflect a reporting entity’s own assumptions about the assumptions that market participants would use in pricing an asset or liability.

Assets and Liabilities Measured on a Recurring Basis

Assets and liabilities measured at fair value on a recurring basis are summarized below:

		Fair Value Measurements Using		
	Carrying Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
	December 31, 2018 (In thousands)			
Assets:				
Available-for-sale securities				
U.S. government - sponsored agencies	$25,749	$—	$ 25,749	$ —
Obligations of state and political subdivisions	3,121	—	3,121	—
Mortgage-backed securities	62,163	—	62,163	—
Asset-backed securities	4,922	—	4,922	—
Corporate bonds	12,856	—	12,856	—
Total available-for-sale securities	$108,811	$—	$ 108,811	$ —
Other equity investments	$1,648	$1,588	$ 60	$ —
Interest Rate Swap	$134	$—	$ 134	$ —
Liabilities:				
Interest rate swap	$246	$—	$ 246	$ —

		Fair Value Measurements Using		
	Carrying Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
	December 31, 2017 (In thousands)			
Assets:				
Available-for-sale securities				
U.S. government -	$21,333	$—	$ 21,333	$ —

sponsored agencies				
Obligations of state and political subdivisions	3,165	—	3,165	—
Mortgage-backed securities	63,834	—	63,834	—
Asset-backed securities	6,698	—	6,698	—
Corporate bonds	14,229	—	14,229	—
Total available-for-sale securities	$ 109,259	$—	$ 109,259	$ —
Other equity investments	$ 3,756	$ 3,696	$ 60	$ —
Liabilities:				
Interest rate swap	$ 29	$—	$ 29	$ —

There were no transfers of assets between Level 1 and Level 2 during the years ended December 31, 2018 and 2017. There were no changes to the valuation techniques for fair value measurements as of December 31, 2018 and 2017.

The fair values of investment securities are determined by quoted market prices, if available (Level 1). If quoted prices are not available, fair values of investment securities are determined by 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 (Level 2 inputs). The Corporation performs quarterly analyses on the prices received from the pricing service to determine whether the prices are reasonable estimates of fair value. Specifically, the Corporation compares the prices received from the pricing service to a secondary pricing source. The Corporation’s internal price verification procedures have not historically resulted in adjustment in the prices obtained from the pricing service.

Other equity investments primarily represent a Community Reinvestment Act (CRA) mutual fund investment.

The interest rate swaps are reported at fair values obtained from brokers who utilize internal models with observable market data inputs to estimate the values of these instruments (Level 2 inputs).

Assets and Liabilities Measured on a Non-Recurring Basis

Assets and liabilities measured at fair value on a non-recurring basis are summarized below:

		Fair Value Measurements Using		
	Carrying Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
	December 31, 2018			
	(In thousands)			
Assets:				
Impaired loans				
Commercial:				
Secured by real estate	$301	$ —	$ —	$ 301
Residential real estate	308	—	—	308
Total Assets	$609	$ —	$ —	$ 609

		Fair Value Measurements Using		
	Carrying Value	Quoted Prices in Active	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)

		Markets for Identical Assets (Level 1)		
	December 31, 2017 (In thousands)			
Assets:				
Impaired loans				
Commercial:				
Secured by real estate	$ 109	$ —	$ —	$ 109
Commercial real estate	192	—	—	192
Residential real estate	296	—	—	296
Total Assets	$ 597	$ —	$ —	$ 597

Collateral-dependent impaired loans measured for impairment using the fair value of the collateral had a recorded investment value of $692,000, resulting in an increase of the allocation for loan losses of $83,000 for the year ended December 31, 2018.

Collateral-dependent impaired loans measured for impairment using the fair value of the collateral had a recorded investment value of $624,000, resulting in an increase of the allocation for loan losses of $27,000 for the year ended December 31, 2017.

There was no OREO at December 31, 2018 or 2017.

The Corporation does not record loans at fair value on a recurring basis. However, from time to time, the Corporation records non-recurring fair value adjustments to collateral dependent loans to reflect impairment. The Corporation measures impairment of collateralized loans based on the estimated fair value of the collateral less estimated costs to sell the collateral, incorporating assumptions that experienced parties might use in estimating the value of such collateral (Level 3 inputs). At the time a loan is considered impaired, it is valued at the lower of cost or fair value. Generally, impaired loans carried at fair value have been partially charged-off or receive specific allocations of the allowance for loan losses. For collateral dependent loans, fair value is commonly based on real estate appraisals. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. In the appraisal process, the independent appraiser routinely adjusts for differences between the comparable sales and income data available. Such adjustments typically result in a Level 3 classification of the inputs for determining fair value. Methods for valuing non-real estate collateral include using an appraisal, the net book value recorded for the collateral on the borrower's financial statements, or aging reports. Collateral is then adjusted or discounted based on management's historical knowledge, changes in market conditions from the time of the valuation, and management's expertise and knowledge of the borrower and borrower's business, resulting in a Level 3 fair value classification. Impaired loans are evaluated on a quarterly basis for additional impairment and adjusted accordingly.

Appraisals are generally obtained to support the fair value of collateral. Appraisals for collateral-dependent impaired loans are performed by licensed appraisers whose qualifications and licenses have been reviewed and verified by the Corporation. The Corporation utilizes a third party to order appraisals and, once received, reviews the assumptions and approaches utilized in the appraisal as well as the resulting fair value in comparison with independent data sources such as recent market data or industry-wide statistics.

Real estate appraisals typically incorporate measures such as recent sales prices for comparable properties. Appraisers may make adjustments to the sales price of the comparable properties as deemed appropriate based on the age, condition or general characteristics of the subject property. Management generally applies a 12% discount to real estate appraised values to cover disposition / selling costs and to reflect the potential price reductions in the market necessary to complete an expedient sale transaction and to factor in the impact of the perception that a transaction being completed by a bank may result in further price reduction pressure.

For the Level 3 assets measured at fair value on a non-recurring basis, the significant unobservable inputs used in the fair value measurements were as follows:

December 31, 2018

Assets	Fair Value	Valuation Technique	Unobservable Inputs	Range
(Dollars in thousands)				
Impaired loans	$ 609	Comparable real estate sales and / or the income approach.	Adjustments for differences between comparable sales and income data available.	5%
			Estimated selling costs.	7%

December 31, 2017

Assets	Fair Value	Valuation Technique	Unobservable Inputs	Range
(Dollars in thousands)				
Impaired loans	$ 597	Comparable real estate sales and / or the income approach.	Adjustments for differences between comparable sales and income data available.	5%
			Estimated selling costs.	7%

Fair value estimates for the Corporation’s financial instruments are summarized below:

		Fair Value Measurements Using		
	Carrying Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
	December 31, 2018 (In thousands)			
Financial assets:				
Cash and cash equivalents	$16,823	$16,823	$ —	$ —
Securities available-for-sale	108,811	—	108,811	—
Securities held-to-maturity	62,308	—	60,997	—
Other Equity Investments	1,648	1,588	60	—
FHLB-NY stock	3,965	N/A	N/A	N/A
Loans, net	725,404	—	—	704,273
Interest rate swap	134	—	134	—
Financial liabilities:				
Deposits	782,091	578,460	201,846	—
FHLB-NY advances	65,700	—	65,477	—
Subordinated Debentures and Subordinated Notes	23,382	—	—	23,441
Interest rate swap	246	—	246	—

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	Carrying Value	Fair Value Measurements Using Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
	December 31, 2017 (In thousands)			
Financial assets:				
Cash and cash equivalents	$21,270	$21,270	$ —	$ —
Securities available-for-sale	109,259	—	109,259	—
Securities held-to-maturity	52,442	—	51,551	—
Other equity investments	3,756	3,696	60	—
FHLB-NY stock	3,715	N/A	N/A	N/A
Mortgage loans held for sale	370	—	—	370
Loans, net	702,561	—	—	714,387
Financial liabilities:				
Deposits	764,099	565,292	197,696	—
FHLB-NY advances	63,760	—	63,340	—
Subordinated Debentures and Subordinated Notes	23,317	—	—	23,478
Interest rate swap	29	—	29	—

The following methods and assumptions were used to estimate the fair value of financial instruments recorded at fair value on a recurring or non-recurring basis not previously described:

Cash and cash equivalents – The carrying amount approximates fair value and is classified as Level 1.

FHLB-NY stock – It is not practicable to determine the fair value of FHLB-NY stock due to restrictions placed on the transferability of the stock.

Mortgage loans held for sale – Loans in this category have been committed for sale to third party investors at the current carrying amount resulting in a Level 3 classification.

Loans, net – Fair values are estimated for portfolios of loans with similar financial characteristics. Loans are segregated by type such as residential and commercial mortgages, commercial and other installment loans. Fair value of loans at December 31, 2018 is based on an exit price model as required by ASU 2016-01 taking into account inputs such as probability of default and loss given default assumptions. As of December 31, 2017, the fair value of loans is estimated by discounting cash flows using estimated market discount rates which reflect the credit and interest rate risk inherent in the loans resulting in a Level 3 classification. Fair values estimated in this manner do not fully incorporate an exit-price approach to fair value, but instead are based on a comparison to current market rates for comparable loans.

Deposits – The fair value of deposits, with no stated maturity, such as noninterest-bearing demand deposits, savings, NOW and money market accounts, is equal to the amount payable on demand resulting in a Level 1 classification. The fair value of certificates of deposit is based on the discounted value of cash flows resulting in a Level 2 classification.

The discount rate is estimated using market discount rates which reflect interest rate risk inherent in the certificates of deposit. Fair values estimated in this manner do not fully incorporate an exit-price approach to fair value, but instead are based on a comparison to current market rates for comparable deposits.

FHLB-NY advances – With respect to FHLB-NY borrowings, the fair value is based on the discounted value of cash flows. The discount rate is estimated using market discount rates which reflect the interest rate risk and credit risk inherent in the term borrowings resulting in a Level 2 classification.

Subordinated Debentures and Subordinated Notes – The fair value of the Subordinated Debentures and the Subordinated Notes (see Note 8) is based on the discounted value of the cash flows. The discount rate is estimated using market rates which reflect the interest rate and credit risk inherent in the Subordinated Debentures and the Subordinated Notes resulting in a Level 3 classification.

Interest rate swap – The fair value of derivatives, which is included in Accrued Expenses and Other Liabilities on the Consolidated Statements of Financial Condition, are based on valuation models using observable market data as of the measurement date (Level 2).

Commitments to extend credit – The fair value of commitments is estimated using the fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the present credit worthiness of the counter parties. At December 31, 2018 and 2017 the fair value of such commitments were not material.

Limitations

The preceding fair value estimates were made at December 31, 2018 and 2017 based on pertinent market data and relevant information concerning the financial instruments. These estimates do not include any premiums or discounts that could result from an offer to sell at one time the Corporation's entire holdings of a particular financial instrument or category thereof. Since no market exists for a substantial portion of the Corporation's financial instruments, fair value estimates were necessarily based on judgments with respect to future expected loss experience, current economic conditions, risk assessments of various financial instruments, and other factors. Given the subjective nature of these estimates, the uncertainties surrounding them and the matters of significant judgment that must be applied, these fair value estimates cannot be calculated with precision. Modifications in such assumptions could meaningfully alter these estimates.

Since these fair value approximations were made solely for on- and off-balance sheet financial instruments at December 31, 2018 and 2017, no attempt was made to estimate the value of anticipated future business. Furthermore, certain tax implications related to the realization of unrealized gains and losses could have a substantial impact on these fair value estimates and have not been incorporated into the estimates.

Note 17. PARENT COMPANY ONLY

The Corporation was formed in January 1995 as a bank holding company to operate its wholly-owned subsidiary, the Bank. The earnings of the Bank are recognized by the Corporation using the equity method of accounting. Accordingly, the Bank dividends paid reduce the Corporation's investment in the subsidiary. Condensed financial statements are presented below:

Condensed Statements of Financial Condition

	December 31,	
	2018	2017
	(In thousands)	
Assets		
Cash and due from banks	$750	$378
Securities available-for-sale	3,877	3,911
Investment in subsidiary	97,861	91,689
Accrued interest receivable	21	21
Other assets	1,458	1,435
Total assets	$103,967	$97,434
Liabilities and Shareholders' equity		
Subordinated Debentures	$7,217	$7,217
Subordinated Notes	16,165	16,100
Other liabilities	435	452
Shareholders' equity	80,150	73,665
Total liabilities and Shareholders' equity	$103,967	$97,434

Condensed Statements of Income and Comprehensive Income

	Years Ended December 31,	
	2018	2017
	(In thousands)	
Interest income - securities available-for-sale	$94	$76
Dividend income	2,700	2,218
Other income	11	10
Total income	2,805	2,304
Interest expense	1,575	1,492
Other expenses	351	354
Total expenses	1,926	1,846
Income before income tax benefit	879	458
Tax benefit	(381)	(597)
Income before equity in undistributed earnings of subsidiary	1,260	1,055
Equity in undistributed earnings of subsidiary	6,770	2,892
Net income	8,030	3,947
Equity in other comprehensive income (loss)	(715)	160
Total comprehensive income	$7,315	$4,107

Condensed Statements of Cash Flows

	Years Ended December 31,	
	2018	2017
	(In thousands)	
Cash flows from operating activities:		
Net income	$8,030	$3,947
Adjustments to reconcile net income to net cash provided by operating activities:		
Equity in undistributed earnings of subsidiary	(6,770)	(2,892)
Amortization of Subordinated Notes issuance cost	65	65
Restricted stock-forfeited	(122)	—
Gain on calls of securities	—	(1)
Increase in accrued interest receivable	—	(11)
Decrease (increase) in other assets	92	(139)
Increase in other liabilities	4	18
Net cash provided by operating activities	1,299	987
Cash flows from investing activities:		
Purchase of securities available-for-sale	—	(2,999)
Proceeds from calls on securities available-for-sale	—	500
Proceeds from maturities on securities available-for-sale	—	500
Investment in subsidiary bank	—	(16,800)
Net cash used in investing activities	—	(18,799)
Cash flows from financing activities:		
Proceeds from issuance of common stock, net of costs	—	18,860
Restricted stock-forfeited	—	(135)
Cash dividends paid on common stock	(1,040)	(961)
Payment of discount on dividend reinvestment plan	(4)	(5)
Issuance of common stock	117	167
Net cash provided by (used in) financing activities	(927)	17,926
Net decrease in cash and cash equivalents	372	114
Cash and cash equivalents - beginning	378	264
Cash and cash equivalents - ending	$750	$378

Note 18. ACCUMULATED OTHER COMPREHENSIVE INCOME

The components of comprehensive income, both gross and net of tax, are presented for the periods below:

	Years Ended December 31, 2018			December 31, 2017		
	Gross	Tax Effect	Net	Gross	Tax Effect	Net
	(In thousands)					
Net income	$11,050	$(3,020)	$8,030	$8,723	$(4,776)	$3,947
Other comprehensive income:						
Change in unrealized holding gains (losses) on securities available-for-sale	(1,020)	343	(677)	241	(91)	150
Reclassification adjustment for gains in net income	(6)	2	(4)	(1)	—	(1)
Accretion of loss on securities reclassified to held-to-maturity	27	(5)	22	46	(18)	28
Change in fair value of interest rate swap	(128)	40	(88)	(31)	12	(19)
Reclassification adjustment for interest rate swap interest expense in net income	46	(14)	32	2	—	2
Total other comprehensive income	(1,081)	366	(715)	257	(97)	160
Total comprehensive income	$9,969	$(2,654)	$7,315	$8,980	$(4,873)	$4,107

The Corporation, in accordance with ASU No. 2018-02, elected to reclassify the income tax effects of the Tax Act from accumulated other comprehensive income (loss) to retained earnings for the year ended December 31, 2017.

The following table presents the components of accumulated other comprehensive income (loss), net of tax, for the years ended December 31, 2018 and 2017, including the reclassification of income tax effects due to the adoption of ASU No. 2018-02 for the year ended December 31, 2017.

	Year Ended December 31, 2018			
	Components of Accumulated Other Comprehensive Income			Total
	Unrealized Gains / (Losses) on Available-for-Sale (AFS) Securities	Loss on Securities Reclassified from Available-for-Sale to Held-to-Maturity	Unrealized Gains / (Losses) on Derivatives	Accumulated Other Comprehensive Income (Loss)
	(In thousands)			
Balance at December 31, 2017	$(1,303)	$ (60)	$ (21)	$ (1,384)
Other comprehensive income (loss) before reclassifications	(677)	22	(88)	(743)
Amounts reclassified from other comprehensive income	(4)	—	32	28
Other comprehensive income (loss), net	(681)	22	(56)	(715)
Reclassification due to the adoption of ASU No. 2016-01	163	—	—	163
Balance at December 31, 2018	$(1,821)	$ (38)	$ (77)	$ (1,936)

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	Year Ended December 31, 2017 Components of Accumulated Other Comprehensive Income			Total
	Unrealized Gains / (Losses) on Available-for-Sale (AFS) Securities	Loss on Securities Reclassified from Available-for-Sale to Held-to-Maturity	Unrealized Gains / (Losses) on Derivatives	Accumulated Other Comprehensive Income (Loss)
	(In thousands)			
Balance at December 31, 2016	$(1,243)	$ (78)	$ —	$ (1,321)
Other comprehensive income (loss) before reclassifications	150	28	(19)	159
Amounts reclassified from other comprehensive income	(1)	—	2	1
Other comprehensive income, net	149	28	(17)	160
Reclassification of tax effects due to the adoption of ASU No. 2018-02	(209)	(10)	(4)	(223)
Balance at December 31, 2017	$(1,303)	$ (60)	$ (21)	$ (1,384)

The following table presents amounts reclassified from each component of accumulated other comprehensive income on a gross and net of tax basis for the years ended December 31, 2018 and 2017.

Components of Accumulated Other Comprehensive Income (Loss)	Years Ended December 31, 2018	2017	Income Statement Line Item
	(In thousands)		
Unrealized gains on AFS securities before tax	$6	$1	Gains on securities transactions, net
Tax effect	(2)	—	
Total, net of tax	4	1	
Unrealized losses on derivatives before tax	(46)	(2)	Interest expense on derivatives
Tax effect	14	—	
Total, net of tax	(32)	(2)	
Total reclassifications, net of tax	$(28)	$(1)	

Note 19. REVENUE RECOGNITION

Effective January 1, 2018, the Corporation adopted ASU No. 2014-09 (Topic 606) and all subsequent ASUs that modified Topic 606. For further details on Topic 606 see Note 1 - “Significant Accounting Policies - Adoption of New Accounting Standards”. The adoption of Topic 606 did not have any impact on the measurement or recognition of revenue as it does not apply to revenue associated with financial instruments, including revenue from loans and investment securities, which is the Corporation's primary source of revenue. In addition, certain non-interest income streams such as income on bank owned life insurance, gains on securities, and other non-interest income are not in the scope of the guidance. The Corporation’s revenue streams that are within the scope of Topic 606 include service charges on deposit accounts, ATM and card interchange fees, and investment services fees. However, the revenue recognition of these revenue streams did not change upon adoption of Topic 606 as our customer contracts generally do not have performance obligations and fees are assessed and collected as the transaction occurs.

The following table summarizes non-interest income for the periods indicated (in thousands):

	For the Years Ended December 31,	
	2018	2017
	(In thousands)	
Noninterest income		
In-scope of Topic 606:		
Banking service charges and other fees:		
Overdrafts	$728	$671
Interchange	696	646
Other	763	745
Total banking service charges and other fees	2,187	2,062
Miscellaneous	424	416
Total in-scope noninterest income	2,611	2,478
Total out-of-scope noninterest income	806	829
Total noninterest income	$3,417	$3,307

Service Charges on Deposit Accounts: The Corporation earns fees from its deposit customers for transaction-based, account maintenance, and overdraft services. Transaction-based fees, which include services such as ATM use fees, stop payment charges, statement rendering and ACH fees, are recognized at the time the transaction is executed as that is the point in time the Corporation fulfills the customer's request. Account maintenance fees, which relate primarily to monthly maintenance, are earned over the course of a month, representing the period over which the Corporation satisfies the performance obligation. Overdraft fees are recognized at the point in time that the overdraft occurs. Service charges on deposits are withdrawn from the customer's account balance.

Interchange Income: The Corporation earns interchange fees from debit cardholder transactions conducted through the Mastercard payment network. Interchange fees from cardholder transactions represent a percentage of the underlying transaction value and are recognized daily, concurrently with the transaction processing services provided to the cardholder.

Other: The Corporation earns other service charges such as minimum balance fees, stop payment charges, wire transfer fees and fees for utilizing online bill pay payment. These fees are either recognized at the time the service is rendered or monthly.

Miscellaneous: The Corporation earns income from checkbook income, safe deposit box rental income, and referral fee income related to credit cards and merchant services. These fees are either recognized at the time the service is rendered or monthly.

Out-of-scope non-interest income primarily consists of Bank-owned life insurance along with gains and losses on the call and sale of securities, gains and losses on the sale of loans and other real estate, and loan servicing fees. None of these revenue streams are subject to the requirements of Topic 606.

Note 20. QUARTERLY FINANCIAL DATA (Unaudited)

The following table contains quarterly financial data for the years ended December 31, 2018 and 2017.

	Year Ended December 31, 2018				
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Total
	(In thousands, except per share amounts)				
Interest income	$8,539	$8,868	$9,215	$9,377	$35,999
Interest expense	1,716	1,860	2,013	2,247	7,836
Net interest income before provision for loan losses	6,823	7,008	7,202	7,130	28,163
Provision for loan losses	(335)	(780)	(490)	(10)	(1,615)
Net interest income after provision for loan losses	7,158	7,788	7,692	7,140	29,778
Noninterest income	725	859	837	996	3,417
Noninterest expenses	5,428	5,504	5,554	5,659	22,145
Income before income tax expense	2,455	3,143	2,975	2,477	11,050
Income tax expense	647	842	813	718	3,020
Net income	$1,808	$2,301	$2,162	$1,759	$8,030
Basic and diluted earnings per share	$0.21	$0.27	$0.25	$0.20	$0.93

	Year Ended December 31, 2017				
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Total
	(In thousands, except per share amounts)				
Interest income	$7,424	$7,943	$8,400	$8,463	$32,230
Interest expense	1,244	1,409	1,577	1,628	5,858
Net interest income before provision for loan losses	6,180	6,534	6,823	6,835	26,372
Provision for loan losses	300	260	20	75	655
Net interest income after provision for loan losses	5,880	6,274	6,803	6,760	25,717
Noninterest income	799	813	845	850	3,307
Noninterest expenses	5,114	5,083	5,036	5,068	20,301
Income before income tax expense	1,565	2,004	2,612	2,542	8,723
Income tax expense	574	736	972	2,494	4,776
Net income	$991	$1,268	$1,640	$48	$3,947
Basic and diluted earnings per share	$0.16	$0.16	$0.19	$0.01	$0.50

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

None.

Item 9A. Controls and Procedures

(a) Evaluation of internal controls and procedures

Based on their evaluation as of the end of the period covered by this Annual Report on Form 10-K, our principal executive officer and principal financial officer have concluded that our internal disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934 (the "Exchange Act")) are effective to ensure that information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms.

(b) Management's Report on Internal Control over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting as defined in Rule 13a-15(f) of the Exchange Act. Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements and can only provide reasonable assurance with respect to financial statement preparation. 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.

We assessed the effectiveness of our internal control over financial reporting as of December 31, 2018. In making this assessment, we used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO") in Internal Control—Integrated Framework (2013). Based on our assessment using those criteria, our management (including our principal executive officer and principal accounting officer) concluded that our internal control over financial reporting was effective as of December 31, 2018.

Our independent registered public accounting firm, BDO USA LLP, has audited the Corporation's Consolidated Financial Statements and the effectiveness of the Corporation's internal control over financial reporting as of December 31, 2018. Their report appears in this Annual Report on Form 10-K.

(c) Changes in Internal Controls over Financial Reporting

There were no significant changes in our internal control over financial reporting or in other factors that could significantly affect these controls subsequent to the date of their evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses during the quarter ended December 31, 2018 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Item 9B. Other Information

None.

Part III

Item 10. Directors, Executive Officers and Corporate Governance

The information required to be furnished pursuant to this Item will be set forth in our proxy statement for the 2019 Annual Meeting of Shareholders, and is incorporated herein by reference.

Item 11. Executive Compensation

The information required to be furnished pursuant to this Item will be set forth in our proxy statement for the 2019 Annual Meeting of Shareholders, and is incorporated herein by reference.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

The information required to be furnished pursuant to this Item will be set forth in our proxy statement for the 2019 Annual Meeting of Shareholders, and is incorporated herein by reference.

Item 13. Certain Relationships and Related Transactions, and Director Independence

The information required to be furnished pursuant to this Item will be set forth in our proxy statement for the 2019 Annual Meeting of Shareholders, and is incorporated herein by reference.

Item 14. Principal Accounting Fees and Services

Information concerning principal accountant fees and services under the caption "Fees Billed by our Independent Registered Public Accounting Firm During Fiscal 2018 and Fiscal 2017," in the Proxy Statement for the Corporation's 2019 Annual Meeting of Shareholders is incorporated herein by reference.

Part IV

Item 15. Exhibits and Financial Statement Schedules

(a) (1) Financial Statements

The Consolidated Financial Statements of Stewardship Financial Corporation and Subsidiary included in Item 8:

(2) Financial Statement Schedules

None.

(3) Exhibits

Exhibit Number	Description of Exhibits
3(i)	Amended and Restated Certificate of Incorporation dated May 15, 2017 of Stewardship Financial Corporation (1)
3(ii)	Amended and Restated By-Laws of Stewardship Financial Corporation (2)
4.1	Form of 6.75% Subordinated Note dated as of August 28, 2015 issued by Stewardship Financial Corporation (3)
10.1	Stewardship Financial Corporation 1995 Employee Stock Purchase Plan (4)
10.2	Amended and Restated Director Stock Plan (5)
10.3	Stewardship Financial Corporation Dividend Reinvestment Plan, as amended and restated effective May 21, 2015 (6)
10.4	Stewardship Financial Corporation 2010 Stock Incentive Plan (7)
10.5	Subordinated Note Purchase Agreement dated as of August 28, 2015 between the Corporation and the Purchasers identified therein (8)
10.6	Change in Control Severance Agreement dated November 12, 2013 between the Corporation and Paul Van Ostenbridge, as amended by Acknowledgement and Consent dated March 14, 2019
10.7	Change in Control Severance Agreement dated November 12, 2013 between the Corporation and Claire M. Chadwick, as amended by Acknowledgement and Consent dated March 14, 2019
10.8	Change in Control Severance Agreement dated March 21, 2017 between the Corporation and William S. Clement, as amended by Acknowledgement and Consent dated March 14, 2019
10.9	Change in Control Severance Agreement dated March 21, 2017 between the Corporation and Julie E. Holland, as amended by Acknowledgement and Consent dated March 14, 2019
10.10	Change in Control Severance Agreement dated March 21, 2017 between the Corporation and James H. Shields, as amended by Acknowledgement and Consent dated March 14, 2019
10.11	Change in Control Severance Agreement dated March 21, 2017 between the Corporation and Gail K. Tilstra, as amended by Acknowledgement and Consent dated March 14, 2019
10.12	Supplemental Executive Retirement Agreement dated April 1, 2017 between the Corporation and Paul Van Ostenbridge (9)
10.13	Supplemental Executive Retirement Agreement dated January 1, 2018 between the Corporation and Claire M. Chadwick
10.14	Supplemental Executive Retirement Agreement dated January 1, 2018 between the Corporation and William S. Clement
13	Annual Report to Shareholders for the year ended December 31, 2018
21	Subsidiaries of the Registrant
23.1	Consent of BDO USA, LLP
23.2	Consent of KPMG LLP
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1	Certification of Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101	The following materials from Stewardship Financial Corporation's Annual Report on Form 10-K for the year ended December 31, 2018, formatted in XBRL (Extensible Business Reporting Language): (i) Consolidated Statements of Financial Condition, (ii) Consolidated Statements of Income, (iii) Consolidated Statement of Changes in Shareholders' Equity, (iv) Consolidated Statements of Comprehensive Income, (v) Consolidated Statements of Cash Flows and (vi) Notes to Consolidated Financial Statements (10)

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(1) Incorporated by reference to Exhibit 3.1 to the Corporation's Current Report on Form 8-K, filed May 18, 2017.

(2) Incorporated by reference from Exhibit 3.1(i) to the Corporation’s Annual Report on Form 10-K, filed March 28, 2013.

(3) Incorporated by reference to Exhibit 4.1 to the Corporation’s Current Report on Form 8-K filed with the SEC on September 1, 2015.

(4) Incorporated by reference from Exhibit 4(c) to the Corporation’s Registration Statement on Form S-8, Registration No. 333-20793, filed January 31, 1997.

(5) Incorporated by reference from Exhibit 10(viii) to the Corporation’s Annual Report on Form 10-KSB, filed March 31, 1999.

(6) Incorporated by reference from Exhibit 4.2 to the Corporation’s Registration Statement on Form S-3D, Registration No. 333-204352, filed May 21, 2015.

(7) Incorporated by reference from Exhibit 10.1 to the Corporation’s Current Report on Form 8-K, filed May 19, 2010.

(8) Incorporated by reference to Exhibit 10.1 to the Corporation’s Current Report on Form 8-K filed with the SEC on September 1, 2015.

(9) Incorporated by reference from Exhibit 10.12 to the Corporation's Annual Report on Form 10-K, filed March 23, 2018.

(10) This exhibit shall not be deemed “filed” for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, or otherwise subject to the liability of that section, nor shall it be deemed incorporated by reference into any filing under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended, whether made before or after the date hereof and irrespective of any general incorporation language in any filing, except to the extent the Corporation specifically incorporates it by reference.

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.

STEWARDSHIP FINANCIAL
CORPORATION

By: /s/ Paul Van Ostenbridge
Paul Van Ostenbridge
Chief Executive Officer and Director

Dated: March 15, 2019

POWER OF ATTORNEY

KNOW ALL PERSONS BY THESE PRESENTS, that each of the undersigned constitutes and appoints Paul Van Ostenbridge and Claire M. Chadwick, and each of them, as attorneys-in-fact and agents, with full power of substitution and re-substitution, for and in the name, place and stead of the undersigned, in any and all capacities, to sign any and all amendments to this Annual Report on Form 10-K, and to file the same, with all exhibits thereto and all other documents in connection therewith, with the Securities and Exchange Commission, granting unto said attorneys-in-fact and agents full power and authority to do and perform each and every act and thing requisite and necessary to be done in and about the premises, as fully to all intents and purposes as the undersigned might or could do in person, hereby ratifying and confirming all that each of said attorney-in-fact or substitute or substitutes, may lawfully do or cause to be done by virtue hereof.

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.

Name	Title	Date
/s/ Paul Van Ostenbridge Paul Van Ostenbridge	Chief Executive Officer and Director (Principal Executive Officer)	March 15, 2019
/s/ Claire M. Chadwick Claire M. Chadwick	Chief Financial Officer (Principal Financial Officer and (Principal Accounting Officer)	March 15, 2019
/s/ Wayne Aoki Wayne Aoki	Director	March 15, 2019
/s/ Richard W. Culp Richard W. Culp	Director	March 15, 2019
/s/ William Hanse William Hanse	Director	March 15, 2019
/s/ Margo Lane Margo Lane	Director	March 15, 2019
/s/ John C. Scoccola John C. Scoccola	Secretary and Director	March 15, 2019
/s/ John L. Steen John L. Steen	Director	March 15, 2019
/s/ William J. Vander Eems William J. Vander Eems	Director	March 15, 2019
/s/ Kim Vierheilig Kim Vierheilig	Director	March 15, 2019
/s/ Michael Westra Michael Westra	Chairman	March 15, 2019
/s/ Howard Yeaton Howard Yeaton	Vice Chairman	March 15, 2019