

CONSUMERS BANCORP INC /OH/

Form 10-K

September 12, 2018

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**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**WASHINGTON, D.C. 20549**

**FORM 10-K**

**Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**

For the fiscal year ended June 30, 2018

Commission File No. 033-79130

**CONSUMERS BANCORP, INC.**

**(Exact name of registrant as specified in its charter)**

OHIO 34-1771400  
**(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification No.)**

614 East Lincoln Way,

P.O. Box 256, Minerva, Ohio 44657

(330) 868-7701

**(Address, including zip code, and telephone number, including area code, of registrant's principal executive offices)**

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

**Securities registered pursuant Section 12(g) of the Act:** Common Shares, no par value

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

Yes    No

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

Yes    No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.    Yes    No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, 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    No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) 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.

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

|   |                           |
|---|---------------------------|
| Large accelerated filer   | Accelerated filer         |
| Non-accelerated filer (Do not check if small reporting company) | Smaller reporting company |
| Emerging growth company   |                           |

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended 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

Based on the closing sales price on December 31, 2017, the aggregate market value of the voting and non-voting stock held by non-affiliates of the Registrant was approximately \$41,952,356.

The number of shares outstanding of the Registrant's common stock, without par value was 2,729,644 at September 12, 2018.

**DOCUMENTS INCORPORATED BY REFERENCE**

Certain specifically designated portions of Consumers Bancorp, Inc.'s definitive Proxy Statement, dated September 12, 2018, for its 2018 Annual Meeting of Shareholders are incorporated by reference into Part III of this Form 10-K.

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**TABLE OF CONTENTS**

**PART I**

|                                   |   |
|-----------------------------------|---|
| ITEM 1—BUSINESS                   | 3 |
| ITEM 1A—RISK FACTORS              | 6 |
| ITEM 1B—UNRESOLVED STAFF COMMENTS | 6 |
| ITEM 2—PROPERTIES                 | 6 |
| ITEM 3—LEGAL PROCEEDINGS          | 6 |
| ITEM 4—MINE SAFETY DISCLOSURES    | 6 |

**PART II**

|   |    |
|---|----|
| ITEM 5—MARKET FOR REGISTRANT’S COMMON EQUITY, RELATED SHAREHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES | 7  |
| ITEM 6—SELECTED FINANCIAL DATA  | 7  |
| ITEM 7—MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS                        | 8  |
| ITEM 7A—QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK  | 19 |
| ITEM 8—FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA  | 20 |
| ITEM 9—CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE                         | 52 |
| ITEM 9A—CONTROLS AND PROCEDURES   | 52 |
| ITEM 9B—OTHER INFORMATION   | 52 |

**PART III**

|  |    |
|--|----|
| ITEM 10—DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE   | 53 |
| ITEM 11—EXECUTIVE COMPENSATION   | 53 |
| ITEM 12—SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED SHAREHOLDER MATTERS | 53 |
| ITEM 13—CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE                      | 53 |
| ITEM 14—PRINCIPAL ACCOUNTING FEES AND SERVICES   | 54 |

**PART IV**

|   |    |
|---|----|
| ITEM 15—EXHIBITS, FINANCIAL STATEMENT SCHEDULES | 54 |
|---|----|

## **PART I**

### **ITEM 1—BUSINESS**

#### **Business**

Consumers Bancorp, Inc. (Corporation) is a bank holding company under the Bank Holding Company Act of 1956, as amended, and is a registered bank holding company, and was incorporated under the laws of the State of Ohio in 1994. In February 1995, the Corporation acquired all the issued and outstanding capital stock of Consumers National Bank (Bank), a bank chartered under the laws of the United States of America. The Corporation's activities have been limited primarily to holding the common stock of the Bank.

Since 1965, the Bank's main office has been serving the Minerva, Ohio, and surrounding areas from its location at 614 East Lincoln Way, Minerva, Ohio. The Bank's business involves attracting deposits from businesses and individual customers and using such deposits to originate commercial, mortgage and consumer loans in its market area, consisting primarily of Carroll, Columbiana, Jefferson, Stark, Summit, Wayne and contiguous counties in Ohio. The Bank currently has fourteen branch locations and one loan production office. The Bank also invests in securities consisting primarily of obligations of U.S. government-sponsored entities, municipal obligations and mortgage-backed securities issued by Fannie Mae, Freddie Mac and Ginnie Mae.

#### **Supervision and Regulation**

The Corporation and the Bank are subject to regulation by the Securities and Exchange Commission (SEC), the Board of Governors of the Federal Reserve System (Federal Reserve Board), the Office of the Comptroller of the Currency (OCC) and other federal and state regulators. The regulatory framework is intended primarily for the protection of depositors, federal deposit insurance funds and the banking system as a whole and not for the protection of shareholders and creditors. Earnings and dividends of the Corporation are affected by state and federal laws and regulations and by policies of various regulatory authorities. Changes in applicable law or in the policies of various regulatory authorities could affect materially the business and prospects of the Corporation and the Bank. The following describes selected federal and state statutory and regulatory provisions that have, or could have, a material impact on the Corporation. The following discussion of supervision and regulation is qualified in its entirety by reference to the statutory and regulatory provisions discussed.

## Regulation of the Corporation

**The Bank Holding Company Act:** As a bank holding company, the Corporation is subject to regulation under the Bank Holding Company Act of 1956, as amended (BHCA), and the examination and reporting requirements of the Federal Reserve Board. Under the BHCA, the Corporation is subject to periodic examination by the Federal Reserve Board and is required to file periodic reports regarding its operations and any additional information that the Federal Reserve Board may require.

The BHCA generally limits the activities of a bank holding company to banking, managing or controlling banks, furnishing services to or performing services for its subsidiaries and engaging in any other activities that the Federal Reserve Board has determined to be so closely related to banking or to managing or controlling banks as to be a proper incident to those activities. In addition, the BHCA requires every bank holding company to obtain the approval of the Federal Reserve Board prior to acquiring substantially all the assets of any bank, acquiring direct or indirect ownership or control of more than 5% of the voting shares of a bank or merging or consolidating with another bank holding company.

Under Federal Reserve Board policy, a bank holding company is expected to act as a source of financial strength to each subsidiary bank and to commit resources to support those subsidiary banks. Under this policy, the Federal Reserve Board may require a bank holding company to contribute additional capital to an undercapitalized subsidiary bank and may disapprove of the payment of dividends to shareholders if the Federal Reserve Board believes the payment of such dividends would be an unsafe or unsound practice. The Federal Reserve Board has extensive enforcement authority over bank holding companies for violations of laws and regulations and unsafe or unsound practices.

**Privacy Provisions of Gramm-Leach-Bliley Act:** The Gramm-Leach-Bliley Act of 1999 contains extensive provisions on a customer's right to privacy of non-public personal information. Under these provisions, a financial institution must provide to its customers the institution's policies and procedures regarding the handling of customers' non-public personal information. Except in certain cases, an institution may not provide personal information to unaffiliated third parties unless the institution discloses that such information may be disclosed and the customer is given the opportunity to opt out of such disclosure. The Corporation and the Bank are also subject to certain state laws that deal with the use and distribution of non-public personal information.

**Sarbanes-Oxley Act:** The Sarbanes-Oxley Act of 2002 contains important requirements for public companies in the areas of financial disclosure and corporate governance. In accordance with section 302(a) of the Sarbanes-Oxley Act, written certifications by the Corporation's Chief Executive Officer and Chief Financial Officer are required. These certifications attest that the Corporation's quarterly and annual reports filed with the SEC do not contain any untrue statement of a material fact or omit to state a material fact.



## Regulation of the Bank

As a national bank, Consumers National Bank is subject to regulation, supervision and examination by the OCC and by the Federal Deposit Insurance Corporation (FDIC). These examinations are designed primarily for the protection of the depositors of the Bank.

**Dividend Restrictions:** Dividends from the Bank are the primary source of funds for payment of dividends to our shareholders. However, there are statutory limits on the amount of dividends the Bank can pay without regulatory approval. Under regulations promulgated by the OCC, the Bank may not declare a dividend in excess of its undivided profits. Additionally, the Bank may not declare a dividend if the total amount of all dividends, including the proposed dividend, declared by the Bank in any calendar year exceeds the total of its retained net income of that year to date, combined with its retained net income of the two preceding years, unless the dividend is approved by the OCC. The Bank may not declare or pay any dividend if, after making the dividend, the Bank would be “undercapitalized,” as defined in the federal regulations.

**FDIC:** The FDIC is an independent federal agency, which insures the deposits of federally insured banks and savings associations up to certain prescribed limits and safeguards the safety and soundness of financial institutions. The deposits of the Bank are subject to the deposit insurance assessments of the Bank Insurance Fund of the FDIC. Under the FDIC’s deposit insurance assessment system, the assessment rate for any insured institution varies according to regulatory capital levels of the institution and other factors such as supervisory evaluations.

The FDIC is authorized to prohibit any insured institution from engaging in any activity that poses a serious threat to the insurance fund and may initiate enforcement actions against banks, after first giving the institution’s primary regulatory authority an opportunity to take such action. The FDIC may also terminate the deposit insurance of any institution that has engaged in or is engaging in unsafe or unsound practices, is in an unsafe or unsound condition to continue operations or has violated any applicable law, order or condition imposed by the FDIC.

**Risk-Based Capital Requirements:** The Federal Reserve Board and the OCC employ similar risk-based capital guidelines in their examination and regulation of bank holding companies and national banks. The Corporation meets the definition of a Small Bank Holding Company and, therefore, is exempt from consolidated risk-based and leverage capital adequacy guidelines for bank holding companies. The guidelines involve a process of assigning various risk weights to different classes of assets, then evaluating the sum of the risk-weighted balance sheet structure against the capital base. If capital falls below the minimum levels established by the guidelines, the bank holding company or bank may be denied approval to acquire or establish additional banks or non-bank businesses or to open new facilities. In addition, failure to satisfy capital guidelines could subject a banking institution to a variety of enforcement actions by federal bank regulatory authorities, including the termination of deposit insurance by the FDIC and a prohibition on the acceptance of “brokered deposits.”



The Basel III capital requirements for U.S. banking organizations became effective on January 1, 2015. Under Basel III, the Bank is required to maintain a minimum common equity Tier 1 capital ratio of 4.5%, a Tier 1 capital ratio of 6%, a total capital ratio of 8%, and a Tier 1 leverage ratio of 4%. Basel III also established a “capital conservation buffer” of 2.5% above the new regulatory minimum capital requirements, which must consist entirely of common equity Tier 1 capital and began being phased in beginning in January 2016 at 0.625% of risk-weighted assets and will increase by that amount each year until fully implemented in January 2019. The capital conservation buffer is designed to absorb losses during periods of economic stress. Banking institutions with a common equity Tier 1 ratio to risk-weighted assets above the minimum but below the conservation buffer will face constraints on dividends, equity repurchases, and compensation based on the amount of the shortfall.

The OCC and the FDIC may take various corrective actions against any undercapitalized bank and any bank that fails to submit an acceptable capital restoration plan or fails to implement a plan accepted by the OCC or the FDIC. These powers include, but are not limited to, requiring the institution to be recapitalized, prohibiting asset growth, restricting interest rates paid, requiring prior approval of capital distributions by any bank holding company that controls the institution, requiring divestiture by the institution of its subsidiaries or by the holding company of the institution itself, requiring new election of directors, and requiring the dismissal of directors and officers. The OCC’s final supervisory judgment concerning an institution’s capital adequacy could differ significantly from the conclusions that might be derived from the absolute level of an institution’s risk-based capital ratios. Therefore, institutions generally are expected to maintain risk-based capital ratios that exceed the minimum ratios. At June 30, 2018, the Bank exceeded minimum regulatory capital requirements to be considered well-capitalized.

**Dodd-Frank Wall Street Reform and Consumer Protection Act:** The Dodd-Frank Act created many new restrictions and an expanded framework of regulatory oversight for financial institutions, including depository institutions. The Dodd-Frank Act centralized responsibility for consumer financial protection by creating a new agency, the Consumer Financial Protection Bureau (CFPB), and giving it responsibility for implementing, examining and enforcing compliance with federal consumer protection laws. The CFPB has examination and enforcement authority over all banks with more than \$10 billion in assets, as well as their affiliates. Although the CFPB does not have direct supervisory authority over banks with less than \$10 billion in assets, the CFPB has broad rulemaking authority for a wide range of consumer financial laws that apply to all banks, including, among other things, the authority to prohibit “unfair, deceptive or abusive” acts and practices. Abusive acts or practices are defined as those that materially interfere with a consumer’s ability to understand a term or condition of a consumer financial product or service or take unreasonable advantage of a consumer’s (i) lack of financial savvy, (ii) inability to protect himself in the selection or use of consumer financial products or services, or (iii) reasonable reliance on a covered entity to act in the consumer’s interests. The Corporation is closely monitoring all relevant sections of the Dodd-Frank Act to ensure continued compliance with these regulatory requirements and assess their potential impact on our business.

**Interstate Banking and Branching:** The Interstate Banking and Branch Efficiency Act of 1995 has eased restrictions on interstate expansion and consolidation of banking operations by, among other things: (i) permitting interstate bank acquisitions regardless of host state laws, (ii) permitting interstate merger of banks unless specific states have opted out of this provision, and (iii) permitting banks to establish new branches outside the state provided the law of the host state specifically allows interstate bank branching.

**Community Reinvestment Act:** The Community Reinvestment Act requires depository institutions to assist in meeting the credit needs of their market areas, including low- and moderate-income areas, consistent with safe and sound banking practices. Under this Act, each institution is required to adopt a statement for each of its market areas describing the depository institution’s efforts to assist in its community’s credit needs. Depository institutions are periodically examined for compliance and assigned ratings. Banking regulators consider these ratings when considering approval of a proposed transaction by an institution.

**USA Patriot Act:** In 2001, Congress enacted the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (Patriot Act). The Patriot Act is designed to deny terrorists and criminals the ability to obtain access to the United States’ financial system and has significant implications for depository institutions, brokers, dealers, and other businesses involved in the transfer of money. The Patriot Act mandates that financial services companies implement additional policies and procedures with respect to additional measures designed to address any or all of the following matters: money laundering, terrorist financing, identifying and reporting suspicious activities and currency transactions, and currency crimes.

**Cybersecurity:** In March 2015, federal regulators issued two related statements regarding cybersecurity. One statement indicates that financial institutions should design multiple layers of security controls to establish lines of defense and to ensure that their risk management processes also address the risk posed by compromised customer credentials, including security measures to reliably authenticate customers accessing internet-based services of the

financial institution. The other statement indicates that a financial institution's management is expected to maintain sufficient business continuity planning processes to ensure the rapid recovery, resumption and maintenance of the institution's operations after a cyberattack involving destructive malware. A financial institution is also expected to develop appropriate processes to enable recovery of data and business operations and address rebuilding network capabilities and restoring data if the institution or its critical service providers fall victim to this type of cyberattack.

In the ordinary course of business, electronic communications and information systems are relied upon to conduct operations, to deliver services to customers and to store sensitive data. The Corporation employs a variety of preventative and detective tools to monitor, block, and provide alerts regarding suspicious activity, as well as to report on any suspected advanced persistent threats. Risks and exposures related to cybersecurity attacks are expected to remain high for the foreseeable future due to the rapidly evolving nature and sophistication of these threats, increasing volume of attacks, as well as due to the expanding use of internet banking, mobile banking and other technology-based products and services by the Corporation and its customers.

## **Employees**

As of June 30, 2018, the Bank employed 114 full-time and 25 part-time employees. None of the employees are represented by a collective bargaining group. Management considers its relations with employees to be good.

## Available Information

The Corporation files annual, quarterly, and current reports, proxy statements, and other information with the SEC. These filings are available to the public over the Internet at the SEC's website at [www.sec.gov](http://www.sec.gov). Shareholders may also read and copy any document that the Corporation files at the SEC's public reference room located at 100 F Street, NE, Washington, DC 20549. Shareholders may call the SEC at 1-800-SEC-0330 for further information on the public reference room.

The Corporation's reports on Forms 10-K, 10-Q and 8-K, and amendments to those reports, are available, free of charge, on our website ([www.consumersbank.com](http://www.consumersbank.com)) as soon as reasonably practicable after such reports are filed with or furnished to the SEC. The Corporation's Code of Ethics Policy, which is applicable to all directors, officers and employees of the Corporation, and its Code of Ethics for Principal Financial Officers, which is applicable to the principal executive officer and the principal financial officer, are each available on the Investor Relations section under Corporate Governance of the Corporation's website. The Corporation intends to post amendments to or waivers from either of its Code of Ethics Policies on its website. A printed copy of any of these documents will be provided to any requesting shareholder.

## ITEM 1A—RISK FACTORS

Not applicable for Smaller Reporting Companies.

## ITEM 1B—UNRESOLVED STAFF COMMENTS

None.

## ITEM 2—PROPERTIES

The Bank operates fourteen full service banking facilities and one loan production office (LPO) as noted below:

| Location | Address | Owned | Leased |
|----------|---------|-------|--------|
|----------|---------|-------|--------|

|                |   |   |   |
|----------------|---|---|---|
| Minerva        | 614 E. Lincoln Way, P.O. Box 256, Minerva, Ohio, 44657          | X |   |
| Salem          | 141 S. Ellsworth Avenue, P.O. Box 798, Salem, Ohio, 44460       | X |   |
| Waynesburg     | 8607 Waynesburg Drive SE, P.O. Box 746, Waynesburg, Ohio, 44688 | X |   |
| Hanoverton     | 30034 Canal Street, P.O. Box 178, Hanoverton, Ohio, 44423       | X |   |
| Carrollton     | 1017 Canton Road NW, Carrollton, Ohio, 44615                    |   | X |
| Alliance       | 610 West State Street, Alliance, Ohio, 44601                    |   | X |
| Lisbon         | 7985 Dickey Drive, Lisbon, Ohio 44432                           | X |   |
| Louisville     | 1111 N. Chapel Street, Louisville, Ohio 44641                   | X |   |
| East Canton    | 440 W. Noble, East Canton, Ohio, 44730                          | X |   |
| Malvern        | 4070 Alliance Road, Malvern, Ohio 44644                         |   | X |
| Hartville      | 1215 W. Maple Street, Hartville, Ohio 44632                     | X |   |
| Jackson-Belden | 4026 Dressler Road NW, Canton, Ohio 44718                       | X |   |
| Bergholz       | 256 2nd Street, Bergholz, Ohio 43908                            |   | X |
| Fairlawn       | 3680 Embassy Parkway Suite B, Fairlawn, Ohio 44333              |   | X |
| Wooster LPO    | 146 East Liberty Street, Wooster, Ohio 44691                    |   | X |

The Bank considers its physical properties to be in good operating condition and suitable for the purposes for which they are being used. In management's opinion, all properties owned and operated by the Bank are adequately insured.

### ITEM 3—LEGAL PROCEEDINGS

The Corporation is not a party to any pending material legal or administrative proceedings, other than ordinary routine litigation incidental to the business of the Corporation. Further, there are no material legal proceedings in which any director, executive officer, principal shareholder or affiliate of the Corporation is a party or has a material interest therein that is adverse to the Corporation. No routine litigation in which the Corporation is involved is expected to have a material adverse impact on the financial position or results of operations of the Corporation.

### ITEM 4—MINE SAFETY DISCLOSURES

None.

**PART II****ITEM 5—MARKET FOR REGISTRANT’S COMMON EQUITY, RELATED SHAREHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES**

The Corporation had 2,729,644 common shares outstanding on June 30, 2018 with 740 shareholders of record and an estimated 504 additional beneficial holders whose stock was held in nominee name. Attention is directed to Item 12 in this Form 10-K for information regarding the Corporation’s equity incentive plans, which information is incorporated herein by reference.

The common shares of Consumers Bancorp, Inc. are traded on the over-the-counter bulletin board. The following quoted market prices reflect inter-dealer prices, without adjustments for retail markups, markdowns, or commissions and may not represent actual transactions. The market prices represent highs and lows reported during the applicable quarterly period.

| <b><u>Quarter Ended</u></b>   | <b>September<br/>30,<br/>2017</b> | <b>December<br/>31,<br/>2017</b> | <b>March<br/>31,<br/>2018</b> | <b>June<br/>30,<br/>2018</b> |
|-------------------------------|-----------------------------------|----------------------------------|-------------------------------|------------------------------|
| High                          | \$ 21.00                          | \$ 21.85                         | \$21.15                       | \$25.00                      |
| Low                           | 18.51                             | 20.26                            | 20.00                         | 20.25                        |
| Cash dividends paid per share | 0.12                              | 0.125                            | 0.125                         | 0.125                        |

| <b><u>Quarter Ended</u></b>   | <b>September<br/>30,<br/>2016</b> | <b>December<br/>31,<br/>2016</b> | <b>March<br/>31,<br/>2017</b> | <b>June<br/>30,<br/>2017</b> |
|-------------------------------|-----------------------------------|----------------------------------|-------------------------------|------------------------------|
| High                          | \$ 16.65                          | \$ 17.25                         | \$18.75                       | \$19.37                      |
| Low                           | 15.46                             | 15.30                            | 15.85                         | 17.75                        |
| Cash dividends paid per share | 0.12                              | 0.12                             | 0.12                          | 0.12                         |

Management does not have knowledge of the prices paid in all transactions and has not verified the accuracy of those prices that have been reported. Because of the lack of an established market for the Corporation’s common shares, these prices may not reflect the prices at which the common shares would trade in an active market.

The Corporation’s management is currently committed to continuing to pay regular cash dividends; however, there can be no assurance as to future dividends because they are dependent on the Corporation’s future earnings, capital requirements and financial condition. The Corporation’s principal source of funds for dividend payment is dividends

received 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 net profits, combined with the retained net profits of the preceding two years, subject to the capital requirements described above. See Note 1 and Note 11 to the Consolidated Financial Statements and Management's Discussion and Analysis of Financial Condition and Results of Operations for dividend restrictions.

There were no repurchases of the Corporation's securities during the 2018 fiscal year.

**ITEM 6—SELECTED FINANCIAL DATA**

Not applicable for Smaller Reporting Companies.

## ITEM 7—MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

*(Dollars in thousands, except per share data)*

### General

The following is management’s analysis of the Corporation’s financial condition and results of operations as of and for the years ended June 30, 2018 and 2017. This discussion is designed to provide a more comprehensive review of the operating results and financial position than could be obtained from an examination of the financial statements alone. This analysis should be read in conjunction with the consolidated financial statements and related footnotes and the selected financial data included elsewhere in this report.

### Forward-Looking Statements

Certain statements contained in this Annual Report on Form 10-K, which are not statements of historical fact, constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. In addition, all statements set forth in future filings by the Corporation with the SEC, or other public or shareholder communications, or in oral statements made with the approval of an authorized executive officer, that are not historical in nature, including words or phrases such as “will likely result,” “are expected to,” “will continue,” “is anticipated,” “estimate,” “project,” “believe” or similar expressions are intended to identify “forward-looking statements” within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. These forward-looking statements may involve risks and uncertainties that are difficult to predict, may be beyond our control, and could cause actual results to differ materially from those described in such statements. Any such forward-looking statements are made only as of the date of this report or the respective dates of the relevant incorporated documents, as the case may be, and, except as required by law, we undertake no obligation to update these forward-looking statements to reflect subsequent events or circumstances. Factors that could cause actual results for future periods to differ materially from those anticipated or projected include, but are not limited to:

- changes in local, regional and national economic conditions becoming less favorable than we expect, resulting in a deterioration in credit quality of our loan assets, among other things;
- the effects of, and changes in, trade, monetary and fiscal policies and laws, including interest rate policies of the Federal Reserve Board;
- inflation, interest rate, securities market and monetary fluctuations;
- changes in the level of non-performing assets and charge-offs;
- declining asset values impacting the underlying value of collateral;
- the effect of changes in laws and regulations (including laws and regulations concerning taxes, banking, securities and insurance) with which we must comply;



competitive pressures on product pricing and services;  
breaches of security or failures of our technology systems due to technological or other factors and cybersecurity threats;  
changes in the reliability of our vendors, internal control systems or information systems;  
our ability to attract and retain qualified employees;  
changes in accounting policies, rules and interpretations;  
unanticipated changes in our liquidity position, including, but not limited to, changes in the cost of liquidity and our ability to find alternative funding sources; and  
changes in consumer spending, borrowing and savings habits.

The risks and uncertainties identified above are not the only risks we face. Additional risks and uncertainties not presently known to us or that we currently believe to be immaterial also may adversely affect us. Should any known or unknown risks and uncertainties develop into actual events, those developments could have material adverse effects on our business, financial condition and results of operations.

## **Overview**

Consumers Bancorp, Inc., a bank holding company incorporated under the laws of the State of Ohio, owns all the issued and outstanding capital stock of Consumers National Bank, a bank chartered under the laws of the United States of America. The Corporation's activities have been limited primarily to holding the common stock of the Bank. The Bank's business involves attracting deposits from businesses and individual customers and using such deposits to originate commercial, mortgage and consumer loans in its market area, consisting primarily of Carroll, Columbiana, Jefferson, Stark, Summit, Wayne and contiguous counties in Ohio. The Bank also invests in securities consisting primarily of U.S. government-sponsored entities, municipal obligations, mortgage-backed and collateralized mortgage obligations issued by Fannie Mae, Freddie Mac and Ginnie Mae.

**Comparison of Results of Operations for the Years Ended June 30, 2018 and June 30, 2017**

**Net Income.** Net income was \$3,581 for fiscal year 2018 compared with \$2,994 for fiscal year 2017. The following key factors summarize our results of operations for the year ended June 30, 2018 compared with the same prior year period:

net interest income increased by \$1,427, or 9.9%, in fiscal year 2018, primarily as a result of an increase in average loans receivable;  
 loan loss provision expense in fiscal year 2018 declined by \$286 and totaled \$310 in 2018 compared with \$596 in 2017;  
 total other income increased by \$141, or 4.3% in fiscal year 2018;  
 total other expenses increased by \$759, or 5.6% in fiscal year 2018; and  
 the enactment of the Tax Cuts and Jobs Act (Tax Act) resulted in a charge to income tax expense of \$348 in conjunction with writing down the Corporation's net deferred tax assets in fiscal year 2018.

Return on average equity and return on average assets were 8.15% and 0.75%, respectively, for the 2018 fiscal year-to-date period compared with 6.89% and 0.67%, respectively, for the same period last year.

**Net Interest Income.** Net interest income, the difference between interest income earned on interest-earning assets and interest expense incurred on interest-bearing liabilities, is the largest component of the Corporation's earnings. Net interest income is affected by changes in the volumes, rates and composition of interest-earning assets and interest-bearing liabilities. Net interest margin is calculated by dividing net interest income on a fully tax equivalent basis (FTE) by total interest-earning assets. FTE income includes tax-exempt income, restated to a pre-tax equivalent, based on the statutory federal income tax rate. The federal income tax rate in effect for the 2018 fiscal year was 27.55% and for the 2017 fiscal year was 34.0%. With the enactment of the Tax Act, the statutory tax rate was changed in the second quarter of fiscal year 2018 to 27.55% by using a blended rate of the new 21.0% federal rate that went into effect on January 1, 2018 and the previous federal rate of 34.0%. All average balances are daily average balances. Non-accruing loans are included in average loan balances.

| <b><u>Net Interest Income Year ended June 30,</u></b> | <b>2018</b> | <b>2017</b> |
|---|-------------|-------------|
| Net interest income                                   | \$ 15,886   | \$ 14,459   |
| Taxable equivalent adjustments to net interest        | 543         | 769         |
| Net interest income, fully taxable equivalent         | \$ 16,429   | \$ 15,228   |
| Net interest margin                                   | 3.55 %      | 3.51 %      |
| Taxable equivalent adjustment                         | 0.12        | 0.18        |
| Net interest margin, fully taxable equivalent         | 3.67 %      | 3.69 %      |

FTE net interest income for the 2018 fiscal year was \$16,429, an increase of \$1,201 or 7.9%, from \$15,228 in the 2017 fiscal year. The Corporation's tax equivalent net interest margin for the year ended June 30, 2018 was 3.67% and for the year ended 2017 was 3.69%. FTE interest income for the 2018 fiscal year was \$18,100, an increase of \$1,764, or 10.8%, from \$16,336 in the 2017 fiscal year. Growth of \$27,647, or 10.3%, in average loans receivable positively impacted interest income as well as an increase in the yield on average interest-earning assets. Interest expense for the 2018 fiscal year was \$1,671, an increase of \$563, or 50.8%, from \$1,108 in the 2017 fiscal year. This was mainly the result of an increase in short-term rates impacting the rates paid on savings, short-term borrowings and time deposits as well as a \$27,961, or 9.5%, growth in total interest-bearing liabilities.

**Average Balance Sheet and Net Interest Margin**

|  | <b>2018</b>        |          |                | <b>2017</b>        |          |                |
|--|--------------------|----------|----------------|--------------------|----------|----------------|
|  | Average<br>Balance | Interest | Yield/<br>Rate | Average<br>Balance | Interest | Yield/<br>Rate |
| <b>Interest earning assets:</b>  |                    |          |                |                    |          |                |
| Taxable securities   | \$83,915           | \$1,997  | 2.36 %         | \$77,291           | \$1,678  | 2.19 %         |
| Nontaxable Securities (1)  | 60,072             | 1,996    | 3.34           | 60,036             | 2,176    | 3.68           |
| Loans receivable (1)   | 295,095            | 13,956   | 4.73           | 267,448            | 12,360   | 4.62           |
| Interest bearing deposits and federal funds sold                                       | 8,546              | 151      | 1.77           | 9,213              | 122      | 1.32           |
| Total interest earning assets  | 447,628            | 18,100   | 4.04 %         | 413,988            | 16,336   | 3.96 %         |
| Noninterest earning assets   | 31,449             |          |                | 29,602             |          |                |
| Total assets   | \$479,077          |          |                | \$443,590          |          |                |
| <b>Interest bearing liabilities:</b>   |                    |          |                |                    |          |                |
| Interest bearing demand  | \$57,272           | \$115    | 0.20 %         | \$49,832           | \$75     | 0.15 %         |
| Savings  | 155,000            | 355      | 0.23           | 141,279            | 187      | 0.13           |
| Time deposits  | 71,404             | 740      | 1.04           | 66,761             | 530      | 0.79           |
| Short-term borrowings  | 24,422             | 240      | 0.98           | 21,053             | 90       | 0.43           |
| FHLB advances  | 13,428             | 221      | 1.65           | 14,640             | 226      | 1.54           |
| Total interest-bearing liabilities   | 321,526            | 1,671    | 0.52 %         | 293,565            | 1,108    | 0.38 %         |
| Noninterest-bearing liabilities  | 113,595            |          |                | 106,578            |          |                |
| Total liabilities  | 435,121            |          |                | 400,143            |          |                |
| Shareholders' equity   | 43,956             |          |                | 43,447             |          |                |
| Total liabilities and shareholders' equity   | \$479,077          |          |                | \$443,590          |          |                |
| Net interest income, interest rate spread (1)  |                    | \$16,429 | 3.52 %         |                    | \$15,228 | 3.58 %         |
| Net interest margin (net interest as a percent of average interest earning assets) (1) |                    |          | 3.67 %         |                    |          | 3.69 %         |
| Federal tax exemption on non-taxable securities and loans included in interest income  |                    | \$543    |                |                    | \$769    |                |
| Average interest earning assets to interest bearing liabilities                        |                    |          | 139.22 %       |                    |          | 141.02 %       |

(1) Calculated on a fully taxable equivalent basis utilizing a statutory federal income tax rate of 27.55% in the 2018 fiscal year and 34.0% in the 2017 fiscal year

The following table presents the changes in the Corporation's interest income and interest expense resulting from changes in interest rates and changes in the volume of interest-earning assets and interest-bearing liabilities. Changes attributable to both rate and volume that cannot be segregated have been allocated in proportion to the changes due to rate and volume.

## INTEREST RATES AND INTEREST DIFFERENTIAL

|                               | 2018 Compared to 2017 |                      |                    | 2017 Compared to 2016 |                      |                    |
|-------------------------------|-----------------------|----------------------|--------------------|-----------------------|----------------------|--------------------|
|                               | Increase / (Decrease) |                      |                    | Increase / (Decrease) |                      |                    |
|                               | Total Change          | Change due to Volume | Change due to Rate | Total Change          | Change due to Volume | Change due to Rate |
|                               | (In thousands)        |                      |                    |                       |                      |                    |
| Interest earning assets:      |                       |                      |                    |                       |                      |                    |
| Taxable securities            | \$319                 | \$183                | \$136              | \$(202)               | \$(168)              | \$(34)             |
| Nontaxable securities (1)     | (180)                 | 22                   | (202)              | 70                    | 174                  | (104)              |
| Loans receivable (2)          | 1,596                 | 1,302                | 294                | 1,118                 | 1,241                | (123)              |
| Federal funds sold            | 29                    | (9)                  | 38                 | 5                     | (26)                 | 31                 |
| Total interest income         | 1,764                 | 1,498                | 266                | 991                   | 1,221                | (230)              |
| Interest bearing liabilities: |                       |                      |                    |                       |                      |                    |
| Interest bearing demand       | 40                    | 12                   | 28                 | 6                     | 3                    | 3                  |
| Savings deposits              | 168                   | 20                   | 148                | 65                    | 4                    | 61                 |
| Time deposits                 | 210                   | 39                   | 171                | 42                    | 12                   | 30                 |
| Short-term borrowings         | 150                   | 16                   | 134                | 51                    | —                    | 51                 |
| FHLB advances                 | (5)                   | (19)                 | 14                 | 42                    | 121                  | (79)               |
| Total interest expense        | 563                   | 68                   | 495                | 206                   | 140                  | 66                 |
| Net interest income           | \$1,201               | \$1,430              | \$(229)            | \$785                 | \$1,081              | \$(296)            |

(1) Nontaxable income is adjusted to a fully tax equivalent basis utilizing a statutory federal income tax rate of 27.55% in the 2018 fiscal year and 34.0% in the 2017 fiscal year.

(2) Non-accrual loan balances are included for purposes of computing the rate and volume effects although interest on these balances has been excluded.

**Provision for Loan Losses.** The provision for loan losses represents the charge to income necessary to adjust the allowance for loan losses to an amount that represents management's assessment of the estimated probable credit losses in the Corporation's loan portfolio that have been incurred at each balance sheet date. The provision for loan losses was \$310 in fiscal year 2018 compared to \$596 in fiscal year 2017.

For the 2018 fiscal year, net recoveries of \$26 were recorded compared with net charge-offs of \$1,076 for the same period last year. Net charge-offs for the 2017 fiscal year were primarily within the commercial real estate portfolio and included a partial charge-off of \$700 for one credit for which a specific valuation allowance was reserved for in the 2016 fiscal year. The Bank is currently pursuing all legal avenues against the borrowers in an effort to recover a portion of the loss in future periods. The allowance for loan losses as a percentage of loans was 1.07% at June 30, 2018 and 1.13% at June 30, 2017.

Non-performing loans were \$1,090 as of June 30, 2018 and represented 0.34% of total loans. This compared with \$1,187, or 0.44% of total loans at June 30, 2017. Non-performing loans have been considered in management's analysis of the appropriateness of the allowance for loan losses. Management and the Board of Directors closely monitor these loans and believe the prospect for recovery of principal, less identified specific reserves, are favorable.

**Other Income.** Total other income increased by \$141, or 4.3%, to \$3,391 for the 2018 fiscal year.

Debit card interchange income increased by \$172, or 14.8% in 2018 to \$1,333; however, debit card processing expenses increased by \$118 over the same period.

Gain on sale of mortgage loans increased by \$109, or 42.2%, from the same period last year primarily as a result of an increase in volume.

These increases were partially offset by a \$176 decline in gains from the sale of securities.

**Other Expenses.** Total other expenses were \$14,237 for the year ended June 30, 2018; an increase of \$759, or 5.6%, from \$13,478 for the year ended June 30, 2017.

Salaries and employee benefit expenses increased by \$556, or 7.8%, during the fiscal year ended June 30, 2018 mainly due to an increase in salary and incentive expenses.

Professional and director fees decreased by \$85, or 14.0%, during the 2018 fiscal year from the same period last year primarily as a result of a decrease in legal and consulting fees.

Loan and collection expenses decreased by \$38, or 24.5%, during the 2018 fiscal year from the same period last year primarily as a result of a reduction in collection expenses.

Marketing and advertising expenses increased by \$41, or 15.4%, during the 2018 fiscal year from the same period last year primarily due to an increase in advertising and promotional campaigns initiated to attract core deposit customers.

**Income Tax Expense.** Income tax expense totaled \$1,149 and \$641 and the effective tax rates were 24.3% and 17.6% for the years ended June 30, 2018 and 2017, respectively. Income tax expense and the effective tax rate was higher in the 2018 fiscal year period compared to the same prior year period primarily due to the enactment of the Tax Act and increased income before income taxes. The enactment of the Tax Act required the Corporation to revalue its deferred tax assets and liabilities based upon the lower enacted federal corporate income tax rate at which the Corporation expects to recognize the benefit. During the three months ended December 31, 2017 a one-time income tax expense of \$348 was recorded in conjunction with writing down its net deferred tax assets. The Tax Act lowered the federal corporate tax rate beginning on January 1, 2018. As a result, the Corporation utilized a blended tax rate for its fiscal year ending June 30, 2018. In addition, the effective tax rate differs from the federal statutory rate as a result of tax-exempt income from obligations of states and political subdivisions, loans and earnings on bank owned life insurance.

## **Financial Condition**

Total assets at June 30, 2018 were \$502,619 compared to \$457,883 at June 30, 2017, an increase of \$44,736, or 9.8%. The growth in total assets was mainly attributed to an increase of \$45,642, or 16.7%, in total loans. This growth was primarily funded by an increase in total deposits.

**Securities.** Total securities increased by \$1,707 to \$148,052 at June 30, 2018, of which \$144,028 were classified as available-for-sale and \$4,024 were classified as held-to-maturity. The securities portfolio is mainly comprised of residential mortgage-backed securities and collateralized mortgage obligations issued by Fannie Mae, Freddie Mac and Ginnie Mae, state and political subdivisions and obligations of government-sponsored enterprises.

The following tables summarize the amortized cost and fair value of available-for-sale securities at June 30, 2018 and 2017 and the corresponding amounts of gross unrealized gains and losses recognized in accumulated other comprehensive income or loss:

| <u>Available-for-sale</u>                                      | <b>Amortized<br/>Cost</b> | <b>Gross<br/>Unrealized<br/>Gains</b> | <b>Gross<br/>Unrealized<br/>Losses</b> | <b>Fair<br/>Value</b> |
|--|---------------------------|---------------------------------------|--|-----------------------|
| <b>June 30, 2018</b>   |                           |                                       |  |                       |
| Obligations of U.S. government-sponsored entities and agencies | \$ 16,488                 | \$ 6                                  | \$ (372)                               | ) \$16,122            |
| Obligations of state and political subdivisions                | 56,964                    | 339                                   | (713)                                  | ) 56,590              |
| Mortgage-backed securities - residential                       | 65,062                    | 6                                     | (1,660)                                | ) 63,408              |
| Mortgage-backed securities - commercial                        | 1,432                     | —                                     | (17)                                   | ) 1,415               |
| Collateralized mortgage obligations                            | 5,973                     | 9                                     | (216)                                  | ) 5,766               |
| Pooled trust preferred security                                | 178                       | 549                                   | —                                      | 727                   |
| Total available-for-sale securities                            | \$ 146,097                | \$ 909                                | \$ (2,978)                             | ) \$144,028           |

| <u>Available-for-sale</u>                                      | <b>Amortized<br/>Cost</b> | <b>Gross<br/>Unrealized<br/>Gains</b> | <b>Gross<br/>Unrealized<br/>Losses</b> | <b>Fair<br/>Value</b> |
|--|---------------------------|---------------------------------------|--|-----------------------|
| <b>June 30, 2017</b>   |                           |                                       |  |                       |
| Obligations of U.S. government-sponsored entities and agencies | \$ 12,571                 | \$ 90                                 | \$ (74)                                | ) \$12,587            |
| Obligations of state and political subdivisions                | 56,824                    | 890                                   | (254)                                  | ) 57,460              |
| Mortgage-backed securities - residential                       | 64,092                    | 184                                   | (438)                                  | ) 63,838              |
| Mortgage-backed securities - commercial                        | 1,459                     | —                                     | (1)                                    | ) 1,458               |
| Collateralized mortgage obligations                            | 6,310                     | 1                                     | (100)                                  | ) 6,211               |
| Pooled trust preferred security                                | 155                       | 377                                   | —                                      | 532                   |
| Total available-for-sale securities                            | \$ 141,411                | \$ 1,542                              | \$ (867)                               | ) \$142,086           |



The following tables summarize the amortized cost and fair value of held-to-maturity securities at June 30, 2018 and 2017 and the corresponding gross unrecognized gains and losses:

| <b><u>Held-to-maturity</u></b>                  | <b>Amortized<br/>Cost</b> | <b>Gross<br/>Unrecognized<br/>Gains</b> | <b>Gross<br/>Unrecognized<br/>Losses</b> | <b>Fair<br/>Value</b> |
|---|---------------------------|---|--|-----------------------|
| <b>June 30, 2018</b>                            |                           |   |  |                       |
| Obligations of state and political subdivisions | \$ 4,024                  | \$ 24                                   | \$ —                                     | \$4,048               |
| Total held-to-maturity securities               | \$ 4,024                  | \$ 24                                   | \$ —                                     | \$4,048               |

| <b><u>Held-to-maturity</u></b>                  | <b>Amortized<br/>Cost</b> | <b>Gross<br/>Unrecognized<br/>Gains</b> | <b>Gross<br/>Unrecognized<br/>Losses</b> | <b>Fair<br/>Value</b> |
|---|---------------------------|---|--|-----------------------|
| <b>June 30, 2017</b>                            |                           |   |  |                       |
| Obligations of state and political subdivisions | \$ 4,259                  | \$ 73                                   | \$ (3 )                                  | \$4,329               |
| Total held-to-maturity securities               | \$ 4,259                  | \$ 73                                   | \$ (3 )                                  | \$4,329               |

The following tables summarize the amounts and distribution of the Corporation's securities held and the weighted average yields as of June 30, 2018:

|  | <b>Amortized<br/>Cost</b> | <b>Fair<br/>Value</b> | <b>Average<br/>Yield /<br/>Cost</b> |   |
|--|---------------------------|-----------------------|-------------------------------------|---|
| <b>Available-for-sale</b>                                    |                           |                       |                                     |   |
| <b>Obligations of government-sponsored entities:</b>         |                           |                       |                                     |   |
| Over 1 year through 5 years                                  | \$ 9,375                  | \$9,205               | 2.25                                | % |
| Over 5 years through 10 years                                | 7,113                     | 6,917                 | 2.68                                |   |
| <b>Total obligations of government-sponsored entities</b>    | <b>16,488</b>             | <b>16,122</b>         | <b>2.44</b>                         |   |
| <b>Obligations of state and political subdivisions:</b>      |                           |                       |                                     |   |
| 3 Months or less   | 1,346                     | 1,348                 | 3.83                                |   |
| Over 3 months through 1 year                                 | 1,742                     | 1,749                 | 3.40                                |   |
| Over 1 year through 5 years                                  | 11,412                    | 11,440                | 2.90                                |   |
| Over 5 years through 10 years                                | 20,349                    | 20,318                | 3.27                                |   |
| Over 10 years  | 22,115                    | 21,735                | 3.26                                |   |
| <b>Total obligations of state and political subdivisions</b> | <b>56,964</b>             | <b>56,590</b>         | <b>3.21</b>                         |   |
| <b>Mortgage-backed securities - residential:</b>             |                           |                       |                                     |   |
| Over 3 months through 1 year                                 |                           |                       |                                     |   |
| Over 1 year through 5 years                                  | 42,140                    | 40,940                | 2.18                                |   |
| Over 5 years through 10 years                                | 22,922                    | 22,468                | 2.86                                |   |
| <b>Total mortgage-backed securities - residential</b>        | <b>65,062</b>             | <b>63,408</b>         | <b>2.42</b>                         |   |

**Mortgage-backed securities - commercial:**

|  |                   |                   |              |          |
|--|-------------------|-------------------|--------------|----------|
| Over 1 year through 5 years                          | 1,432             | 1,415             | 1.97         |          |
| <b>Total mortgage-backed securities - commercial</b> | <b>1,432</b>      | <b>1,415</b>      | <b>1.97</b>  |          |
| <b>Collateralized mortgage obligations:</b>          |                   |                   |              |          |
| Over 3 months through 1 year                         |                   |                   |              |          |
| Over 1 year through 5 years                          | 4,068             | 3,908             | 1.86         |          |
| Over 5 years through 10 years                        | 1,905             | 1,858             | 2.89         |          |
| <b>Total collateralized mortgage obligations</b>     | <b>5,973</b>      | <b>5,766</b>      | <b>2.19</b>  |          |
| <b>Pooled trust preferred security</b>               | <b>178</b>        | <b>727</b>        | <b>32.10</b> |          |
| <b>Total available-for-sale securities</b>           | <b>\$ 146,097</b> | <b>\$ 144,028</b> | <b>2.75</b>  | <b>%</b> |

|   | <b>Amortized<br/>Cost</b> | <b>Fair<br/>Value</b> | <b>Average<br/>Yield /<br/>Cost</b> |          |
|---|---------------------------|-----------------------|-------------------------------------|----------|
| <b>Held-to-maturity</b>                                 |                           |                       |                                     |          |
| <b>Obligations of state and political subdivisions:</b> |                           |                       |                                     |          |
| Over 5 years through 10 years                           | \$ 527                    | \$527                 | 2.91                                | %        |
| Over 10 years   | 3,497                     | 3,521                 | 2.38                                |          |
| <b>Total held-to-maturity securities</b>                | <b>\$ 4,024</b>           | <b>\$4,048</b>        | <b>2.45</b>                         | <b>%</b> |

The weighted average interest rates are based on coupon rates for securities purchased at par value and on effective yields considering amortization or accretion if the securities were purchased at a premium or discount. The weighted average yield on tax-exempt obligations has been calculated on a tax equivalent basis. Average yields are based on amortized cost balances. The effective yield on the pooled trust preferred security was 32.10% due to the other-than-temporary impairment charges taken in prior years which reduced the amortized cost along with principal and interest payments being received during the 2018 fiscal year.

At June 30, 2018, there were no holdings of securities of any one issuer, other than the U.S. government-sponsored entities and agencies, with an aggregate book value which exceeds 10% of shareholders' equity.

**Loans.** Loan receivables increased by \$45,642 to \$318,509 at June 30, 2018 compared to \$272,867 at June 30, 2017. Loan demand increased, particularly in the commercial and commercial real estate segments, principally as a result of increased calling efforts within and around the surrounding markets of the Bank's branch locations and the loan production office.

Major classifications of loans, net of deferred loan fees and costs, were as follows as of June 30:

|                                     | <b>2018</b> | <b>2017</b> |
|-------------------------------------|-------------|-------------|
| Commercial                          | \$60,953    | \$46,336    |
| Commercial real estate:             |             |             |
| Construction                        | 5,375       | 5,588       |
| Other                               | 182,966     | 157,861     |
| 1-4 Family residential real estate: |             |             |
| Owner occupied                      | 47,683      | 41,581      |
| Non-owner occupied                  | 15,480      | 14,377      |
| Construction                        | 1,187       | 1,993       |
| Consumer loans                      | 4,865       | 5,131       |
| Total loans                         | \$318,509   | \$272,867   |

The following is a schedule of contractual maturities and repayments of 1-4 family residential real estate construction, commercial and commercial real estate loans, as of June 30, 2018:

|  |           |
|--|-----------|
| Due in one year or less                  | \$20,860  |
| Due after one year but within five years | 31,575    |
| Due after five years                     | 198,046   |
| Total                                    | \$250,481 |

The following is a schedule of fixed and variable rate 1-4 family residential real estate construction, commercial and commercial real estate loans due after one year (variable rate loans are those loans with floating or adjustable interest rates) as of June 30, 2018:

|   | <b>Fixed<br/>Interest<br/>Rates</b> | <b>Variable<br/>Interest<br/>Rates</b> |
|---|-------------------------------------|--|
| Total 1-4 family residential real estate construction, commercial and commercial real estate loans due after one year | \$ 96,164                           | \$ 133,457                             |

Foreign Outstandings. There were no foreign outstandings during the periods presented. There are no concentrations of loans greater than 10% of total loans, which are not otherwise disclosed as a category of loans.

**Allowance for Loan Losses.** The allowance for loan losses balance and the provision charged to expense are judgmentally determined by management based upon a periodic review of the loan portfolio, an analysis of impaired loans, past loan loss experience, current economic conditions, collateral value assumptions for collateral-dependent loans and various other circumstances which are subject to change over time. Probable incurred losses are estimated by stratifying the total loan portfolio into pools of homogenous loans by occupancy, collateral type and loan purpose and applying the Bank's historical loss ratio, increased for more recent trends in loss experience, to each loan pool. Also, local unemployment rates are monitored and additional reserves are applied to all loans that are not assigned a specific reserve if there is an increase in the local unemployment rate. Specific reserves are determined by management's review of delinquent loans, impaired loans, non-accrual loans, loans classified as substandard, watch list loans, loans to industries experiencing economic difficulties and other selected large loans. The collectability of these loans is evaluated after considering the current financial position of the borrower, the estimated market value of the collateral, guarantees and the Corporation's collateral position versus other creditors. Judgments, which are necessarily subjective, as to the probability of loss and the amount of such loss, are formed on these loans, as well as other loans in the aggregate.

Failure to receive principal and interest payments when due on any loan results in efforts to restore such loan to a current status. Loans are classified as non-accrual when, in the opinion of management, full collection of principal and accrued interest is not expected. The loans must be brought and kept current for six sustained payments before being considered for removal from non-accrual status. Commercial and commercial real estate loans are classified as impaired if management determines that full collection of principal and interest, in accordance with the terms of the loan documents, is not probable. If a loan is impaired, a portion of the allowance is allocated so the loan is reported, net, at the present value of estimated future cash flows using the loan's existing rate or at the fair value of collateral if repayment is expected from the collateral. Loans are evaluated for impairment when payments are delayed, typically 90 days or more, or when it is probable that not all principal and interest amounts will be collected according to the original terms of the loan. As of June 30, 2018, impaired loans totaled \$2,060, of which \$1,090 are included in non-accrual loans. Continued unsuccessful collection efforts generally lead to initiation of foreclosure or other legal proceedings.

The following schedule summarizes non-accrual, past due, impaired and restructured loans for the years ended June 30:

|   | <b>2018</b> | <b>2017</b> |
|---|-------------|-------------|
| Non-accrual loans                       | \$1,090     | \$1,187     |
| Accruing loans past due 90 days or more | —           | —           |
| Total non-performing loans              | \$1,090     | \$1,187     |
| Other real estate owned                 | —           | 71          |
| Total non-performing assets             | \$1,090     | \$1,258     |
| Impaired loans                          | \$2,060     | \$2,234     |
| Accruing restructured loans             | \$971       | \$1,082     |

The non-performing loans are either in the process of foreclosure or efforts are being made to work with the borrower to bring the loan current. Properties acquired by the Corporation as a result of foreclosure, or by deed in lieu of foreclosure, are classified as "other real estate owned" until they are sold or otherwise disposed of.

**Potential Problem Loans.** There were no loans, not otherwise identified above, included on management's watch or troubled loan lists that management has serious doubts as to the ability of such borrowers to comply with the loan repayment terms. Management's watch and troubled loan lists includes loans which management has some doubt as to the borrowers' ability to comply with the present repayment terms, loans which management is actively monitoring due to changes in the borrower's financial condition and other loans which management wants to more closely monitor due to special circumstances. These loans and their potential loss exposure have been considered in management's analysis of the adequacy of the allowance for loan losses.

The following table summarizes the Corporation's loan loss experience, and provides a breakdown of the charge-off, recovery and other activity for the years ended June 30:

|   | <b>2018</b> | <b>2017</b> |
|---|-------------|-------------|
| Allowance for loan losses at beginning of year  | \$3,086     | \$3,566     |
| <b>Loans charged off:</b>                       |             |             |
| Commercial                                      | —           | 6           |
| Commercial real estate                          | 4           | 1,061       |
| 1-4 Family residential real estate              | 33          | 44          |
| Consumer loans                                  | 24          | 37          |
| Total charge offs                               | 61          | 1,148       |
| <b>Recoveries:</b>                              |             |             |
| Commercial                                      | 17          | 1           |
| Commercial real estate                          | 41          | —           |
| 1-4 Family residential real estate              | 14          | 38          |
| Consumer loans                                  | 15          | 33          |
| Total recoveries                                | 87          | 72          |
| Net charge-offs (recoveries)                    | (26 )       | 1,076       |
| Provision for loan losses charged to operations | 310         | 596         |
| Allowance for loan losses at end of year        | \$3,422     | \$3,086     |

The following schedule is a breakdown of the allowance for loan losses allocated by type of loan and related ratios:

|                                    | <b>Allocation of the Allowance for Loan Losses</b> |       |   |  |       |   |
|------------------------------------|--|-------|---|--|-------|---|
|                                    | <b>% of Loan Allowance Amount to Total Loans</b>   |       |   | <b>% of Loan Allowance Amount to Total Loans</b> |       |   |
|                                    | <b>June 30, 2018</b>                               |       |   | <b>June 30, 2017</b>                             |       |   |
|                                    |  |       |   |  |       |   |
| Commercial                         | \$586  | 19.1  | % | \$518  | 17.0  | % |
| Commercial real estate loans       | 2,277  | 59.2  |   | 2,038  | 59.9  |   |
| 1-4 Family residential real estate | 499  | 20.2  |   | 473  | 21.2  |   |
| Consumer loans                     | 60   | 1.5   |   | 57   | 1.9   |   |
| Total                              | \$3,422  | 100.0 | % | \$3,086  | 100.0 | % |

While management's periodic analysis of the adequacy of the allowance for loan loss may allocate portions of the allowance for specific problem loan situations, the entire allowance is available for any loan charge-off that may occur.

**Funding Sources.** Total deposits increased by \$55,492, or 14.8%, from \$374,471 at June 30, 2017 to \$429,963 at June 30, 2018. During the quarter ended June 30, 2018, the nature of some of our public fund deposit account relationships changed. As a result, \$21,163 in public funds previously reported as short-term borrowings are now reported as deposit accounts. If not for this change, deposits would have increased by \$34,329, or 9.2%, for the 12-month period ended June 30, 2018 compared to June 30, 2017. For the fiscal year ended June 30, 2018, interest bearing demand deposits increased by \$27,176, or 50.2%, time deposits increased by \$12,030, or 18.1%, savings deposits increased by \$11,050, or 7.3% and noninterest-bearing demand deposits increased by \$5,236, or 5.1% from the same prior year period. The increases in noninterest-bearing demand, savings and time deposits is primarily from business and public fund customer relationships as a result of the continued focus on attracting low cost core deposit account relationships and from the opening of the new branch location in Jefferson, Ohio.

Short-term borrowings decreased by \$10,619, or 44.3%, from \$23,986 at June 30, 2017 to \$13,367 at June 30, 2018. As mentioned in the preceding paragraph, short-term borrowings declined primarily as a result of public fund sweep repurchase agreements that were previously reported as short-term borrowings are now reported as deposit accounts. This decline was partially offset by an \$8,881 increase in federal funds purchased.

The following is a schedule of average deposit amounts and average rates paid on each category for the periods included:

|                                      | <b>Years Ended June 30,</b> |             |               |             |
|--------------------------------------|-----------------------------|-------------|---------------|-------------|
|                                      | <b>2018</b>                 |             | <b>2017</b>   |             |
|                                      | <b>Amount</b>               | <b>Rate</b> | <b>Amount</b> | <b>Rate</b> |
| Noninterest-bearing demand deposit   | \$109,675                   | —           | \$103,017     | —           |
| Interest-bearing demand deposit      | 57,272                      | 0.20%       | 49,832        | 0.15%       |
| Savings                              | 155,000                     | 0.23        | 141,279       | 0.13        |
| Certificates and other time deposits | 71,404                      | 1.04        | 66,761        | 0.79        |
| Total                                | \$393,351                   | 0.31%       | \$360,889     | 0.22%       |

The following table summarizes time deposits issued in amounts of \$100 or more as of June 30, 2018 by time remaining until maturity:

Maturing in:

|                     |          |
|---------------------|----------|
| Under 3 months      | \$3,090  |
| Over 3 to 6 months  | 8,181    |
| Over 6 to 12 months | 7,366    |
| Over 12 months      | 20,786   |
| Total               | \$39,423 |

See Note 6—Short-Term Borrowings to the Consolidated Financial Statements, for information concerning short-term borrowings.



## Capital Resources

Total shareholders' equity increased by \$226 from \$43,535 at June 30, 2017 to \$43,761 at June 30, 2018. The increase was primarily the result of \$3,581 of net income for the current fiscal year. This increase was partially offset by a net reduction of \$2,080 in accumulated other comprehensive income from a shift in unrealized gains on the mark-to-market of available-for-sale securities to net unrealized losses and cash dividends paid of \$1,351.

At June 30, 2018, management believes the Bank complied with all regulatory capital requirements. Based on the Bank's computed regulatory capital ratios, the OCC has determined the Bank to be well capitalized under the Federal Deposit Insurance Act as of its latest exam date. The Bank's actual and required capital amounts are disclosed in Note 11-Regulatory Matters to the Consolidated Financial Statements. Management is not aware of any matters occurring subsequent to that exam that would cause the Bank's capital category to change.

## Liquidity

Management considers the asset position of the Bank to be sufficiently liquid to meet normal operating needs and conditions. The Bank's earning assets are divided primarily between loans and available-for-sale securities, with any excess funds placed in federal funds sold or interest-bearing deposit accounts with other financial institutions.

Net cash inflows from operating activities for the 2018 fiscal year were \$5,851 and net cash inflows from financing activities were \$42,958. Net cash outflows from investing activities were \$50,949. The major sources of cash were a \$55,492 net increase in deposits and an \$18,262 net increase from sales, maturities or principal pay downs on available-for-sale securities. The major uses of cash were a \$45,869 net increase in loans and the \$23,878 purchase of available-for-sale securities. Total cash and cash equivalents were \$7,772 as of June 30, 2018 compared to \$9,912 at June 30, 2017.

The Bank groups its loan portfolio into four major categories: commercial loans; commercial real estate loans; 1-4 family residential real estate loans; and consumer loans. The Bank's 1-4 family residential real estate loan portfolio primarily consists of fixed and variable rate mortgage loans for terms generally not longer than thirty years and variable rate home equity lines of credit. Commercial and commercial real estate loans are comprised of both variable rate notes subject to interest rate changes based on the prime rate or Treasury index, and fixed rate notes having maturities of generally not greater than twenty years. Consumer loans offered by the Bank are generally written for periods of up to seven years, based on the nature of the collateral. These may be either installment loans having regular monthly payments or demand type loans for short periods of time.

Funds not allocated to the Bank's loan portfolio are invested in various securities having diverse maturity schedules. A majority of the Bank's securities are held in obligations of U.S. Government-sponsored entities, mortgage-backed securities, and investments in tax-exempt municipal bonds.

The Bank offers several forms of deposit products to its customers. We believe the rates offered by the Bank and the fees charged for them are competitive with others currently available in the market area. While the Bank continues to be under competitive pressures in the Bank's market area as financial institutions attempt to attract and keep new deposits, we believe many commercial and retail customers have been continuing to turn to community banks. Compared to our peers, the Corporation's core deposits consist of a larger percentage of noninterest-bearing demand deposits resulting in the cost of funds remaining at a low level of 0.52%.

Jumbo time deposits (those with balances of \$250 and over) were \$23,018 and \$14,252 at June 30, 2018 and 2017, respectively. These deposits are monitored closely by the Bank and typically priced on an individual basis. When these deposits are from a municipality, certain bank-owned securities are pledged to guarantee the safety of these public fund deposits as required by Ohio law. The Corporation has the option to use a fee paid broker to obtain deposits from outside its normal service area as an additional source of funding. However, these deposits are not relied upon as a primary source of funding.

Dividends from the Bank are the primary source of funds for payment of dividends to our shareholders. However, there are statutory limits on the amount of dividends the Bank can pay without regulatory approval. Under these regulations, the amount of dividends that may be paid in any calendar year is limited to the current year's net profits, combined with the retained net profits of the preceding two years, subject to the capital requirements described above. Additionally, the Bank may not declare or pay any dividend if, after making the dividend, the Bank would be "undercapitalized," as defined in the federal regulations. As of June 30, 2018, the Bank could, without prior approval, declare a dividend of approximately \$4,448.

### **Impact of Inflation and Changing Prices**

The financial statements and related data presented herein have been prepared in accordance with U.S. generally accepted accounting principles, which require the measurement of financial position and results of operations primarily in terms of historical dollars without considering changes in the relative purchasing power of money over time due to inflation. Unlike most industrial companies, virtually all the assets and liabilities of the Corporation are monetary in nature. Therefore, as a financial institution, interest rates have a more significant impact on the Corporation's performance than the effects of general levels of inflation. Interest rates do not necessarily move in the same direction or in the same magnitude as the prices of goods and services. The liquidity, maturity structure and quality of the Corporation's assets and liabilities are critical to the maintenance of acceptable performance levels.

## Critical Accounting Policies and Use of Significant Estimates

The financial condition and results of operations for the Corporation presented in the Consolidated Financial Statements, accompanying notes to the Consolidated Financial Statements and management's discussion and analysis are, to a large degree, dependent upon the Corporation's accounting policies. The selection and application of these accounting policies involve judgments, estimates and uncertainties that are susceptible to change.

Presented below is a discussion of the accounting policies that management believes are the most important to the portrayal and understanding of the Corporation's financial condition and results of operations. These policies require management's most difficult, subjective and complex judgments about matters that are inherently uncertain. In the event that different assumptions or conditions were to prevail, and depending upon the severity of such changes, the possibility of materially different financial condition or results of operations is a reasonable likelihood. Also, see Note 1-Summary of Significant Accounting Policies to the Consolidated Financial Statements for additional information related to significant accounting policies.

**Allowance for Loan Losses.** Management periodically reviews the loan portfolio to establish an estimated allowance for loan losses (allowance) that are probable as of the respective reporting date. Additions to the allowance are charged against earnings for the period as a provision for loan losses. Actual loan losses are charged against the allowance when management believes the collection of principal will not occur. Unpaid interest for loans placed on non-accrual status is reversed against current interest income.

The allowance is regularly reviewed by management to determine whether the amount is considered adequate to absorb probable incurred losses. If not, an additional provision is made to increase the allowance. This evaluation includes specific loss estimates on certain individually reviewed loans, loss estimates for loan groups or pools based on historical loss experience and general loss estimates based upon the size, quality, and concentration characteristics of the various loan portfolios, adverse situations that may affect a borrower's ability to repay, and current economic and industry conditions, among other things. The allowance is also subject to periodic examination by regulators whose review includes a determination as to its adequacy to absorb probable incurred losses.

Those judgments and assumptions that are most critical to the application of this accounting policy are the initial and on-going credit-worthiness of the borrower, the amount and timing of future cash flows of the borrower that are available for repayment of the loan, the sufficiency of underlying collateral, the enforceability of third-party guarantees, the frequency and subjectivity of loan reviews and risk grading, emerging or changing trends that might not be fully captured in the historical loss experience, and charges against the allowance for actual losses that are greater than previously estimated. These judgments and assumptions are dependent upon or can be influenced by a variety of factors, including the breadth and depth of experience of lending officers, credit administration and the loan review staff that periodically review the status of the loan, changing economic and industry conditions, changes in the financial condition of the borrower, and changes in the value and availability of the underlying collateral and

guarantees.

While we strive to reflect all known risk factors in our evaluations, judgment errors may occur. If different assumptions or conditions were to prevail, the amount and timing of interest income and loan losses could be materially different. These factors are most pronounced during economic downturns. Since, as described above, so many factors can affect the amount and timing of losses on loans, it is difficult to predict, with any degree of certainty, the affect on income if different conditions or assumptions were to prevail.

18

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**Contractual Obligations, Commitments and Contingent Liabilities**

The following table presents, as of June 30, 2018, the Corporation's significant fixed and determinable contractual obligations by payment date. The payment amounts represent those amounts contractually due to the recipient and do not include any unamortized premiums or discounts. Further discussion of the nature of each obligation is included in the referenced note to the consolidated financial statements.

|                            | <b>Note<br/>Reference</b> | <b>2019</b> | <b>2020</b> | <b>2021</b> | <b>2022</b> | <b>2023</b> | <b>Thereafter</b> | <b>Total</b> |
|----------------------------|---------------------------|-------------|-------------|-------------|-------------|-------------|-------------------|--------------|
| Certificates of deposit    | 5                         | \$37,984    | \$24,575    | \$6,261     | \$7,528     | \$1,472     | \$ 721            | \$78,541     |
| Short-term borrowings      | 6                         | 13,367      | —           | —           | —           | —           | —                 | 13,367       |
| Federal Home Loan advances | 7                         | 2,056       | 1,500       | 1,500       | 1,700       | 5,000       | —                 | 11,756       |
| Salary continuation plan   | 8                         | 77          | 146         | 146         | 146         | 146         | 1,660             | 2,321        |
| Operating leases           | 4                         | 83          | 85          | 78          | 71          | 65          | —                 | 382          |
| Deposits without maturity  |                           | —           | —           | —           | —           | —           | —                 | 351,422      |

Note 12-Commitments with Off-Balance Sheet Risk to the Consolidated Financial Statements discusses in greater detail other commitments and contingencies and the various obligations that exist under those agreements. These commitments and contingencies consist primarily of commitments to extend credit to borrowers under lines of credit.

**Off-Balance Sheet Arrangements**

At June 30, 2018, the Corporation had no unconsolidated, related special purpose entities, nor did the Corporation engage in derivatives and hedging contracts, such as interest rate swaps, which may expose the Corporation to liabilities greater than the amounts recorded on the consolidated balance sheet. The Corporation's investment policy prohibits engaging in derivative contracts for speculative trading purposes; however, in the future, the Corporation may pursue certain contracts, such as interest rate swaps, to execute a sound and defensive interest rate risk management policy.

**ITEM 7A—QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

Not applicable for Smaller Reporting Companies.



## **ITEM 8—FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA**

### **REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

Shareholders and the Board of Directors of Consumers Bancorp, Inc.

Minerva, Ohio

#### **Opinion on the Financial Statements**

We have audited the accompanying consolidated balance sheets of Consumers Bancorp, Inc. (the "Company") as of June 30, 2018 and 2017, the related consolidated statements of income, comprehensive income, changes in shareholders' equity, and cash flows for each of the years then ended, and the related notes (collectively referred to as the "financial statements"). In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company as of June 30, 2018 and 2017, and the results of its operations and its cash flows for each of the years then ended, in conformity with accounting principles generally accepted in the United States of America.

#### **Basis for Opinion**

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

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

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

/s/ Crowe LLP

Crowe LLP

We have served as the Company's auditor since 1998.

Cleveland, Ohio

September 12, 2018



**CONSOLIDATED BALANCE SHEETS**

As of June 30, 2018 and 2017

(Dollar amounts in thousands, except per share data)

|  | <b>2018</b> | <b>2017</b> |
|--|-------------|-------------|
| <b>ASSETS:</b>   |             |             |
| Cash on hand and noninterest-bearing deposits in financial institutions  | \$7,615     | \$9,439     |
| Federal funds sold and interest-bearing deposits in financial institutions                                     | 157         | 473         |
| Total cash and cash equivalents  | 7,772       | 9,912       |
| Certificate of deposits in financial institutions  | 2,973       | 3,921       |
| Securities, available-for-sale   | 144,028     | 142,086     |
| Securities, held-to-maturity (fair value 2018 \$4,048 and 2017 \$4,329)  | 4,024       | 4,259       |
| Federal bank and other restricted stocks, at cost  | 1,459       | 1,425       |
| Loans held for sale  | 1,448       | 1,252       |
| Total loans  | 318,509     | 272,867     |
| Less allowance for loan losses   | (3,422 )    | (3,086 )    |
| Net loans  | 315,087     | 269,781     |
| Cash surrender value of life insurance   | 9,335       | 9,065       |
| Premises and equipment, net  | 13,315      | 13,398      |
| Accrued interest receivable and other assets   | 3,178       | 2,784       |
| Total assets   | \$502,619   | \$457,883   |
| <b>LIABILITIES:</b>  |             |             |
| Deposits:  |             |             |
| Noninterest-bearing demand   | \$107,919   | \$102,683   |
| Interest bearing demand  | 81,299      | 54,123      |
| Savings  | 162,204     | 151,154     |
| Time   | 78,541      | 66,511      |
| Total deposits   | 429,963     | 374,471     |
| Short-term borrowings  | 13,367      | 23,986      |
| Federal Home Loan Bank advances  | 11,756      | 12,320      |
| Accrued interest payable and other liabilities   | 3,772       | 3,571       |
| Total liabilities  | 458,858     | 414,348     |
| Commitments and contingent liabilities (Note 12)   |             |             |
| <b>SHAREHOLDERS' EQUITY:</b>   |             |             |
| Preferred stock, no par value; 350,000 shares authorized   | —           | —           |
| Common shares, no par value; 3,500,000 shares authorized; 2,854,133 shares issued as of June 30, 2018 and 2017 | 14,630      | 14,630      |
| Retained earnings  | 32,342      | 30,122      |
| Treasury stock, at cost (124,489 and 130,606 common shares at June 30, 2018 and 2017, respectively)            | (1,576 )    | (1,662 )    |
| Accumulated other comprehensive income (loss)  | (1,635 )    | 445         |

|  |           |           |
|--|-----------|-----------|
| Total shareholders' equity                 | 43,761    | 43,535    |
| Total liabilities and shareholders' equity | \$502,619 | \$457,883 |

*See accompanying notes to consolidated financial statements.*

**CONSOLIDATED STATEMENTS OF INCOME**

Years Ended June 30, 2018 and 2017

(Dollar amounts in thousands, except per share data)

|  | <b>2018</b> | <b>2017</b> |
|--|-------------|-------------|
| <b>Interest income:</b>  |             |             |
| Loans, including fees  | \$13,937    | \$12,333    |
| Federal funds sold and interest-bearing deposits in financial institutions | 151         | 122         |
| Securities, taxable  | 1,997       | 1,678       |
| Securities, tax-exempt   | 1,472       | 1,434       |
| Total interest and dividend income   | 17,557      | 15,567      |
| <b>Interest expense:</b>   |             |             |
| Deposits   | 1,210       | 792         |
| Short-term borrowings  | 240         | 90          |
| Federal Home Loan Bank advances  | 221         | 226         |
| Total interest expense   | 1,671       | 1,108       |
| Net interest income  | 15,886      | 14,459      |
| Provision for loan losses  | 310         | 596         |
| Net interest income after provision for loan losses                        | 15,576      | 13,863      |
| <b>Other income:</b>   |             |             |
| Service charges on deposit accounts  | 1,200       | 1,245       |
| Debit card interchange income  | 1,333       | 1,161       |
| Bank owned life insurance income   | 270         | 246         |
| Gain on sale of mortgage loans   | 367         | 258         |
| Securities gains, net  | 33          | 209         |
| Loss on disposition of other real estate owned                             | (2 )        | (35 )       |
| Other  | 190         | 166         |
| Total other income   | 3,391       | 3,250       |
| <b>Other expenses:</b>   |             |             |
| Salaries and employee benefits   | 7,692       | 7,136       |
| Occupancy and equipment  | 1,867       | 1,888       |
| Data processing expenses   | 601         | 583         |
| Professional and director fees   | 523         | 608         |
| Federal Deposit Insurance Corporation assessments                          | 168         | 175         |
| Franchise taxes  | 343         | 336         |
| Marketing and advertising  | 308         | 267         |
| Loan and collection expenses   | 117         | 155         |
| Telephone and communications   | 307         | 305         |
| Debit card processing expenses   | 754         | 636         |
| Other  | 1,557       | 1,389       |
| Total other expenses   | 14,237      | 13,478      |

|   |                |                |
|---|----------------|----------------|
| Income before income taxes                  | 4,730          | 3,635          |
| Income tax expense                          | 1,149          | 641            |
| <b>Net income</b>                           | <b>\$3,581</b> | <b>\$2,994</b> |
| <b>Basic and diluted earnings per share</b> | <b>\$1.31</b>  | <b>\$1.10</b>  |

*See accompanying notes to consolidated financial statements.*

**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**

Years Ended June 30, 2018 and 2017

(Dollar amounts in thousands, except per share data)

|  | <b>2018</b> | <b>2017</b> |
|--|-------------|-------------|
| Net income   | \$3,581     | \$2,994     |
| Other comprehensive income, net of tax:                  |             |             |
| Net change in unrealized losses:                         |             |             |
| Unrealized losses arising during the period              | (2,711)     | (2,737)     |
| Reclassification adjustment for gains included in income | (33 )       | (209 )      |
| Net unrealized loss                                      | (2,744)     | (2,946)     |
| Income tax effect  | 650         | 1,002       |
| Other comprehensive loss                                 | (2,094)     | (1,944)     |
| Total comprehensive income                               | \$1,487     | \$1,050     |

*See accompanying notes to consolidated financial statements.*

**CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY**

Years Ended June 30, 2018 and 2017

(Dollar amounts in thousands, except per share data)

|   | <b>Common<br/>Shares</b> | <b>Retained<br/>Earnings</b> | <b>Treasury<br/>Stock</b> | <b>Accumulated<br/>Other<br/>Comprehensive<br/>Income<br/>(Loss)</b> | <b>Total<br/>Shareholders'<br/>Equity</b> |
|---|--------------------------|------------------------------|---------------------------|--|---|
| <b>Balance, June 30, 2016</b>   | \$ 14,630                | \$ 28,432                    | \$ (1,658 )               | \$ 2,389   | \$ 43,793                                 |
| Net income  |                          | 2,994                        |                           |  | 2,994                                     |
| Other comprehensive loss  |                          |                              |                           | (1,944 )   | (1,944 )                                  |
| 231 Dividend reinvestment plan shares associated with expired and forfeited restricted stock awards retired to treasury |                          | 4                            | (4 )                      |  | —   |
| Cash dividends declared (\$0.48 per share)  |                          | (1,308 )                     |                           |  | (1,308 )                                  |
| <b>Balance, June 30, 2017</b>   | \$ 14,630                | \$ 30,122                    | \$ (1,662 )               | \$ 445   | \$ 43,535                                 |
| Net income  |                          | 3,581                        |                           |  | 3,581                                     |
| Other comprehensive loss  |                          |                              |                           | (2,094 )   | (2,094 )                                  |
| Reclassification of disproportionate income tax effects   |                          | (14 )                        |                           | 14   | —   |
| 6,321 shares issued associated with stock awards  |                          |                              | 90                        |  | 90  |
| 204 Dividend reinvestment plan shares associated with expired and forfeited restricted stock awards retired to treasury |                          | 4                            | (4 )                      |  | —   |
| Cash dividends declared (\$0.495 per share)   |                          | (1,351 )                     |                           |  | (1,351 )                                  |
| <b>Balance, June 30, 2018</b>   | \$ 14,630                | \$ 32,342                    | \$ (1,576 )               | \$ (1,635 )  | \$ 43,761                                 |

*See accompanying notes to consolidated financial statements.*

**CONSOLIDATED STATEMENTS OF CASH FLOWS**

Years Ended June 30, 2018 and 2017

(Dollar amounts in thousands, except per share data)

|  | <b>2018</b> | <b>2017</b> |
|--|-------------|-------------|
| <b>Cash flows from operating activities:</b>                                     |             |             |
| Net income   | \$3,581     | \$2,994     |
| Adjustments to reconcile net income to net cash flows from operating activities: |             |             |
| Depreciation   | 771         | 781         |
| Securities amortization and accretion, net                                       | 963         | 1,087       |
| Provision for loan losses  | 310         | 596         |
| (Gain) loss on disposal of fixed assets  | (6 )        | 2           |
| Loss on disposition or direct write-down of other real estate owned              | 2           | 35          |
| Net gain on sale of loans  | (367 )      | (258 )      |
| Deferred income tax expense  | 462         | 128         |
| Gain on sale of securities   | (33 )       | (209 )      |
| Origination of loans held for sale   | (22,336)    | (24,379)    |
| Proceeds from loans held for sale  | 22,760      | 24,775      |
| Increase in cash surrender value of life insurance                               | (270 )      | (246 )      |
| Change in other assets and other liabilities                                     | 14          | 73          |
| Net cash flows from operating activities   | 5,851       | 5,379       |
| <b>Cash flows from investing activities:</b>                                     |             |             |
| Securities available-for-sale:   |             |             |
| Purchases  | (23,878)    | (41,752)    |
| Maturities, calls and principal pay downs  | 15,618      | 21,869      |
| Proceeds from sales of available-for-sale securities                             | 2,644       | 7,342       |
| Securities held-to-maturity:   |             |             |
| Purchases  | —           | (1,000 )    |
| Principal pay downs  | 235         | 235         |
| Net decrease in certificates of deposit with other financial institutions        | 948         | 1,985       |
| Purchase of Federal Home Loan Stock  | (34 )       | (29 )       |
| Net increase in loans  | (45,869)    | (18,120)    |
| Purchase of Bank owned life insurance  | —           | (2,000 )    |
| Acquisition of premises and equipment  | (688 )      | (598 )      |
| Disposal of premises and equipment   | 6           | 2           |
| Proceeds from sale of other real estate owned                                    | 69          | 7           |
| Net cash flows from investing activities   | (50,949)    | (32,059)    |
| <b>Cash flows from financing activities:</b>                                     |             |             |
| Net increase in deposit accounts   | 55,492      | 27,823      |
| Proceeds from Federal Home Loan Bank advances                                    | 2,700       | 19,325      |
| Repayments of Federal Home Loan Bank advances                                    | (3,264 )    | (24,286)    |

|   |                |                |
|---|----------------|----------------|
| Change in short-term borrowings               | (10,619)       | 4,857          |
| Dividends paid                                | (1,351 )       | (1,308 )       |
| Net cash flows from financing activities      | 42,958         | 26,411         |
| Decrease in cash and cash equivalents         | (2,140 )       | (269 )         |
| Cash and cash equivalents, beginning of year  | 9,912          | 10,181         |
| <b>Cash and cash equivalents, end of year</b> | <b>\$7,772</b> | <b>\$9,912</b> |

*See accompanying notes to consolidated financial statements.*



## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2018 and 2017

(Dollar amounts in thousands, except per share data)

### NOTE 1—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

**Principles of Consolidation:** The consolidated financial statements include the accounts of Consumers Bancorp, Inc. (Corporation) and its wholly owned subsidiary, Consumers National Bank (Bank), together referred to as the Corporation. All significant intercompany transactions have been eliminated in the consolidation.

**Nature of Operations:** Consumers Bancorp, Inc. is a bank holding company headquartered in Minerva, Ohio that provides, through its banking subsidiary, a broad array of products and services throughout its primary market area of Carroll, Columbiana, Jefferson, Stark, Summit, Wayne and contiguous counties in Ohio. The Bank's business involves attracting deposits from businesses and individual customers and using such deposits to originate commercial, mortgage and consumer loans in its primary market area.

**Business Segment Information:** The Corporation is engaged in the business of commercial and retail banking, which accounts for substantially all of its revenues, operating income, and assets. Accordingly, all of its operations are reported in *one* segment, banking.

**Use of Estimates:** To prepare financial statements in conformity with U.S. generally accepted accounting principles, management makes estimates and assumptions based on available information. These estimates and assumptions affect the amounts reported in the financial statements and the disclosures provided, and actual results could differ.

**Cash Flows:** Cash and cash equivalents include cash, deposits with other financial institutions with original maturities of less than 90 days and federal funds sold. Net cash flows are reported for customer loan and deposit transactions, interest bearing deposits in other financial institutions and short-term borrowings. Additional cash flow information was as follows:

**Year Ended  
June 30,**

|   | <b>2018</b> | <b>2017</b> |
|---|-------------|-------------|
| Cash paid for interest  | \$1,643     | \$1,108     |
| Cash paid for Federal income taxes  | 730         | 300         |
| Non-cash transactions:  |             |             |
| Transfer from loans to repossessed assets   | —           | 113         |
| Transfer from loans held for sale to portfolio  | 253         | 342         |
| Issuance of treasury stock for stock awards   | 90          | —           |
| Expired and forfeited dividend reinvestment plan shares associated with restricted stock awards that were retired to treasury stock | 4           | 4           |

**Interest-Bearing Deposits in Other Financial Institutions:** Interest-bearing deposits in other financial institutions mature within *one* year and are carried at cost.

**Certificates of Deposit in Financial Institutions:** Certificates of deposit in other financial institutions are carried at cost.

**Cash Reserves:** The Bank is required to maintain cash on hand and noninterest-bearing balances on deposit with the Federal Reserve Bank to meet regulatory reserve and clearing requirements. The required reserve balance at *June 30, 2018* and *2017* was \$329 and \$304, respectively.

**Securities:** Securities are generally classified into either held-to-maturity or available-for-sale categories. Held-to-maturity securities are carried at amortized cost and are those that the Corporation has the positive intent and ability to hold to maturity. Available-for-sale securities are those that the Corporation *may* decide to sell before maturity if needed for liquidity, asset-liability management, or other reasons. Available-for-sale securities are reported at fair value, with unrealized gains or losses included in other comprehensive income (loss) as a separate component of equity, net of tax.

Interest income includes amortization of purchase premiums and accretion of discounts. 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.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Management evaluates securities for other-than-temporary impairment (OTTI) at least on 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 whether 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. For equity securities, the entire amount of impairment is recognized through earnings.

**Federal Bank and Other Restricted Stocks:** The Bank is a member of the Federal Home Loan Bank (FHLB) system. Members are required to own a certain amount of stock based on the level of borrowings and other factors, and *may* invest in additional amounts. FHLB stock, included with Federal bank and other restricted stocks on the Consolidated Balance Sheet, is carried at cost, classified as a restricted security and periodically evaluated for impairment based on ultimate recovery of par value. Federal Reserve Bank stock is also carried at cost. Since these stocks are viewed as a long-term investment, impairment is based on ultimate recovery of par value. Both cash and stock dividends are reported as income.

**Loans Held for Sale:** Mortgage loans originated and intended for sale in the secondary market are carried at the lower of aggregate cost or fair value, as determined by outstanding commitments from investors. Mortgage loans held for sale are generally sold with servicing rights released. Net unrealized losses, if any, are recorded as a valuation allowance and charged to earnings. Gains and losses on sales of mortgage loans are based on the difference between the selling price and the carrying value of the related loan sold.

**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 balance 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 includes accrued interest receivable.

Interest income on commercial, commercial real estate and 1-4 family residential loans is discontinued at the time the loan is 90 days delinquent unless the loan is well-secured and in the process of collection. Consumer loans are typically charged off *no* later than 120 days past due. Past due status is determined by the contractual terms of the

loan. In all cases, loans are placed on non-accrual or charged-off at an earlier date if collection of principal or interest is considered doubtful.

All interest accrued but *not* received on loans placed on non-accrual 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 accrual status when the customer has exhibited the ability to repay and demonstrated this ability over at least a consecutive *six*-month period and future payments are reasonably assured.

**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 funded.

**Concentrations of Credit Risk:** The Bank grants consumer, real estate and commercial loans primarily to borrowers in Carroll, Columbiana, Jefferson, Stark, Summit and Wayne counties. Therefore, the Corporation's exposure to credit risk is significantly affected by changes in the economy in these counties. Automobiles and other consumer assets, business assets and residential and commercial real estate secure most loans.

**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 uncollectability of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance. Management estimates the allowance balance required based on 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.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The allowance consists of specific and general components. The specific component relates to loans that are individually classified as impaired. The general component covers non-classified loans and is based on historical loss experience adjusted for current factors.

A loan is considered impaired when, based on current information and events, it is probable that the Corporation will be unable to collect all amounts due according to the contractual terms of the loan agreement. Loans, for which the terms have been modified, resulting in a concession, and for which the borrower is experiencing financial difficulties, are considered troubled debt restructurings 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 evaluated collectively for smaller-balance loans of similar nature such as residential mortgage, consumer loans and on an individual loan basis for other loans. If a loan is impaired, a portion of the allowance is allocated so the loan is reported, net, at the present value of estimated future cash flows using the loan's existing rate or at the fair value of collateral if repayment is expected from the collateral. Loans are evaluated for impairment when payments are delayed, typically 90 days or more, or when it is probable that *not* all principal and interest amounts will be collected according to the original terms of the loan. 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 interest rate at inception. If a troubled debt restructuring is considered to be a collateral dependent loan, the loan is reported, net, at the 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 covers non-impaired loans and is based on historical loss experience adjusted for current factors. The historical loss experience is determined by portfolio segment and is based on the actual loss history experienced by the Corporation over the most recent *two*-year or *three*-year period, depending on loan segment. This actual loss experience is supplemented with economic and other factors based on the risks present for each portfolio segment. These factors include consideration of the following: levels of and trends in volume and terms of loans; effects of any changes in risk selection and underwriting standards; other changes in lending policies, procedures and practices; experience, ability and depth of lending management and other relevant staff; national and local economic trends and conditions; industry conditions; and effects of changes in credit concentrations. The following portfolio segments have been identified:

*Commercial:* Commercial loans are made for a wide variety of general business purposes, including financing for equipment, inventories and accounts receivable. The term of each commercial loan varies by its purpose. Commercial loans are underwritten after evaluating and understanding the borrower's ability to operate profitably and prudently expand its business. Current and projected cash flows are evaluated to determine the ability of the borrower to repay their obligations as agreed. Commercial loans are primarily made based on the identified cash flows of the borrower and secondarily made based on the underlying collateral provided by the borrower. The cash flows of borrowers, however, *may not* be as expected and the collateral securing these loans *may* fluctuate in value. Most commercial loans are secured by the assets being financed or other business assets such as accounts receivable or inventory and usually incorporate a personal guarantee; however, some short-term loans *may* be made on an unsecured basis. In the case of loans secured by accounts receivable, the availability of funds for the repayment of these loans *may* be substantially dependent on the ability of the borrower to collect amounts due from its customers. The commercial loan portfolio includes loans to a wide variety of corporations and businesses across many industrial classifications in the areas where the Bank operates.

*Commercial Real Estate:* Commercial real estate loans include mortgage loans to farmers, owners of multi-family investment properties, developers and owners of commercial real estate. Commercial real estate lending typically involves higher loan principal amounts and the repayment of these loans is generally largely dependent on the successful operation of the property securing the loan or the business conducted on the property securing the loan. Commercial real estate loans *may* be more adversely affected by conditions in the real estate markets or in the general economy. The properties securing the Corporation's commercial real estate portfolio are diverse in terms of type and geographic location. This diversity helps reduce the Corporation's exposure to adverse economic events that affect any single market or industry. Management monitors and evaluates commercial real estate loans based on collateral, geography and risk grade criteria. In addition, management tracks the level of owner-occupied commercial real estate loans versus non-owner occupied loans.

*1-4 Family Residential Real Estate:* Residential real estate loans are secured by *one* to *four* family residential properties and include both owner occupied, non-owner occupied and home equity loans. Credit approval for residential real estate loans requires demonstration of sufficient income to repay the principal and interest and the real estate taxes and insurance, stability of employment, an established credit record and an appropriately appraised value of the real estate securing the loan that generally requires that the residential real estate loan amount be *no* more than 85% of the purchase price or the appraised value of the real estate securing the loan unless the borrower provides private mortgage insurance.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

**Consumer:** The Corporation originates direct and indirect consumer loans, primarily automobile loans, personal lines of credit, and unsecured consumer loans in its primary market areas. Credit approval for consumer loans requires income sufficient to repay principal and interest due, stability of employment, an established credit record and sufficient collateral for secured loans. Consumer loans typically have shorter terms and lower balances with higher yields as compared to real estate mortgage loans, but generally carry higher risks of default. Consumer loan collections are dependent on the borrower's continuing financial stability, and thus are more likely to be affected by adverse personal circumstances.

**Other Real Estate Owned:** Real estate properties acquired through, or in lieu of, loan foreclosure are initially recorded at fair value less costs to sell at the date of acquisition, establishing a new cost basis. Any reduction to fair value from the carrying value of the related loan at the time of acquisition is accounted for as a loan loss. These assets are subsequently accounted for at lower of cost or fair value less estimated costs to sell. If the fair value declines after acquisition, a valuation allowance is recorded as a charge to income. Operating costs after acquisition are expensed. Gains and losses on disposition are reported as a charge to income.

**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 carried at cost. Premises and equipment are stated at cost less accumulated depreciation. Depreciation is computed primarily using the straight-line method over the estimated useful life of the owned asset and, for leasehold improvements, generally over the lesser of the remaining term of the lease facility or the estimated economic life of the improvement. Useful lives range from *three* years for software to *thirty-nine* and *one-half* years for buildings.

**Cash Surrender Value of Life Insurance:** The Bank has purchased single-premium life insurance policies to insure the lives of current and former participants in the salary continuation plan. As of *June 30, 2018*, the Bank had policies with total death benefits of *\$19,776* and total cash surrender values of *\$9,335*. As of *June 30, 2017*, the Bank had policies with total death benefits of *\$19,728* and total cash surrender values of *\$9,065*. 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. Tax-exempt income is recognized from the periodic increases in cash surrender value of these policies.

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

**Repurchase Agreements:** Substantially all repurchase agreement liabilities, which are classified as short-term borrowings, represent amounts advanced by various customers. Securities are pledged to cover these liabilities, which are *not* covered by federal deposit insurance.

**Retirement Plans:** The Bank maintains a 401(k) savings and retirement plan covering all eligible employees and matching contributions are expensed as made. Salary continuation plan expense allocates the benefits over years of service.

**Income Taxes:** The Corporation files a consolidated federal income tax return. Income tax expense is the sum of the current-year income tax due or refundable and the change in deferred tax assets and liabilities. Deferred tax assets and liabilities are the expected future tax consequences of temporary differences between the carrying amounts and tax basis of assets and liabilities, computed using enacted tax rates. A valuation allowance, if needed, reduces deferred tax assets to the amount expected to be realized. The Corporation applies a more likely than *not* recognition threshold for all tax uncertainties in accordance with U.S. generally accepted accounting principles. A tax position is recognized as a benefit only if it is more likely than *not* that the 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 greater than 50% likely of being realized on examination. The Corporation recognizes interest and/or penalties related to income tax matters in income tax expense.



## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

**Earnings per Common Share:** Basic earnings per common share is net income divided by the weighted average number of common shares outstanding during the period. Diluted earnings per common share includes the dilutive effect of additional potential common shares issuable upon the vesting of restricted stock awards.

**Stock-Based Compensation:** Compensation cost is recognized for restricted stock awards issued to employees over the required service period, generally defined as the vesting period. The fair value of restricted stock awards is estimated by using the market price of the Corporation's common stock at the date of grant. For awards with graded vesting, compensation cost is recognized on a straight-line basis over the requisite service period for the entire award.

**Comprehensive Income:** Comprehensive income consists of net income and other comprehensive income (loss). Other comprehensive income (loss) includes unrealized gains and losses on securities available-for-sale, which are also recognized as a separate component of equity, net of tax.

**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 Corporation's financial statements.

**Fair Value of Financial Instruments:** Fair value of financial instruments are estimated using relevant market information and other assumptions, as more fully disclosed in Note 13 of the Consolidated Financial Statements. Fair value estimates involve uncertainties and matters of significant judgment regarding interest rates, credit risk, discounted cash flows, 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.

**Dividend Restrictions:** Banking regulations require maintaining certain capital levels and *may* limit the dividends paid by the Bank to the holding company or by the holding company to shareholders.

**Reclassifications:** Certain reclassifications have been made to the *June 30, 2017* financial statements to be comparable to the *June 30, 2018* presentation. The reclassifications had *no* impact on prior year net income or shareholders' equity.

**Recently Issued Accounting Pronouncements Not Yet Effective:** In *May 2014*, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) *2014-09, Revenue from Contracts with Customers (Topic 606)*. This ASU creates a new topic, Topic *606*, to provide guidance on revenue recognition for entities that enter into contracts with customers to transfer goods or services or enter into contracts for the transfer of nonfinancial assets. The core principle of the guidance is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Additional disclosures are required to provide quantitative and qualitative information regarding the nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers. The new guidance is effective for annual reporting periods, and interim reporting periods within those annual periods, beginning after *December 15, 2017*. Most of the Corporation's revenue is derived from loans and financial instruments, which is *not* part of the scope of this ASU. The adoption of this guidance on *July 1, 2018* did *not* have a material impact on the Corporation's financial statements; however, the adoption of this standard will result in additional disclosures beginning with the *first* quarter of fiscal year *2019* Form *10-Q*.

In *January 2016*, FASB issued ASU *2016-01, Financial Instruments – Overall: Recognition and Measurement of Financial Assets and Financial Liabilities*. The main provisions of ASU *2016-01* address the valuation and impairment of certain equity investments along with simplified disclosures about those investments. For equity securities, the guidance requires equity investments to be measured at fair value with changes in fair value recognized in net income. ASU *2016-01* is effective for fiscal years beginning after *December 15, 2017*, including interim periods within those fiscal years. The adoption of ASU *2016-01* on *July 1, 2018* did *not* have a material impact on the Corporation's financial statements.

In *June 2016*, FASB issued ASU *2016-13, Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*. This ASU adds a new Topic *326* to the codification and removes the thresholds that companies apply to measure credit losses on financial instruments measured at amortized cost, such as loans, receivables, and held-to-maturity debt securities. Under current U.S. generally accepted accounting principles, companies generally recognize credit losses when it is probable that the loss has been incurred. The revised guidance will remove all current loss recognition thresholds and will require companies to recognize an allowance for credit losses for the difference between the amortized cost basis of a financial instrument and the amount of amortized cost that the corporation expects to collect over the instrument's contractual life. ASU *2016-13* also amends the credit loss measurement guidance for available-for-sale debt securities and beneficial interests in securitized financial assets. The guidance in ASU *2016-13* is effective for "public business entities," as defined, that are SEC filers for fiscal years and for interim periods within those fiscal years beginning after *December 15, 2019*. Early adoption of the guidance is permitted for fiscal years beginning after *December 15, 2018*, including interim periods within those fiscal years. Management is currently evaluating the impact of the adoption of this guidance on the Corporation's consolidated financial statements and are in the midst of gathering critical data to evaluate the impact. However, it is too early to estimate the impact.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

In *February 2016*, FASB issued ASU 2016-02, *Leases (Topic 842)*. This ASU will require all organizations that lease assets to recognize on the balance sheet the assets and liabilities for the rights and obligations created by those leases. Additional qualitative and quantitative disclosures will be required so that users can understand more about the nature of an entity's leasing activities. The new guidance is effective for annual reporting periods and interim reporting periods within those annual periods, beginning after *December 15, 2018*. Early adoption is permitted. Management is currently evaluating the impact of the adoption of this guidance on the Corporation's consolidated financial statements and expects to recognize an increase in other assets and other liabilities for the rights and obligations created by leasing of branch offices. Management also expects minimal impact in the income statement with respect to occupancy expense related to leases.

In *March 2017*, FASB issued ASU 2017-08, *Receivables-Nonrefundable Fees and Other Costs: Premium Amortization on Purchased Callable Debt Securities*. This ASU amends the guidance related to amortization for certain callable debt securities held at a premium, requiring the premium to be amortized to the earliest call date. The adoption of ASU 2017-08 will *not* have a material impact on the Corporation's financial statements.

In *February 2018*, the FASB issued ASU 2018-02, *Income Statement – Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income*. This ASU was issued in response to the U.S. federal government enacting the Tax Cuts and Jobs Act of 2017. The ASU will require reclassifying certain income tax effects from accumulated other comprehensive income to retained earnings. The amount of that reclassification is the difference between the amount initially charged or credited directly to other comprehensive income at the previously enacted U.S. federal corporate income tax rate that remains in accumulated other comprehensive income and the amount that would have been charged or credited directly to other comprehensive income using the newly enacted 21.0% U.S. federal corporate income tax rate, excluding the effect of any valuation allowance previously charged to income from continuing operations. The new guidance is effective for annual reporting periods, and interim reporting periods within those annual periods, beginning after *December 15, 2018*. Early adoption is permitted. The Corporation adopted this ASU as of *March 2018*, which resulted in a \$14 reclassification between retained earnings and accumulated other comprehensive income.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

**NOTE 2—SECURITIES**

The following table summarizes the amortized cost and fair value of securities available-for-sale and securities held-to-maturity at *June 30, 2018* and *2017* and the corresponding amounts of gross unrealized gains and losses recognized in accumulated other comprehensive income (loss) and gross unrecognized gains and losses:

| <b><u>Available-for-sale</u></b>  | <b>Amortized<br/>Cost</b> | <b>Gross<br/>Unrealized<br/>Gains</b> | <b>Gross<br/>Unrealized<br/>Losses</b> | <b>Fair<br/>Value</b> |
|---|---------------------------|---------------------------------------|--|-----------------------|
| <b>June 30, 2018</b>  |                           |                                       |  |                       |
| Obligations of U.S. government-sponsored entities and agencies              | \$ 16,488                 | \$ 6                                  | \$ (372)                               | \$ 16,122             |
| Obligations of state and political subdivisions                             | 56,964                    | 339                                   | (713)                                  | 56,590                |
| U.S. Government-sponsored mortgage-backed securities - residential          | 65,062                    | 6                                     | (1,660)                                | 63,408                |
| U.S. Government-sponsored mortgage-backed securities - commercial           | 1,432                     | —                                     | (17)                                   | 1,415                 |
| U.S. Government-sponsored collateralized mortgage obligations - residential | 5,973                     | 9                                     | (216)                                  | 5,766                 |
| Pooled trust preferred security   | 178                       | 549                                   | —                                      | 727                   |
| Total available-for-sale securities   | \$ 146,097                | \$ 909                                | \$ (2,978)                             | \$ 144,028            |

| <b><u>Held-to-maturity</u></b>                  | <b>Amortized<br/>Cost</b> | <b>Gross<br/>Unrecognized<br/>Gains</b> | <b>Gross<br/>Unrecognized<br/>Losses</b> | <b>Fair<br/>Value</b> |
|---|---------------------------|---|--|-----------------------|
| <b>June 30, 2018</b>                            |                           |   |  |                       |
| Obligations of state and political subdivisions | \$ 4,024                  | \$ 24                                   | \$ —                                     | \$ 4,048              |
| Total held-to-maturity securities               | \$ 4,024                  | \$ 24                                   | \$ —                                     | \$ 4,048              |

| <b><u>Available-for-sale</u></b>                                   | <b>Amortized<br/>Cost</b> | <b>Gross<br/>Unrealized<br/>Gains</b> | <b>Gross<br/>Unrealized<br/>Losses</b> | <b>Fair<br/>Value</b> |
|--|---------------------------|---------------------------------------|--|-----------------------|
| <b>June 30, 2017</b>   |                           |                                       |  |                       |
| Obligations of U.S. government-sponsored entities and agencies     | \$ 12,571                 | \$ 90                                 | \$ (74)                                | \$ 12,587             |
| Obligations of state and political subdivisions                    | 56,824                    | 890                                   | (254)                                  | 57,460                |
| U.S. Government-sponsored mortgage-backed securities - residential | 64,092                    | 184                                   | (438)                                  | 63,838                |

|   |            |          |         |   |            |
|---|------------|----------|---------|---|------------|
| U.S. Government-sponsored mortgage-backed securities - commercial           | 1,459      | —        | (1      | ) | 1,458      |
| U.S. Government-sponsored collateralized mortgage obligations - residential | 6,310      | 1        | (100    | ) | 6,211      |
| Pooled trust preferred security   | 155        | 377      | —       |   | 532        |
| Total available-for-sale securities   | \$ 141,411 | \$ 1,542 | \$ (867 | ) | \$ 142,086 |

| <b><u>Held-to-maturity</u></b>                  | <b>Amortized Cost</b> | <b>Gross Unrecognized Gains</b> | <b>Gross Unrecognized Losses</b> | <b>Fair Value</b> |
|---|-----------------------|---------------------------------|----------------------------------|-------------------|
| <b>June 30, 2017</b>                            |                       |                                 |                                  |                   |
| Obligations of state and political subdivisions | \$ 4,259              | \$ 73                           | \$ (3                            | ) \$4,329         |
| Total held-to-maturity securities               | \$ 4,259              | \$ 73                           | \$ (3                            | ) \$4,329         |

Proceeds from sales and calls of available-for-sale securities during fiscal year 2018 and fiscal year 2017 were as follows:

|                               | <b>2018</b> | <b>2017</b> |
|-------------------------------|-------------|-------------|
| Proceeds from sales and calls | \$2,644     | \$14,255    |
| Gross realized gains          | 40          | 213         |
| Gross realized losses         | 7           | 4           |

The income tax provision related to these net realized gains amounted to \$12 in fiscal year 2018 and \$71 in fiscal year 2017. During the *first* quarter of fiscal year 2019, the pooled trust preferred security was sold for gross proceeds of \$771.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The amortized cost and fair values of debt securities at *June 30, 2018* by expected maturity are shown below. Expected maturities will differ from contractual maturities because borrowers *may* have the right to call or prepay obligations with or without call or prepayment penalties. Securities *not* due at a single maturity date, primarily mortgage-backed securities, collateralized mortgage obligations and the pooled trust preferred security are shown separately.

| <b><u>Available-for-sale</u></b>                                 | <b>Amortized</b> | <b>Fair</b>  |
|--|------------------|--------------|
|  | <b>Cost</b>      | <b>Value</b> |
| Due in one year or less  | \$ 3,087         | \$3,097      |
| Due after one year through five years                            | 20,787           | 20,645       |
| Due after five years through ten years                           | 27,462           | 27,235       |
| Due after ten years  | 22,115           | 21,735       |
| Total  | 73,451           | 72,712       |
| U.S. Government-sponsored mortgage-backed and related securities | 72,468           | 70,589       |
| Pooled trust preferred security                                  | 178              | 727          |
| Total  | \$ 146,097       | \$ 144,028   |

| <b><u>Held-to-maturity</u></b>         | <b>Amortized</b> | <b>Fair</b>  |
|--|------------------|--------------|
|  | <b>Cost</b>      | <b>Value</b> |
| Due after five years through ten years | \$ 527           | \$527        |
| Due after ten years                    | 3,497            | 3,521        |
| Total                                  | \$ 4,024         | \$4,048      |

Securities with a carrying value of approximately \$71,673 and \$55,932 were pledged at *June 30, 2018* and *2017*, respectively, to secure public deposits and commitments as required or permitted by law. At *June 30, 2018* and *2017*, there were *no* holdings of securities of any *one* issuer, other than the U.S. government and its agencies, with an aggregate book value greater than *10%* of shareholders' equity.

The following table summarizes the securities with unrealized and unrecognized losses at *June 30, 2018* and *2017*, aggregated by investment category and length of time that the individual securities have been in a continuous unrealized loss position:

| <b>Less than 12<br/>Months</b> | <b>12 Months or more</b> | <b>Total</b> |
|--------------------------------|--------------------------|--------------|
|--------------------------------|--------------------------|--------------|

| <u>Available-for-sale</u>                                      | <b>Fair<br/>Value</b> | <b>Unrealized<br/>Loss</b> | <b>Fair<br/>Value</b> | <b>Unrealized<br/>Loss</b> | <b>Fair<br/>Value</b> | <b>Unrealized<br/>Loss</b> |
|--|-----------------------|----------------------------|-----------------------|----------------------------|-----------------------|----------------------------|
| <b>June 30, 2018</b>   |                       |                            |                       |                            |                       |                            |
| Obligations of U.S. government-sponsored entities and agencies | \$12,400              | \$ (224 )                  | \$2,747               | \$ (148 )                  | \$15,147              | \$ (372 )                  |
| Obligations of states and political subdivisions               | 26,775                | (369 )                     | 7,975                 | (344 )                     | 34,750                | (713 )                     |
| Mortgage-backed securities - residential                       | 31,038                | (581 )                     | 29,716                | (1,079 )                   | 60,754                | (1,660 )                   |
| Mortgage-backed securities - commercial                        | 1,415                 | (17 )                      | —                     | —                          | 1,415                 | (17 )                      |
| Collateralized mortgage obligations - residential              | —                     | —                          | 4,821                 | (216 )                     | 4,821                 | (216 )                     |
| Total temporarily impaired                                     | \$71,628              | \$ (1,191 )                | \$45,259              | \$ (1,787 )                | \$116,887             | \$ (2,978 )                |

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

| <u>Available-for-sale</u>                                      | Less than 12 Months |                 | 12 Months or more |                 | Total      |                 |
|--|---------------------|-----------------|-------------------|-----------------|------------|-----------------|
|  | Fair Value          | Unrealized Loss | Fair Value        | Unrealized Loss | Fair Value | Unrealized Loss |
| <b>June 30, 2017</b>   |                     |                 |                   |                 |            |                 |
| Obligations of U.S. government-sponsored entities and agencies | \$4,336             | \$ (74 )        | \$—               | \$ —            | \$4,336    | \$ (74 )        |
| Obligations of states and political subdivisions               | 13,881              | (241 )          | 834               | (13 )           | 14,715     | (254 )          |
| Mortgage-backed securities - residential                       | 42,071              | (391 )          | 2,805             | (47 )           | 44,876     | (438 )          |
| Mortgage-backed securities - commercial                        | 1,458               | (1 )            | —                 | —               | 1,458      | (1 )            |
| Collateralized mortgage obligations - residential              | 5,417               | (88 )           | 654               | (12 )           | 6,071      | (100 )          |
| Total temporarily impaired                                     | \$67,163            | \$ (795 )       | \$4,293           | \$ (72 )        | \$71,456   | \$ (867 )       |

| <u>Held-to-Maturity</u>                          | Less than 12 Months |                 | 12 Months or more |                 | Total      |                 |
|--|---------------------|-----------------|-------------------|-----------------|------------|-----------------|
|  | Fair Value          | Unrealized Loss | Fair Value        | Unrealized Loss | Fair Value | Unrealized Loss |
| <b>June 30, 2017</b>                             |                     |                 |                   |                 |            |                 |
| Obligations of states and political subdivisions | \$933               | \$ (3 )         | \$—               | \$ —            | \$933      | \$ (3 )         |
| Total temporarily impaired                       | \$933               | \$ (3 )         | \$—               | \$ —            | \$933      | \$ (3 )         |

Management evaluates securities for other-than-temporary impairment (OTTI) on a quarterly basis, and more frequently when economic or market conditions warrant such an evaluation. The securities portfolio is evaluated for OTTI by segregating the portfolio into *two* general segments and applying the appropriate OTTI model. Investment securities are generally evaluated for OTTI under FASB ASC Topic 320, *Accounting for Certain Investments in Debt and Equity Securities*.

In determining OTTI under the ASC Topic 320 model, management considers many factors, including: (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, (3) whether the market decline was affected by macroeconomic conditions, and (4) whether the entity has the intent to sell the debt security or more likely than *not* will be required to sell the debt security before its anticipated recovery. The assessment of whether an other-than-temporary decline exists involves a high degree of subjectivity and judgment and is based on the information available to management at a point in time.

As of *June 30, 2018*, the Corporation's securities portfolio consisted of *264* available-for-sale and *three* held-to-maturity securities. There were *189* securities in an unrealized loss position at *June 30, 2018*, *68* of which were in a continuous loss position for *twelve* or more months. The unrealized losses within the securities portfolio



were primarily attributed to a change in market rates. At *June 30, 2018*, all the mortgage-backed securities and collateralized mortgage obligations held by the Corporation were issued by U.S. government-sponsored entities and agencies, primarily Fannie Mae and Freddie Mac, institutions which the government has affirmed its commitment to support. Also, management monitors the financial condition of the individual municipal securities to ensure they meet minimum credit standards. Since the Corporation does *not* intend to sell these securities and it is *not* likely that the Corporation will be required to sell these securities at an unrealized loss position prior to any anticipated recovery in fair value, which *may* be maturity, management does *not* believe there is any OTTI related to these securities at *June 30, 2018*. Also, there was *no* OTTI recognized at *June 30, 2017*.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

**NOTE 3—LOANS**

Major classifications of loans were as follows as of *June 30*:

|                                       | <b>2018</b> | <b>2017</b> |
|---------------------------------------|-------------|-------------|
| Commercial                            | \$60,995    | \$46,380    |
| Commercial real estate:               |             |             |
| Construction                          | 5,394       | 5,604       |
| Other                                 | 183,383     | 158,225     |
| 1 – 4 Family residential real estate: |             |             |
| Owner occupied                        | 47,433      | 41,411      |
| Non-owner occupied                    | 15,516      | 14,415      |
| Construction                          | 1,171       | 1,988       |
| Consumer                              | 4,873       | 5,138       |
| Subtotal                              | 318,765     | 273,161     |
| Net Deferred loan fees and costs      | (256 )      | (294 )      |
| Allowance for loan losses             | (3,422 )    | (3,086 )    |
| Net loans                             | \$315,087   | \$269,781   |

The following table presents the activity in the allowance for loan losses by portfolio segment for the year ending *June 30, 2018*:

|                                | Commercial | Commercial<br>Real<br>Estate | 1-4 Family<br>Residential<br>Real<br>Estate | Consumer | Total   |
|--------------------------------|------------|------------------------------|---|----------|---------|
| Allowance for loan losses:     |            |                              |   |          |         |
| Beginning balance              | \$ 518     | \$ 2,038                     | \$ 473                                      | \$ 57    | \$3,086 |
| Provision for loan losses      | 51         | 202                          | 45  | 12       | 310     |
| Loans charged-off              | —          | (4 )                         | (33 )                                       | (24 )    | (61 )   |
| Recoveries                     | 17         | 41                           | 14  | 15       | 87      |
| Total ending allowance balance | \$ 586     | \$ 2,277                     | \$ 499                                      | \$ 60    | \$3,422 |

The following table presents the activity in the allowance for loan losses by portfolio segment for the year ending *June 30, 2017*:

|                                | Commercial | Commercial<br>Real<br>Estate | 1-4 Family<br>Residential<br>Real<br>Estate | Consumer | Total   |
|--------------------------------|------------|------------------------------|---|----------|---------|
| Allowance for loan losses:     |            |                              |   |          |         |
| Beginning balance              | \$ 505     | \$ 2,518                     | \$ 402                                      | \$ 141   | \$3,566 |
| Provision for loan losses      | 18         | 581                          | 77  | (80 )    | 596     |
| Loans charged-off              | (6 )       | (1,061 )                     | (44 )                                       | (37 )    | (1,148) |
| Recoveries                     | 1          | —                            | 38  | 33       | 72      |
| Total ending allowance balance | \$ 518     | \$ 2,038                     | \$ 473                                      | \$ 57    | \$3,086 |

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following table presents the balance in the allowance for loan losses and the recorded investment in loans by portfolio segment and based on impairment method as of *June 30, 2018*. Included in the recorded investment in loans is \$732 of accrued interest receivable.

|   | Commercial | Commercial<br>Real<br>Estate | 1-4 Family<br>Residential<br>Real<br>Estate | Consumer | Total      |
|---|------------|------------------------------|---|----------|------------|
| Allowance for loan losses:                      |            |                              |   |          |            |
| Ending allowance balance attributable to loans: |            |                              |   |          |            |
| Individually evaluated for impairment           | \$ —       | \$ 29                        | \$ —  | \$ —     | \$ 29      |
| Collectively evaluated for impairment           | 586        | 2,248                        | 499   | 60       | 3,393      |
| Total ending allowance balance                  | \$ 586     | \$ 2,277                     | \$ 499                                      | \$ 60    | \$ 3,422   |
| Recorded investment in loans:                   |            |                              |   |          |            |
| Loans individually evaluated for impairment     | \$ 100     | \$ 1,562                     | \$ 398                                      | \$ —     | \$ 2,060   |
| Loans collectively evaluated for impairment     | 60,979     | 187,191                      | 64,135                                      | 4,876    | 317,181    |
| Total ending loans balance                      | \$ 61,079  | \$ 188,753                   | \$ 64,533                                   | \$ 4,876 | \$ 319,241 |

The following table presents the balance in the allowance for loan losses and the recorded investment in loans by portfolio segment and based on impairment method as of *June 30, 2017*. Included in the recorded investment in loans is \$581 of accrued interest receivable.

|   | Commercial | Commercial<br>Real<br>Estate | 1-4 Family<br>Residential<br>Real<br>Estate | Consumer | Total    |
|---|------------|------------------------------|---|----------|----------|
| Allowance for loan losses:                      |            |                              |   |          |          |
| Ending allowance balance attributable to loans: |            |                              |   |          |          |
| Individually evaluated for impairment           | \$ —       | \$ 42                        | \$ 2  | \$ —     | \$ 44    |
| Collectively evaluated for impairment           | 518        | 1,996                        | 471   | 57       | 3,042    |
| Total ending allowance balance                  | \$ 518     | \$ 2,038                     | \$ 473                                      | \$ 57    | \$ 3,086 |
| Recorded investment in loans:                   |            |                              |   |          |          |
| Loans individually evaluated for impairment     | \$ 444     | \$ 1,587                     | \$ 203                                      | \$ —     | \$ 2,234 |
| Loans collectively evaluated for impairment     | 45,993     | 162,176                      | 57,901                                      | 5,144    | 271,214  |

|                            |           |            |           |          |           |
|----------------------------|-----------|------------|-----------|----------|-----------|
| Total ending loans balance | \$ 46,437 | \$ 163,763 | \$ 58,104 | \$ 5,144 | \$273,448 |
|----------------------------|-----------|------------|-----------|----------|-----------|

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following table presents information related to loans individually evaluated for impairment by class of loans as of and for the year ended *June 30, 2018*:

|                                     | Unpaid    |            | Allowance<br>for    | Average    | Interest   | Cash Basis |
|-------------------------------------|-----------|------------|---------------------|------------|------------|------------|
|                                     | Principal | Recorded   | Loan                | Recorded   | Income     | Interest   |
|                                     | Balance   | Investment | Losses<br>Allocated | Investment | Recognized | Recognized |
| With no related allowance recorded: |           |            |                     |            |            |            |
| Commercial                          | \$ 100    | \$ 100     | \$ —                | \$ 111     | \$ 5       | \$ 5       |
| Commercial real estate:             |           |            |                     |            |            |            |
| Other                               | 1,330     | 1,330      | —                   | 1,102      | 17         | 17         |
| 1-4 Family residential real estate: |           |            |                     |            |            |            |
| Owner occupied                      | 101       | 101        | —                   | 71         | —          | —          |
| Non-owner occupied                  | 297       | 297        | —                   | 314        | —          | —          |
| With an allowance recorded:         |           |            |                     |            |            |            |
| Commercial real estate:             |           |            |                     |            |            |            |
| Other                               | 231       | 232        | 29                  | 285        | 28         | 28         |
| Total                               | \$ 2,059  | \$ 2,060   | \$ 29               | \$ 1,883   | \$ 50      | \$ 50      |

The following table presents information related to loans individually evaluated for impairment by class of loans as of and for the year ended *June 30, 2017*:

|                                     | Unpaid    |            | Allowance<br>for    | Average    | Interest   | Cash Basis |
|-------------------------------------|-----------|------------|---------------------|------------|------------|------------|
|                                     | Principal | Recorded   | Loan                | Recorded   | Income     | Interest   |
|                                     | Balance   | Investment | Losses<br>Allocated | Investment | Recognized | Recognized |
| With no related allowance recorded: |           |            |                     |            |            |            |
| Commercial                          | \$ 482    | \$ 444     | \$ —                | \$ 207     | \$ 80      | \$ 80      |
| Commercial real estate:             |           |            |                     |            |            |            |
| Construction                        | —         | —          | —                   | 87         | 6          | 6          |
| Other                               | 1,928     | 1,039      | —                   | 951        | 105        | 105        |
| 1-4 Family residential real estate: |           |            |                     |            |            |            |
| Owner occupied                      | 104       | 103        | —                   | 119        | —          | —          |
| Non-owner occupied                  | —         | —          | —                   | 183        | —          | —          |
| With an allowance recorded:         |           |            |                     |            |            |            |

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Commercial real estate:

|                                     |          |          |       |          |        |        |
|-------------------------------------|----------|----------|-------|----------|--------|--------|
| Other                               | 548      | 548      | 42    | 1,884    | 21     | 21     |
| 1-4 Family residential real estate: |          |          |       |          |        |        |
| Owner occupied                      | 99       | 100      | 2     | 120      | 6      | 6      |
| Total                               | \$ 3,161 | \$ 2,234 | \$ 44 | \$ 3,551 | \$ 218 | \$ 218 |

37

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## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following table presents the recorded investment in non-accrual and loans past due over 90 days still on accrual by class of loans as of *June 30, 2018* and *2017*:

|                           | June 30, 2018  |  | June 30, 2017  |  |
|---------------------------|--|--|--|--|
|                           | Loans<br>Past Due<br>Over 90<br>Days<br>Still<br>Non-accrual | Loans<br>Past Due<br>Over 90<br>Days<br>Still<br>Non-accrual | Loans<br>Past Due<br>Over 90<br>Days<br>Still<br>Non-accrual | Loans<br>Past Due<br>Over 90<br>Days<br>Still<br>Non-accrual |
| Commercial                | \$—  | \$ —   | \$368  | \$ —   |
| Commercial real estate:   |  |  |  |  |
| Other                     | 702  | —  | 729  | —  |
| 1 – 4 Family residential: |  |  |  |  |
| Owner occupied            | 90   | —  | 90   | —  |
| Non-owner occupied        | 298  | —  | —  | —  |
| Total                     | \$1,090  | \$ —   | \$1,187  | \$ —   |

Non-accrual 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.

The following table presents the aging of the recorded investment in past due loans as of *June 30, 2018* by class of loans:

|                         | Days Past Due      |                    |                             | Total<br>Past<br>Due | Loans<br>Not<br>Past Due | Total    |
|-------------------------|--------------------|--------------------|-----------------------------|----------------------|--------------------------|----------|
|                         | 30 -<br>59<br>Days | 60 -<br>89<br>Days | 90<br>Days<br>or<br>Greater |                      |                          |          |
| Commercial              | \$—                | \$ —               | \$ —                        | \$—                  | \$61,079                 | \$61,079 |
| Commercial real estate: |                    |                    |                             |                      |                          |          |
| Construction            | —                  | —                  | —                           | —                    | 5,386                    | 5,386    |
| Other                   | 238                | —                  | —                           | 238                  | 183,129                  | 183,367  |
| 1-4 Family residential: |                    |                    |                             |                      |                          |          |
| Owner occupied          | 11                 | —                  | 80                          | 91                   | 47,738                   | 47,829   |
| Non-owner occupied      | —                  | —                  | —                           | —                    | 15,514                   | 15,514   |



|              |       |     |       |       |           |           |
|--------------|-------|-----|-------|-------|-----------|-----------|
| Construction | —     | —   | —     | —     | 1,190     | 1,190     |
| Consumer     | 7     | —   | —     | 7     | 4,869     | 4,876     |
| Total        | \$256 | \$— | \$ 80 | \$336 | \$318,905 | \$319,241 |

The above table of past due loans includes the recorded investment in non-accrual loans of \$249 in the 30-59 days, \$80 in the 90 days or greater category and \$761 in the loans *not* past due category.

The following table presents the aging of the recorded investment in past due loans as of *June 30, 2017* by class of loans:

|                         | Days Past Due |            |                             | Total<br>Past<br>Due | Loans<br>Not<br>Past Due | Total     |
|-------------------------|---------------|------------|-----------------------------|----------------------|--------------------------|-----------|
|                         | 30 -<br>59    | 60 -<br>89 | 90<br>Days<br>or<br>Greater |                      |                          |           |
| Commercial              | \$—           | \$—        | \$ 35                       | \$35                 | \$46,402                 | \$46,437  |
| Commercial real estate: |               |            |                             |                      |                          |           |
| Construction            | —             | —          | —                           | —                    | 5,596                    | 5,596     |
| Other                   | —             | —          | 130                         | 130                  | 158,037                  | 158,167   |
| 1-4 Family residential: |               |            |                             |                      |                          |           |
| Owner occupied          | 13            | —          | 74                          | 87                   | 41,605                   | 41,692    |
| Non-owner occupied      | —             | —          | —                           | —                    | 14,416                   | 14,416    |
| Construction            | —             | —          | —                           | —                    | 1,996                    | 1,996     |
| Consumer                | 22            | —          | —                           | 22                   | 5,122                    | 5,144     |
| Total                   | \$35          | \$—        | \$ 239                      | \$274                | \$273,174                | \$273,448 |

The above table of past due loans includes the recorded investment in non-accrual loans of \$239 in the 90 days or greater category and \$948 in the loans *not* past due category.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

**Troubled Debt Restructurings (TDR):**

The Corporation has certain loans that have been modified in order to maximize collection of loan balances. A modified loan is classified as a TDR if, for economic reasons, management grants a concession to the original terms and conditions of the loan to a borrower who is experiencing financial difficulties that it would *not* have otherwise considered.

At *June 30, 2018* and *2017*, the Corporation had *\$1,269* and *\$1,740*, respectively, of loans classified as TDRs which are included in impaired loans above. At *June 30, 2018* and *2017*, the Corporation had *\$29* and *\$33*, respectively, of specific reserves allocated to these loans.

There were *no* loan modifications completed during the *2018* fiscal year that were classified as troubled debt restructurings. As of *June 30, 2018*, the Corporation had committed to lend an additional *\$174* to customers with outstanding loans that were classified as troubled debt restructurings.

During the fiscal year ended *June 30, 2017*, the terms of certain loans were modified as troubled debt restructurings. The modification of the terms of such loans included a combination of an extension of the maturity date and the extension of additional credit to provide operating funds. The following table presents loans by class modified as troubled debt restructurings that occurred during the year ended *June 30, 2017*:

|                         |           | Pre-Modification | Post-Modification |
|-------------------------|-----------|------------------|-------------------|
|                         | Number of | Outstanding      | Outstanding       |
|                         | Loans     | Recorded         | Recorded          |
|                         |           | Investment       | Investment        |
| Commercial              | 2         | \$ 518           | \$ 518            |
| Commercial real estate: |           |                  |                   |
| Other                   | 1         | 512              | 512               |
| Total                   | 3         | \$ 1,030         | \$ 1,030          |

The troubled debt restructurings described above did *not* increase the allowance for loan losses or result in any charge-offs during the *twelve* months ended *June 30, 2017*. As of *June 30, 2017*, the Corporation had committed to lend an additional *\$175* as part of the restructurings described above. There were *no* loans classified as troubled debt

restructurings that were modified within the last *twelve* months for which there was a payment default.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

**Credit Quality Indicators:**

The Corporation categorizes loans into risk categories based on relevant information about the ability of 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 loans with a total outstanding loan relationship greater than \$100 and non-homogeneous loans, such as commercial and commercial real estate loans. This analysis is performed on a monthly basis. The Corporation uses the following definitions for risk ratings:

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

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

**Doubtful.** Loans classified as doubtful have all 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 existing facts, conditions, and values, highly questionable and improbable.

Loans *not* meeting the criteria above that are analyzed individually as part of the above described process are considered to be pass rated loans. Loans listed as *not* rated are either less than \$100 or are included in groups of homogeneous loans. These loans are evaluated based on delinquency status, which was discussed previously.

As of June 30, 2018, and based on the most recent analysis performed, the recorded investment by risk category of loans by class of loans is as follows:

|            | Pass     | Special<br>Mention | Substandard | Doubtful | Not<br>Rated |
|------------|----------|--------------------|-------------|----------|--------------|
| Commercial | \$59,214 | \$ 288             | \$ 1,162    | \$ —     | \$415        |

|                                     |           |          |          |          |          |
|-------------------------------------|-----------|----------|----------|----------|----------|
| Commercial real estate:             |           |          |          |          |          |
| Construction                        | 5,386     | —        | —        | —        | —        |
| Other                               | 172,471   | 7,061    | 1,878    | 702      | 1,255    |
| 1-4 Family residential real estate: |           |          |          |          |          |
| Owner occupied                      | 2,577     | —        | 27       | 11       | 45,214   |
| Non-owner occupied                  | 14,025    | 195      | 417      | 298      | 579      |
| Construction                        | 8         | —        | —        | —        | 1,182    |
| Consumer                            | 93        | —        | —        | —        | 4,783    |
| Total                               | \$253,774 | \$ 7,544 | \$ 3,484 | \$ 1,011 | \$53,428 |

As of *June 30, 2017*, and based on the most recent analysis performed, the recorded investment by risk category of loans by class of loans is as follows:

|                                     | Pass      | Special<br>Mention | Substandard | Doubtful | Not<br>Rated |
|-------------------------------------|-----------|--------------------|-------------|----------|--------------|
| Commercial                          | \$44,435  | \$ 907             | \$ 642      | \$ —     | \$453        |
| Commercial real estate:             |           |                    |             |          |              |
| Construction                        | 4,514     | 1,035              | —           | 4        | 43           |
| Other                               | 150,460   | 5,110              | 1,566       | 470      | 561          |
| 1-4 Family residential real estate: |           |                    |             |          |              |
| Owner occupied                      | 2,668     | —                  | 11          | 30       | 38,983       |
| Non-owner occupied                  | 13,633    | 210                | 261         | 187      | 125          |
| Construction                        | 1,223     | —                  | —           | —        | 773          |
| Consumer                            | 145       | —                  | —           | —        | 4,999        |
| Total                               | \$217,078 | \$ 7,262           | \$ 2,480    | \$ 691   | \$45,937     |

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

**NOTE 4—PREMISES AND EQUIPMENT**

Major classifications of premises and equipment were as follows as of *June 30*:

|   | <b>2018</b> | <b>2017</b> |
|---|-------------|-------------|
| Land                                      | \$1,469     | \$1,469     |
| Land improvements                         | 344         | 340         |
| Building and leasehold improvements       | 12,636      | 12,180      |
| Furniture, fixture and equipment          | 5,164       | 5,023       |
| Total premises and equipment              | 19,613      | 19,012      |
| Accumulated depreciation and amortization | (6,298 )    | (5,614 )    |
| Premises and equipment, net               | \$13,315    | \$13,398    |

Depreciation expense was \$771 and \$781 for the years ended *June 30, 2018* and *2017*, respectively.

The Corporation is obligated under non-cancelable operating leases for facilities and equipment. The approximate minimum annual rentals and commitments under these non-cancelable agreements and leases with remaining terms in excess of *one* year are as follows:

| <u>Twelve Months Ending June 30</u> |       |
|-------------------------------------|-------|
| 2019                                | \$83  |
| 2020                                | 85    |
| 2021                                | 78    |
| 2022                                | 71    |
| Thereafter                          | 65    |
| Total                               | \$382 |

Rent expense incurred was \$159 and \$158 during the years ended *June 30, 2018* and *2017*, respectively.

**NOTE 5—DEPOSITS**

The aggregate amount of time deposits, each with a minimum denomination of \$250 was \$23,018 and \$14,252 as of *June 30, 2018* and *2017*, respectively.

Scheduled maturities of time deposits at *June 30, 2018* were as follows:

**Twelve Months Ending June 30**

|            |          |
|------------|----------|
| 2019       | \$37,984 |
| 2020       | 24,575   |
| 2021       | 6,261    |
| 2022       | 7,528    |
| 2023       | 1,472    |
| Thereafter | 721      |
|            | \$78,541 |

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

**NOTE 6—SHORT-TERM BORROWINGS**

Short-term borrowings consisted of repurchase agreements and federal fund purchased. Information concerning all short-term borrowings at *June 30, 2018* and *2017*, maturing in less than *one* year is summarized as follows:

|                                       | <b>2018</b> |  | <b>2017</b> |
|---------------------------------------|-------------|--|-------------|
| Balance at June 30                    | \$13,367    |  | \$23,986    |
| Average balance during the year       | 24,422      |  | 21,053      |
| Maximum month-end balance             | 28,621      |  | 28,073      |
| Average interest rate during the year | 0.98 %      |  | 0.43 %      |
| Weighted average rate, June 30        | 1.02 %      |  | 0.82 %      |

Securities sold under agreements to repurchase are utilized to facilitate the needs of our customers. Physical control is maintained for all securities pledged to secure repurchase agreements. Securities available-for-sale pledged for repurchase agreements as of *June 30, 2018* and *2017* are presented in the following table:

|   | <b>Overnight and<br/>Continuous</b> |             |
|---|-------------------------------------|-------------|
|   | <b>2018</b>                         | <b>2017</b> |
| U.S. government-sponsored entities and agencies pledged | \$—                                 | \$2,015     |
| Residential mortgage-backed securities pledged          | 5,294                               | 20,923      |
| Collateralized mortgage obligations pledged             | —                                   | 2,355       |
| Total pledged   | \$5,294                             | \$25,293    |
| Repurchase agreements                                   | \$4,486                             | \$23,986    |

Total interest expense on short-term borrowings was \$240 and \$90 for the years ended *June 30, 2018* and *2017*, respectively.

**NOTE 7—FEDERAL HOME LOAN BANK ADVANCES**



A summary of Federal Home Loan Bank (FHLB) advances were as follows:

| Advance Type           | June 30, 2018        |       |          |      | June 30, 2017 |      |   |
|------------------------|----------------------|-------|----------|------|---------------|------|---|
|                        | Stated Interest Rate |       | Weighted |      | Weighted      |      |   |
|                        | Range                |       | Average  |      | Average       |      |   |
|                        | From                 | To    | Amount   | Rate | Amount        | Rate |   |
| Fixed-rate, amortizing | 4.30%                | 4.30% | \$56     | 4.30 | % \$120       | 4.30 | % |
| Fixed-rate             | 1.16                 | 1.78  | 11,700   | 1.46 | 12,200        | 1.47 |   |

Each fixed rate advance has a prepayment penalty equal to the present value of 100% of the lost cash flow based upon the difference between the contract rate on the advance and the current rate on a comparable new advance. The following table is a summary of the scheduled principal payments for all advances:

| <u>Twelve Months Ending June 30</u> | <u>Principal Payments</u> |
|-------------------------------------|---------------------------|
| 2019                                | \$ 2,056                  |
| 2020                                | 1,500                     |
| 2021                                | 1,500                     |
| 2022                                | 1,700                     |
| Thereafter                          | 5,000                     |
| Total                               | \$ 11,756                 |

Pursuant to collateral agreements with the FHLB, advances are secured by all the stock invested in the FHLB and certain qualifying *first* mortgage and multi-family loans. The advances were collateralized by \$53,572 and \$49,023 of *first* mortgage and multi-family loans under a blanket lien arrangement at *June 30, 2018* and *2017*, respectively. Based on this collateral and the Corporation's holdings of FHLB stock, the Bank was eligible to borrow up to a total of \$14,892 in additional advances at *June 30, 2018*.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

**NOTE 8—EMPLOYEE BENEFIT PLANS**

The Bank maintains a 401(k) savings and retirement plan that permits eligible employees to make before- or after-tax contributions to the plan, subject to the dollar limits from Internal Revenue Service regulations. The Bank matches 100% of the employee's voluntary contributions to the plan based on the amount of each participant's contributions up to a maximum of 4% of eligible compensation. All regular full-time and part-time employees who complete six months of service and are at least 21 years of age are eligible to participate. Amounts charged to operations were \$206 and \$190 for the years ended June 30, 2018 and 2017, respectively.

The Bank maintains a nonqualified Salary Continuation Plan (SCP) to reward and encourage certain Bank executives to remain employees of the Bank. The SCP is considered an unfunded plan for tax and Employee Retirement Income Security Act (ERISA) purposes and all obligations arising under the SCP are payable from the general assets of the Corporation. The estimated present value of future benefits to be paid to certain current and former executives totaled \$2,321 as of June 30, 2018 and \$2,152 as of June 30, 2017 and is included in other liabilities. For purposes of calculating the present value of future benefits, the discount rate in effect at June 30, 2018 and 2017 was 4.5%. For the years ended June 30, 2018 and 2017, \$225 and \$196, respectively, have been charged to expense in connection with the SCP. Distributions to participants were \$56 and \$64 for the years ending June 30, 2018 and 2017, respectively.

The 2010 Omnibus Incentive Plan (2010 Plan) is a nonqualified share based compensation plan. The 2010 Plan was established to promote alignment between key employees' performance and the Corporation's shareholder interests by motivating performance through the award of stock-based compensation. The 2010 Plan is intended to attract, retain and motivate talented employees and compensate outside directors for their service to the Corporation. The 2010 Plan has been approved by the Corporation's shareholders. The Compensation Committee of the Corporation's Board of Directors has sole authority to select the employees, establish the awards to be issued, and approve the terms and conditions of each award contract.

Under the 2010 Plan, the Corporation may grant, among other things, nonqualified stock options, incentive stock options, stock appreciation rights, restricted stock, restricted stock units, or any combination thereof to any employee and outside director. Each award is evidenced by an award agreement that specifies the number of shares awarded, the vesting period, the performance requirements, and such other provisions as the Compensation Committee determines. Upon a change-in-control of the Corporation, as defined in the 2010 Plan, all outstanding awards immediately vest.

The Corporation has granted restricted stock awards to certain employees and directors. Restricted stock awards are issued at *no* cost to the recipient and can be settled only in shares at the end of the vesting period. If certain specified performance targets as established by the Compensation Committee are achieved, awards vest at the end of the measurement period of the specified performance targets and on each anniversary date of the award over a *three*-year period. Restricted stock awards provide the holder with full voting rights and dividends during the vesting period. Cash dividends are reinvested into shares of stock and are subject to the same restrictions and vesting as the initial award. All dividends are forfeitable in the event the shares do *not* vest. The fair value of the restricted stock awards, which is used to measure compensation expense, is the closing market price of the Corporation's common stock on the date of the grant and compensation expense is recognized over the vesting period of the awards. Restricted stock awarded during the period presented vest under a graduated schedule over a *three*-year period.

The following table summarizes the status of the restricted stock awards:

|                              | <b>Restricted<br/>Stock<br/>Awards</b> | <b>Weighted-<br/>Average<br/>Grant<br/>Date Fair<br/>Value Per<br/>Share</b> |
|------------------------------|--|--|
| Outstanding at June 30, 2017 | 1,429                                  | \$ 15.75   |
| Granted                      | 6,321                                  | 21.00  |
| Vested                       | (4,259 )                               | 21.00  |
| Expired                      | (1,429 )                               | 15.75  |
| Non-vested at June 30, 2018  | 2,062                                  | \$ 21.00   |

There was \$101 in expense recognized in the 2018 fiscal year in connection with the restricted stock awards. There was *no* expense recognized in the 2017 fiscal year in connection with the restricted stock awards since grants scheduled to vest expired due to *not* meeting the performance target. As of *June 30, 2018*, there was \$43 of total unrecognized compensation expense related to non-vested shares and the expense is expected to be recognized over the next *two* years.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

**NOTE 9—INCOME TAXES**

On *December 22, 2017*, the U.S. government enacted comprehensive tax legislation commonly referred to as the Tax Cuts and Jobs Act (Tax Act). The Tax Act significantly revised the future ongoing U.S. corporate income tax structure by, among other things, decreasing U.S. corporate income tax rates to *21.0%* from a maximum of *35.0%*. As the Corporation has a *June 30* fiscal year-end, the lower corporate income tax rate will be phased in, resulting in a blended U.S. statutory federal rate of approximately *27.55%* for the Corporation's fiscal year ending *June 30, 2018*, and *21.0%* for subsequent fiscal years. The provision for income taxes consisted of the following for the years ended *June 30*, calculated utilizing a statutory federal income tax rate of *27.55%* in the *2018* fiscal year and *34.0%* in the *2017* fiscal year:

|                              | <b>2018</b> | <b>2017</b> |
|------------------------------|-------------|-------------|
| Current income taxes         | \$687       | \$513       |
| Deferred income tax expense  | 114         | 128         |
| Change in corporate tax rate | 348         | —           |
| Total income tax expense     | \$1,149     | \$641       |

The reduction of the corporate tax rate required the Corporation to revalue its deferred tax assets and liabilities based on the lower federal tax rate of *21.0%*. As a result of the new legislation, during the quarter ended *December 31, 2017*, the Corporation recorded a charge to income tax expense of \$348 in conjunction with writing down its net deferred tax assets. The net deferred income tax asset consisted of the following components at *June 30*:

|   | <b>2018</b> | <b>2017</b> |
|---|-------------|-------------|
| Deferred tax assets:                      |             |             |
| Allowance for loan losses                 | \$632       | \$919       |
| Deferred compensation                     | 514         | 771         |
| Recognized loss on impairment of security | 164         | 265         |
| AMT credit carryforward                   | —           | 220         |
| Deferred income                           | 68          | 131         |
| Other real estate owned write down        | —           | 10          |
| Non-accrual loan interest income          | 42          | 58          |
| Net unrealized securities loss            | 435         | —           |
| Gross deferred tax asset                  | 1,855       | 2,374       |
| Deferred tax liabilities:                 |             |             |
| Depreciation                              | (489 )      | (788 )      |

|                                |        |         |
|--------------------------------|--------|---------|
| Loan fees                      | (238 ) | (320 )  |
| FHLB stock dividends           | (102 ) | (166 )  |
| Prepaid expenses               | (56 )  | (89 )   |
| Net unrealized securities gain | —      | (229 )  |
| Gross deferred tax liabilities | (885 ) | (1,592) |
| Net deferred asset             | \$970  | \$782   |

The difference between the provision for income taxes and amounts computed by applying the statutory income tax rate of 27.55% for 2018 and 34% for 2017 to income before taxes consisted of the following for the years ended *June 30*:

|  | <b>2018</b> | <b>2017</b> |
|--|-------------|-------------|
| Income taxes computed at the statutory rate on pretax income | \$1,303     | \$1,236     |
| Tax exempt income  | (408 )      | (498 )      |
| Cash surrender value income                                  | (75 )       | (83 )       |
| Tax credit   | (27 )       | (25 )       |
| Change in corporate tax rate                                 | 348         | —           |
| Other  | 8           | 11          |
| Total income tax expense                                     | \$1,149     | \$641       |

The effective tax rate was 24.3% for the year ended *June 30, 2018* compared to 17.6% for the year ended *June 30, 2017*. At *June 30, 2018* and *June 30, 2017*, the Corporation had *no* unrecognized tax benefits recorded. The Corporation does *not* expect the total amount of unrecognized tax benefits to significantly increase within the next *twelve* months. There were *no* interest or penalties recorded for the years ended *June 30, 2018* and *2017* and there were *no* amounts accrued for interest and penalties at *June 30, 2018* and *2017*.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The Corporation and the Bank are subject to U.S. federal income tax as an income-based tax and a capital-based franchise tax in the State of Ohio. The Corporation and the Bank are *no* longer subject to examination by taxing authorities for years before *2014*.

**NOTE 10—RELATED PARTY TRANSACTIONS**

In the ordinary course of business, the Bank has granted loans to certain executive officers, directors and their affiliates. A summary of activity during the year ended *June 30, 2018* of related party loans were as follows:

|                            |          |
|----------------------------|----------|
| Principal balance, July 1  | \$9,487  |
| New loans                  | 3,786    |
| Repayments                 | (2,135 ) |
| Principal balance, June 30 | \$11,138 |

Deposits from executive officers, directors and their affiliates totaled \$5,897 at *June 30, 2018* and \$4,828 at *June 30, 2017*.

**NOTE 11—REGULATORY MATTERS**

The Bank is subject to regulatory capital requirements administered by federal banking agencies. Capital adequacy guidelines and prompt corrective-action regulations involve quantitative measures of assets, liabilities, and certain off-balance-sheet items calculated under regulatory accounting practices. Capital amounts and classifications are also subject to qualitative judgments by regulators about components, risk weightings, and other factors and the regulators can lower classifications in certain cases. Failure to meet various capital requirements can initiate regulatory action that could have a direct material effect on the financial statements. Management believes as of *June 30, 2018*, the Bank has met all capital adequacy requirements to which it is subject.

The prompt corrective action regulations provide *five* classifications, including well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized, and critically undercapitalized, although these terms are

*not* used to represent overall financial condition. If adequately capitalized, regulatory approval is required to accept brokered deposits. If undercapitalized, capital distributions are limited, as is asset growth and expansion, and plans for capital restoration are required.

As of fiscal year-end 2018 and 2017, the Corporation met the definition of a small bank holding company and, therefore, was exempt from consolidated risk-based and leverage capital adequacy guidelines for bank holding companies. The Basel III Capital Rules became effective for the Bank on *January 1, 2015* and certain provisions are subject to a phase-in period. The implementation of the capital conservation buffer began on *January 1, 2016* at the 0.625% level and will be phased in over a *four*-year period (increasing by that amount on each subsequent *January 1*, until it reaches 2.5% on *January 1, 2019*). The capital conservation buffer for 2018 is 1.875%. The capital conservation buffer is designed to absorb losses during periods of economic stress. Banking institutions with a ratio of Common Equity Tier 1 capital to risk-weighted assets above the minimum but below the conservation buffer will face constraints on dividends, equity repurchases and compensation based on the amount of the shortfall. The net unrealized gain or loss on available for sale securities is *not* included in computing regulatory capital.

The following table presents actual and required capital ratios as of *June 30, 2018* and *June 30, 2017* for the Bank:

|  | Actual |        | Minimum Capital Required – Basel III (1) |        | Minimum Required To Be Considered Well Capitalized |        |
|--|--------|--------|--|--------|--|--------|
|  |        |        | Amount                                   | Ratio  | Amount   | Ratio  |
| <b>June 30, 2018</b>                         |        |        |  |        |  |        |
| Common equity Tier 1 to risk-weighted assets | \$43.7 | 12.20% | \$16.1                                   | 4.50 % | \$23.3   | 6.50 % |
| Tier 1 capital to risk weighted assets       | 43.7   | 12.20  | 21.5                                     | 6.00   | 28.7   | 8.00   |
| Total Capital to risk weighted assets        | 47.1   | 13.15  | 28.7                                     | 8.00   | 35.8   | 10.00  |
| Tier 1 capital to average assets             | 43.7   | 8.74   | 20.0                                     | 4.00   | 25.0   | 5.00   |

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

|   | Actual |        | Minimum<br>Capital<br>Required<br>- Basel III<br>(1) |       | Minimum<br>Required<br>To Be<br>Considered<br>Well<br>Capitalized |       |
|---|--------|--------|--|-------|---|-------|
|   | Amount | Ratio  | Amount   | Ratio | Amount  | Ratio |
| <b>June 30, 2017</b>                              |        |        |  |       |   |       |
| Common equity Tier 1 to risk-weighted assets Bank | \$41.4 | 13.21% | \$18.0   | 4.50% | \$20.4  | 6.50% |
| Tier 1 capital to risk weighted assets            | 41.4   | 13.21  | 22.7   | 6.00  | 25.1  | 8.00  |
| Total Capital to risk weighted assets             | 44.5   | 14.20  | 29.0   | 8.00  | 31.4  | 10.00 |
| Tier 1 capital to average assets                  | 41.4   | 9.06   | 18.3   | 4.00  | 22.9  | 5.00  |

(1) These amounts exclude the capital conservation buffer.

As of the latest regulatory examination, the Bank was categorized as well capitalized. There are *no* conditions or events since that examination that management believes *may* have changed the Bank's category.

The Corporation's principal source of funds for dividend payment is dividends received 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 net profits, combined with the retained net profits of the preceding *two* years, subject to the capital requirements described above. As of *June 30, 2018* the Bank could, without prior approval, declare a dividend of approximately \$4,448.

**NOTE 12—COMMITMENTS WITH OFF-BALANCE SHEET RISK**

The Bank is a party to commitments to extend credit in the normal course of business to meet the financing needs of its customers. Commitments are agreements to lend to customers providing that there are *no* violations of any condition established in the contract. Commitments to extend credit have a fixed expiration date or other termination clause. These instruments involve elements of credit and interest rate risk more than the amount recognized in the statements of financial position. The Bank uses the same credit policies in making commitments to extend credit as it does for on-balance sheet instruments.



The Bank evaluates each customer's credit on a case-by-case basis. The amount of collateral obtained is based on management's credit evaluation of the customer. The amount of commitments to extend credit and the exposure to credit loss for non-performance by the customer was \$62,764 and \$53,029 as of *June 30, 2018* and *2017*, respectively. Of the *June 30, 2018* commitments, \$53,082 carried variable rates and \$9,682 carried fixed rates of interest ranging from 3.375% to 6.50% with maturity dates from *August 2018* to *June 2048*. Of the *June 30, 2017* commitments, \$41,167 carried variable rates and \$11,862 carried fixed rates of interest ranging from 2.45% to 6.50%. Financial standby letters of credit were \$1,090 as of *June 30, 2018* and \$713 as of *June 30, 2017*. In addition, commitments to extend credit of \$8,493 and \$8,121 as of *June 30, 2018* and *2017*, respectively, were available to checking account customers related to the overdraft protection program. Since some loan commitments expire without being used, the amount does *not* necessarily represent future cash commitments.

### NOTE 13—FAIR VALUE

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

**Level 1:** Quoted prices (unadjusted) for 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 company's own assumptions about the assumptions that market participants would use in pricing an asset or liability.

Financial assets and financial liabilities measured at fair value on a recurring basis include the following:

**Securities available-for-sale:** When available, the fair values of available-for-sale securities are determined by obtaining quoted prices on nationally recognized securities exchanges (Level 1 inputs). For securities where quoted market prices are *not* available, fair values are calculated based on market prices of similar securities (Level 2 inputs). For securities where quoted prices or market prices of similar securities are *not* available, fair values are calculated using discounted cash flows or other unobservable inputs (Level 3 inputs).



## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Assets and liabilities measured at fair value on a recurring basis are summarized below, segregated by the level of the valuation inputs within the fair value hierarchy utilized to measure fair value:

|  | Balance<br>at<br>June 30,<br>2018 | Fair Value<br>Measurements at<br>June 30, 2018 Using |          |            |
|--|-----------------------------------|--|----------|------------|
|  |                                   | Level<br>1   | Level 2  | Level<br>3 |
|  |                                   |  |          |            |
| Assets:  |                                   |  |          |            |
| Securities available-for-sale:                   |                                   |  |          |            |
| Obligations of government-sponsored entities     | \$16,122                          | \$—  | \$16,122 | \$—        |
| Obligations of states and political subdivisions | 56,590                            | —  | 56,590   | —          |
| Mortgage-backed securities - residential         | 63,408                            | —  | 63,408   | —          |
| Mortgage-backed securities - commercial          | 1,415                             | —  | 1,415    | —          |
| Collateralized mortgage obligations              | 5,766                             | —  | 5,766    | —          |
| Pooled trust preferred security                  | 727                               | —  | 727      | —          |

|  | Balance<br>at<br>June 30,<br>2017 | Fair Value<br>Measurements at<br>June 30, 2017 Using |          |            |
|--|-----------------------------------|--|----------|------------|
|  |                                   | Level<br>1   | Level 2  | Level<br>3 |
|  |                                   |  |          |            |
| Securities available-for-sale:                   |                                   |  |          |            |
| Obligations of government-sponsored entities     | \$12,587                          | \$—  | \$12,587 | \$—        |
| Obligations of states and political subdivisions | 57,460                            | —  | 57,460   | —          |
| Mortgage-backed securities - residential         | 63,838                            | —  | 63,838   | —          |
| Mortgage-backed securities - commercial          | 1,458                             | —  | 1,458    | —          |
| Collateralized mortgage obligations              | 6,211                             | —  | 6,211    | —          |
| Pooled trust preferred security                  | 532                               | —  | 532      | —          |

There were *no* transfers between Level 1 and Level 2 during the 2017 or the 2018 fiscal year.

Certain financial assets and financial liabilities are measured at fair value on a non-recurring basis; that is, the instruments are *not* measured at fair value on an ongoing basis but are subject to fair value adjustments in certain circumstances. Financial assets and financial liabilities measured at fair value on a non-recurring basis include the following:

**Impaired Loans:** At the time a loan is considered impaired, it is valued at the lower of cost or fair value. Impaired loans carried at fair value generally receive specific allocations of the allowance for loan losses or are charged down to their fair value. For collateral dependent loans, fair value is commonly based on recent real estate appraisals. These appraisals *may* utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Adjustments are routinely made in the appraisal process by the appraisers to adjust for differences between the comparable sales and income data available. Such adjustments are usually significant and typically result in a Level 3 classification of the inputs for determining fair value.

**Other Real Estate Owned:** Assets acquired through or instead of loan foreclosure are initially recorded at fair value less costs to sell when acquired, establishing a new cost basis. These assets are subsequently accounted for at lower of cost or fair value less estimated costs to sell. Real estate owned properties are evaluated on a quarterly basis for additional impairment and adjusted accordingly.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

There were *no* financial assets measured at fair value on a non-recurring basis at *June 30, 2018*. Financial assets and financial liabilities measured at fair value on a non-recurring basis at *June 30, 2017* are summarized below:

|                                    | Fair Value Measurements at |         |         |
|------------------------------------|----------------------------|---------|---------|
|                                    | June 30, 2017              |         |         |
| Balance at                         | Using                      |         |         |
| June 30, 2017                      | Level 1                    | Level 2 | Level 3 |
| Impaired loans:                    |                            |         |         |
| Commercial Real Estate - Other     | \$ 130                     | \$—     | \$—     |
| Other Real Estate Owned:           |                            |         |         |
| 1-4 Family residential real estate | \$ 71                      | \$—     | \$—     |

There were *no* impaired loans measured at fair value on a non-recurring basis at *June 30, 2018* and the resulting impact to the provision for loan losses was a decrease of \$17 being recorded for the *twelve* months ended *June 30, 2018*. Impaired loans, measured for impairment using the fair value of the collateral, had a recorded investment of \$130, with *no* valuation allowance at *June 30, 2017*. The resulting impact to the provision for loan losses was an increase of \$314 being recorded for the year ended *June 30, 2017*.

Other real estate owned, which is measured at the lower of carrying or fair value less costs to sell, had a net carrying amount of \$71, which was made up of the outstanding balance of \$103, net of a valuation allowance of \$32 at *June 30, 2017*, resulting in a provision for other real estate owned losses of \$32 for the year ended *June 30, 2017*. There was *no* other real estate owned at *June 30, 2018*.

The following table presents quantitative information about Level 3 fair value measurements for financial instruments measured at fair value on a non-recurring basis at *June 30, 2017*:

| Fair Value | Valuation | Unobservable | Range | Weighted |
|------------|-----------|--------------|-------|----------|
|------------|-----------|--------------|-------|----------|

|                                    |        | <b>Technique</b> | <b>Inputs</b> | <b>Average</b> |   |     |   |
|------------------------------------|--------|------------------|---------------|----------------|---|-----|---|
| Impaired loans:                    |        |                  |               |                |   |     |   |
| Commercial Real Estate – Other     | \$ 130 | Bid Indication   | N/A           | 0.0            | % | 0.0 | % |
| Other Real Estate Owned:           |        |                  |               |                |   |     |   |
| 1-4 Family residential real estate | \$ 71  | Bid Indication   | N/A           | 0.0            | % | 0.0 | % |

The following table shows the estimated fair values of financial instruments that are reported at amortized cost in the Corporation's consolidated balance sheets, segregated by the level of the valuation inputs within the fair value hierarchy utilized to measure fair value:

|  | <b>2018</b>            |                             | <b>2017</b>            |                             |
|--|------------------------|-----------------------------|------------------------|-----------------------------|
|  | <b>Carrying Amount</b> | <b>Estimated Fair Value</b> | <b>Carrying Amount</b> | <b>Estimated Fair Value</b> |
| <b>Financial Assets:</b>                                 |                        |                             |                        |                             |
| Level 1 inputs:  |                        |                             |                        |                             |
| Cash and cash equivalents                                | \$ 7,772               | \$ 7,772                    | \$ 9,912               | \$ 9,912                    |
| Level 2 inputs:  |                        |                             |                        |                             |
| Certificates of deposits in other financial institutions | 2,973                  | 2,976                       | 3,921                  | 3,927                       |
| Loans held for sale                                      | 1,448                  | 1,474                       | 1,252                  | 1,286                       |
| Accrued interest receivable                              | 1,404                  | 1,404                       | 1,212                  | 1,212                       |
| Level 3 inputs:  |                        |                             |                        |                             |
| Securities held-to-maturity                              | 4,024                  | 4,048                       | 4,259                  | 4,329                       |
| Loans, net   | 315,087                | 311,642                     | 269,781                | 266,041                     |
| <b>Financial Liabilities:</b>                            |                        |                             |                        |                             |
| Level 2 inputs:  |                        |                             |                        |                             |
| Demand and savings deposits                              | 351,422                | 351,422                     | 307,960                | 307,960                     |
| Time deposits  | 78,541                 | 78,332                      | 66,511                 | 66,535                      |
| Short-term borrowings                                    | 13,367                 | 13,367                      | 23,986                 | 23,986                      |
| Federal Home Loan Bank advances                          | 11,756                 | 11,146                      | 12,320                 | 12,054                      |
| Accrued interest payable                                 | 68                     | 68                          | 40                     | 40                          |

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The assumptions used to estimate fair value are described as follows:

**Cash and cash equivalents:** The carrying value of cash, deposits in other financial institutions and federal funds sold were considered to approximate fair value resulting in a Level 1 classification.

**Certificates of deposits in other financial institutions:** Fair value of certificates of deposits in other financial institutions was estimated using current rates for deposits of similar remaining maturities resulting in a Level 2 classification.

**Accrued interest receivable and payable, demand and savings deposits and short-term borrowings:** The carrying value of accrued interest receivable and payable, demand and savings deposits and short-term borrowings were considered to approximate fair value due to their short-term duration resulting in a Level 2 classification.

**Loans held for sale:** The fair value of loans held for sale is estimated based upon binding contracts and quotes from *third* party investors resulting in a Level 2 classification.

**Loans:** Fair value for loans was estimated for portfolios of loans with similar financial characteristics. For adjustable rate loans that reprice at least annually and for fixed rate commercial loans with maturities of *six* months or less which possess normal risk characteristics, carrying value was determined to be fair value. Fair value of other types of loans (including adjustable rate loans which reprice less frequently than annually and fixed rate term loans or loans which possess higher risk characteristics) was estimated by discounting future cash flows using the current rates at which similar loans would be made to borrowers with similar credit ratings and for similar anticipated maturities resulting in a Level 3 classification. The methods utilized to estimate the fair value of loans do *not* necessarily represent an exit price.

**Securities held-to-maturity:** The held-to-maturity securities are general obligation and revenue bonds issued by local municipalities. The fair value of these securities are calculated using a spread to the applicable municipal fair market curve resulting in a Level 3 classification.

**Time deposits:** Fair value of fixed-maturity certificates of deposit was estimated using the rates offered at *June 30, 2018* and *2017* for deposits of similar remaining maturities, resulting in Level 2 classification. Estimated fair value does *not* include the benefit that results from low-cost funding provided by the deposit liabilities compared to the cost of borrowing funds in the market.

**Federal Home Loan Bank advances:** Fair value of Federal Home Loan Bank advances was estimated using current rates at *June 30, 2018* and *2017* for similar financing resulting in a Level 2 classification.

**Federal bank and other restricted stocks, at cost:** Federal bank and other restricted stocks include stock acquired for regulatory purposes, such as Federal Home Loan Bank stock and Federal Reserve Bank stock that are accounted for at cost due to restrictions placed on their transferability, and, therefore, are *not* subject to the fair value disclosure requirements.

**Off-balance sheet commitments:** The Corporation's lending commitments have variable interest rates and "escape" clauses if the customer's credit quality deteriorates. Therefore, the fair values of these items are *not* significant and are *not* included in the above table.



## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

## NOTE 14—PARENT COMPANY FINANCIAL STATEMENTS

The condensed financial information of Consumers Bancorp. Inc. (parent company only) follows:

|   | <b>June<br/>30,<br/>2018</b> | <b>June<br/>30,<br/>2017</b> |          | <b>Year<br/>Ended<br/>June<br/>30,<br/>2018</b> | <b>Year<br/>Ended<br/>June<br/>30,<br/>2017</b> |
|---|------------------------------|------------------------------|----------|---|---|
| <b>Condensed Balance Sheets</b>   |                              |                              |          |   |   |
| Assets  |                              |                              |          |   |   |
| Cash  | \$46                         | \$36                         |          |   |   |
| Securities, available-for-sale  | 1,622                        | 1,651                        |          |   |   |
| Other assets  | 73                           | 61                           |          |   |   |
| Investment in subsidiary  | 42,089                       | 41,843                       |          |   |   |
| Total assets  | \$43,830                     | \$43,591                     |          |   |   |
| Liabilities   |                              |                              |          |   |   |
| Other liabilities   | \$69                         | \$56                         |          |   |   |
| Shareholders' equity  | 43,761                       | 43,535                       |          |   |   |
| Total liabilities & shareholders' equity  | \$43,830                     | \$43,591                     |          |   |   |
| <b>Condensed Statements of Income and Comprehensive Income</b>                  |                              |                              |          |   |   |
| Cash dividends from Bank subsidiary   |                              |                              | \$ 1,400 | \$ 1,065  |   |
| Other income  |                              |                              | 39       | 51  |   |
| Other expense   |                              |                              | 222      | 213   |   |
| Income before income taxes and equity in undistributed net income of subsidiary |                              |                              | 1,217    | 903   |   |
| Income tax benefit  |                              |                              | (52 )    | (53 )   |   |
| Income before equity in undistributed net income of Bank subsidiary             |                              |                              | 1,269    | 956   |   |
| Equity in undistributed net income of subsidiary                                |                              |                              | 2,312    | 2,038   |   |
| Net income  |                              |                              | \$ 3,581 | \$ 2,994  |   |
| Comprehensive income  |                              |                              | \$ 1,487 | \$ 1,050  |   |

**Year      Year  
Ended    Ended**

|   | <b>June<br/>30,<br/>2018</b> | <b>June<br/>30,<br/>2017</b> |
|---|------------------------------|------------------------------|
| <b>Condensed Statements of Cash Flows</b>               |                              |                              |
| Cash flows from operating activities                    |                              |                              |
| Net income  | \$3,581                      | \$2,994                      |
| Equity in undistributed net income of Bank subsidiary   | (2,312)                      | (2,038)                      |
| Securities amortization and accretion, net              | (10 )                        | (10 )                        |
| Gain on sale of securities                              | —                            | (11 )                        |
| Change in other assets and liabilities                  | 12                           | 6                            |
| Net cash flows from operating activities                | 1,271                        | 941                          |
| Cash flows from investing activities                    |                              |                              |
| Proceeds from the sale of available-for-sale securities | —                            | 357                          |
| Net cash flows from investing activities                | —                            | 357                          |
| Cash flows from financing activities                    |                              |                              |
| Dividend paid   | (1,351)                      | (1,308)                      |
| Issuance of treasury stock for stock awards             | 90                           | —                            |
| Net cash flows from financing activities                | (1,261)                      | (1,308)                      |
| Change in cash and cash equivalents                     | 10                           | (10 )                        |
| Beginning cash and cash equivalents                     | 36                           | 46                           |
| Ending cash and cash equivalents                        | \$46                         | \$36                         |

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

**NOTE 15—EARNINGS PER SHARE**

Basic earnings per share is the amount of earnings available to each share of common stock outstanding during the reporting period and is equal to net income divided by the weighted average number of shares outstanding during the period. Diluted earnings per share is the amount of earnings available to each share of common stock outstanding during the reporting period adjusted to include the effect of potentially dilutive common shares that *may* be issued upon the vesting of restricted stock awards. There were 1,828 shares of restricted stock that were anti-dilutive for the year ending *June 30, 2018*. There were *no* equity instruments that were anti-dilutive for the year ending *June 30, 2017*. The following table details the calculation of basic and diluted earnings per share:

|  | <b>For the year Ended<br/>June 30,</b> |             |
|--|--|-------------|
|  | <b>2018</b>                            | <b>2017</b> |
| <b>Basic:</b>  |  |             |
| Net income available to common shareholders              | \$3,581                                | \$2,994     |
| Weighted average common shares outstanding               | 2,726,926                              | 2,724,293   |
| Basic income per share                                   | \$1.31                                 | \$1.10      |
| <b>Diluted:</b>  |  |             |
| Net income available to common shareholders              | \$3,581                                | \$2,994     |
| Weighted average common shares outstanding               | 2,726,926                              | 2,724,293   |
| Dilutive effect of restricted stock                      | —                                      | 32          |
| Total common shares and dilutive potential common shares | 2,726,926                              | 2,724,325   |
| Dilutive income per share                                | \$1.31                                 | \$1.10      |

**NOTE 16—ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)**

The components of other comprehensive income related to unrealized gains and losses on available-for-sale securities for the periods ended *June 30, 2018* and *June 30, 2017*, were as follows:

| Pretax | Tax    | After-tax | Affected Line<br>Item |
|--------|--------|-----------|-----------------------|
|        | Effect |           |                       |

in Consolidated  
Statements of  
Income

|  |                  |                  |                   |
|--|------------------|------------------|-------------------|
| <b>Balance as of June 30, 2016</b>   | <b>\$3,621</b>   | <b>\$(1,232)</b> | <b>\$2,389</b>    |
| Unrealized holding loss on available-for-sale securities arising during the period | (2,737)          | 931              | (1,806 )          |
| Amounts reclassified from accumulated other comprehensive income                   | (209 )           | 71               | (138 )(a)(b)      |
| Net current period other comprehensive loss  | (2,946)          | 1,002            | (1,944 )          |
| <b>Balance as of June 30, 2017</b>   | <b>\$675</b>     | <b>\$(230 )</b>  | <b>\$445</b>      |
| Unrealized holding loss on available-for-sale securities arising during the period | (2,711)          | 638              | (2,073 )          |
| Amounts reclassified from accumulated other comprehensive income                   | (33 )            | 12               | (21 )(a)(b)       |
| Net current period other comprehensive loss  | (2,744)          | 650              | (2,094 )          |
| Reclassification of disproportional tax effect                                     | —                | 14               | 14                |
| <b>Balance as of June 30, 2018</b>   | <b>\$(2,069)</b> | <b>\$434</b>     | <b>\$(1,635 )</b> |

(a) Securities gain, net

(b) Income tax expense

## **ITEM 9—CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE**

None.

## **ITEM 9A—CONTROLS AND PROCEDURES**

### *Evaluation of Disclosure Controls and Procedures*

With the participation of the Corporation's management, including the Chief Executive Officer and Chief Financial Officer, an evaluation of the effectiveness of the Corporation's disclosure controls and procedures (as defined under Rule 13a-15(e) of the Securities Exchange Act of 1934) was performed, as of the end of the period covered by this Annual Report on Form 10-K. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the Corporation's disclosure controls and procedures were effective.

### *Management's Report on Internal Control Over Financial Reporting*

The management of Consumers Bancorp, Inc. is responsible for establishing and maintaining adequate internal control over financial reporting. Internal control over financial reporting is a process designed by, or under the supervision of, our principal executive and principal financial officers and effected by the board of directors, management and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with U.S. generally accepted accounting principles.

Management assessed the effectiveness of our internal control over financial reporting as of June 30, 2018 based on the criteria for effective internal control over financial reporting established in "Internal Control-Integrated Framework," issued by the Committee of Sponsoring Organizations (COSO) of the Treadway Commission in 2013. Based on that assessment, we have concluded that, as of June 30, 2018, our internal control over financial reporting is effective based on those criteria.

This annual report does not include an attestation report of the Corporation's registered public accounting firm regarding internal control over financial reporting. Management's report was not subject to attestation by the

Corporation's registered public accounting firm pursuant to rules of the SEC that permit the Corporation to provide only management's report in this annual report.

*Changes In Internal Control Over Financial Reporting*

There were no changes in the Corporation's internal controls over financial reporting that occurred during the fourth quarter of fiscal year 2018 that have materially affected, or are reasonably likely to materially affect, the Corporation's internal controls over financial reporting.

**ITEM 9B—OTHER INFORMATION**

None.

## **PART III**

### **ITEM 10—DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE**

The information required by this item is set forth in the Corporation's Proxy Statement dated September 12, 2018, under the captions "Election of Directors," "Directors and Executive Officers," "The Board of Directors and its Committees," "Section 16(a) Beneficial Ownership Reporting Compliance," and "Certain Transactions and Relationships and Legal Proceedings," and is incorporated herein by reference.

The Corporation's Code of Ethics Policy, which is applicable to all directors, officers and employees of the Corporation, and its Code of Ethics for Principal Financial Officers, which is applicable to the principal executive officer and the principal financial officer, are each available on the Investor Relations section under Corporate Governance of the Corporation's website ([www.consumersbank.com](http://www.consumersbank.com)). Copies of either of the Code of Ethics Policies are also available in print to shareholders upon request, addressed to the Corporate Secretary at Consumers Bancorp, Inc., 614 East Lincoln Way, Minerva, Ohio 44657. The Corporation intends to post amendments to or waivers from either of its Code of Ethics Policies on its website.

### **ITEM 11—EXECUTIVE COMPENSATION**

The information required by this item is set forth in the Corporation's Proxy Statement dated September 12, 2018 under the captions "Director Compensation," "Executive Compensation," "Defined Contribution Plan," "Outstanding Equity Awards at Fiscal Year-End," and "Salary Continuation Program," and is incorporated herein by reference.

### **ITEM 12—SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED SHAREHOLDER MATTERS**

#### **Equity Compensation Plan Information**

The following table sets forth information about common stock authorized for issuance, segregated between stock-based compensation plans approved by shareholders and stock-based compensation plans not approved by shareholders, as of June 30, 2018. Additional information regarding stock-based compensation plans is presented in Note 8 - Employee Benefit Plans to the Consolidated Financial Statements located elsewhere in this report.

| <u>Plan Category</u>               | Number of securities to be issued upon exercise of outstanding options, warrants, and rights | Weighted-average exercise price of outstanding options, warrants and rights | Number of securities remaining available for future issuance under equity compensation plans (excluding securities issuable under outstanding options, warrants and rights) |
|------------------------------------|--|---|---|
| Plans approved by shareholders     | —  | —   | 92,988  |
| Plans not approved by shareholders | —  | —   | —   |
| Total                              | —  | —   | 92,988  |

The remaining information required by this item is set forth in the Corporation’s Proxy Statement, dated September 12, 2018, under the caption “Security Ownership of Certain Beneficial Owners and Management,” and is incorporated herein by reference.

### **ITEM 13—CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE**

The information required by this item is set forth in the Corporation’s Proxy Statement, dated September 12, 2018, under the caption “Certain Transactions and Relationships and Legal Proceedings,” and is incorporated herein by reference.



#### **ITEM 14—PRINCIPAL ACCOUNTING FEES AND SERVICES**

The information required by this item is set forth in the Corporation's Proxy Statement, dated September 12, 2018, under the caption "Principal Accounting Fees and Services," and is incorporated herein by reference.

#### **PART IV**

#### **ITEM 15—EXHIBITS, FINANCIAL STATEMENT SCHEDULES**

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

(1) The report of independent registered accounting firm and the consolidated financial statements appearing in Item 8.

(2) Financial statement schedules are omitted as they are not required or are not applicable, or the required information is included in the financial statements.

(3) The exhibits required by this item are listed in the Exhibit Index of this Form 10-K.

(b) The exhibits to this Form 10-K begin on page 55 of this report.

(c) See Item 15(a)(2) above.

**EXHIBIT INDEX**

| <b>Exhibit Number</b> | <b>Description of Document</b>  |
|-----------------------|---|
| 3.1                   | <u>Amended and Restated Articles of Incorporation of the Corporation. Reference is made to Form 10-K (File No. 033-79130) of the Corporation filed September 22, 2010, which is incorporated herein by reference.</u>   |
| 3.2                   | <u>Amended and Restated Code of Regulations of the Corporation. Reference is made to Form 10-K (File No. 033-79130) of the Corporation filed September 15, 2008, which is incorporated herein by reference.</u>   |
| 4                     | <u>Form of Certificate of Common Shares. Reference is made to Form 10-KSB (File No. 033-79130) of the Corporation filed September 30, 2002, which is incorporated herein by reference.</u>  |
| 10.1                  | <u>Amendment No. 3, October 3, 2016 to the Salary Continuation agreement entered into with Mr. Lober on February 11, 2011. Reference is made to Form 10-Q of the Corporation filed February 14, 2017, which is incorporated herein by reference.</u>  |
| 10.2                  | <u>Salary Continuation agreement entered into with Mr. Dodds on November 4, 2016. Reference is made to Form 8-K of the Corporation filed November 9, 2016, which is incorporated herein by reference.</u>   |
| 10.3                  | <u>Lease Agreement entered into between Furey Holdings, LLC and Consumers National Bank on December 23, 2005. Reference is made to Form 10-Q (File No. 033-79130) of the Corporation filed February 14, 2006, which is incorporated herein by reference.</u>                                    |
| 10.6                  | <u>2011 Amendment and Restatement of Salary Continuation agreement entered into with Mr. Lober on February 11, 2011. Reference is made to Form 10-Q (File No. 033-79130) of the Corporation filed February 11, 2011, which is incorporated herein by reference.</u>                             |
| 10.8                  | <u>Consumers Bancorp 2010 Omnibus Incentive Plan Form of Restricted Stock Award Agreement. Reference is made to Form 8-K (File No. 033-79130) of the Corporation filed September 16, 2011, which is incorporated herein by reference.</u>   |
| 10.9                  | <u>Salary Continuation Agreement with Ms. Wood on December 30, 2015. Reference is made to Form 8-K of the Corporation filed on December 30, 2015, which is incorporated herein by reference.</u>  |
| 10.10                 | <u>First Amendment dated June 13, 2018, to Lease Agreement entered into between Furey Holdings, LLC and Consumers National Bank on December 23, 2005. Reference is made to Form 8-K (File No. 033-79130) of the Corporation filed June 15, 2018, which is incorporated herein by reference.</u> |
| 11                    | <u>Computation of Earnings per Share. Reference is made to this Annual Report on Form 10-K Note 15 to the Consolidated Financial Statements, which is incorporated herein by reference.</u>   |
| 21                    | <u>Subsidiaries of Consumers Bancorp, Inc. Filed with this Annual Report on Form 10-K.</u>  |

23 Consent of Crowe 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 and Treasurer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

32.1 Certification of Chief Executive Officer and Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

101 The following material from Consumers Bancorp, Inc.'s Form 10-K Report for the year ended June 30, 2018, formatted in XBRL (Extensible Business Reporting Language) includes: (1) Consolidated Balance Sheets, (2) Consolidated Statements of Income, (3) Consolidated Statements of Comprehensive Income, (4) Consolidated Statement of Changes in Shareholders' Equity, (5) Consolidated Statements of Cash Flows, and (6) the Notes to Consolidated Financial Statements.

55

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## 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.

### CONSUMERS BANCORP, INC.

Date: September 12, 2018 By: /s/ Ralph J. Lober, II  
**President and Chief Executive Officer**

(principal executive officer)

By: /s/ Renee K. Wood  
**Chief Financial Officer and Treasurer**

(principal financial officer)

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 indicated on September 12, 2018.

#### Signatures

/s/ Laurie L. McClellan

**Laurie L. McClellan**

**Chairman of the Board of Directors**

#### Signatures

/s/ Ralph J. Lober, II

**Ralph J. Lober, II**

**President, Chief Executive Officer and Director**

(principal executive officer)

/s/ Renee K. Wood

**Renee K. Wood**

**Chief Financial Officer and Treasurer**

(principal financial officer)

/s/ John P. Furey

**John P. Furey**

**Director**

/s/ Bradley Goris

**Bradley Goris**

/s/ James V. Hanna

**James V. Hanna**

**Director**

/s/ David W. Johnson  
**David W. Johnson**

**Director**

/s/ Thomas M. Kishman  
**Thomas M. Kishman**

**Director**

/s/ Frank L. Paden  
**Frank L. Paden**

**Director**

**Director**

/s/ Richard T. Kiko, Jr.  
**Richard T. Kiko, Jr.**

**Director**

/s/ Phillip R. Mueller  
**Phillip R. Mueller**

**Director**

/s/ Harry W. Schmuck, Jr.  
**Harry W. Schmuck, Jr.**

**Director**