EVANS BANCORP INC
Form 10-K
March 07, 2017

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

[X]ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended: December 31, 2016

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

For the transition period from __________ to __________

Commission file number: 001-35021

EVANS BANCORP, INC.

(Exact name of registrant as specified in its charter)

New York	16-1332767
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

One Grimsby Drive, Hamburg, New York	14075
(Address of principal executive offices)	(Zip Code)

(716) 926-2000
Registrant’s telephone number (including area code)

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

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock, Par Value $.50 per share	NYSE MKT LLC

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

None
(Title of Class)

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

Yes No X

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

Yes No X

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 X No

Indicate by checkmark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes X No

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

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

Large accelerated filer	Accelerated filer	X
Non-accelerated filer (do not check if a smaller reporting company)	Smaller reporting company	

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

Yes No X

On June 30, 2016, the aggregate market value of the registrant's common stock held by non-affiliates was approximately $101 million, based upon the closing sale price of a share of the registrant's common stock on the NYSE MKT LLC.

As of March 1, 2017, 4,749,846 shares of the registrant's common stock were outstanding.

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DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's Proxy Statement relating to the registrant's 2017 Annual Meeting of Shareholders, to be held on April 27, 2017, which will be subsequently filed with the Securities and Exchange Commission within 120 days after the end of the fiscal year to which this Report relates, are incorporated by reference into Part III of this Annual Report on Form 10-K where indicated.

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PART I

FORWARD LOOKING STATEMENTS

This Annual Report on Form 10-K may contain certain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (the "Securities Act"), and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), that involve substantial risks and uncertainties. When used in this report, or in the documents incorporated by reference herein, the words "will," "anticipate," "believe," "estimate," "expect," "intend," "may "plan," "seek," "look to," "goal," "target" and similar expressions identify such forward-looking statements. These forward-looking statements include statements regarding the business plans, prospects, growth and operating strategies of Evans Bancorp, Inc. (the "Company"), statements regarding the asset quality of the Company's loan and investment portfolios, and estimates of the Company's risks and future costs and benefits.

These forward-looking statements are based largely on the expectations of the Company's management and are subject to a number of risks and uncertainties, including but not limited to: general economic conditions, either nationally or in the Company's market areas, that are worse than expected; increased competition among depository or other financial institutions; inflation and changes in the interest rate environment that reduce the Company's margins or reduce the fair value of financial instruments; changes in laws or government regulations affecting financial institutions, including changes in regulatory fees and capital requirements; the Company's ability to enter new markets successfully and capitalize on growth opportunities; the Company's ability to successfully integrate acquired entities; loan losses in excess of the Company's allowance for loan losses; complications related to the Bank's core systems conversion; changes in accounting pronouncements and practices, as adopted by financial institution regulatory agencies, the Financial Accounting Standards Board ("FASB") and the Public Company Accounting Oversight Board; the impact of such changes in accounting pronouncements and practices being greater than anticipated; the ability to realize the benefit of deferred tax assets; changes in the financial performance and/or condition of the Company's borrowers; changes in consumer spending, borrowing and saving habits; changes in the Company's organization, compensation and benefit plans; and other factors discussed elsewhere in this Annual Report on Form 10-K including the risk factors described in Item 1A, as well as in the Company's periodic reports filed with the Securities and Exchange Commission (the "SEC"). Many of these factors are beyond the Company's control and are difficult to predict.

Because of these and other uncertainties, the Company's actual results, performance or achievements could differ materially from those contemplated, expressed or implied by the forward-looking statements contained herein. Forward-looking statements speak only as of the date they are made. The Company undertakes no obligation to publicly update or revise forward-looking information, whether as a result of new, updated information, future events or otherwise, except to the extent required by law.

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Item 1.BUSINESS

EVANS BANCORP, INC.

Evans Bancorp, Inc. (the "Company") is a New York business corporation which is registered as a financial holding company under the Bank Holding Company Act of 1956, as amended (the "BHCA"). The principal office of the Company is located at One Grimsby Drive, Hamburg, NY 14075 and its telephone number is (716) 926-2000. This facility is occupied by the Office of the President and Chief Executive Officer of the Company, as well as the Administrative and Loan Divisions of Evans Bank. The Company was incorporated on October 28, 1988, but the continuity of its banking business is traced to the organization of the Evans National Bank of Angola on January 20, 1920. Except as the context otherwise requires, the Company and its direct and indirect subsidiaries are collectively referred to in this report as the "Company." The Company's common stock is traded on the NYSE MKT under the symbol "EVBN."

At December 31, 2016, the Company had consolidated total assets of $1.1 billion, deposits of $940 million and stockholders' equity of $97 million.

The Company's primary business is the operation of its subsidiaries. It does not engage in any other substantial business activities. The Company has two direct wholly-owned subsidiaries: (1) Evans Bank, N.A. (the "Bank"), which provides a full range of banking services to consumer and commercial customers in Western New York; and (2) Evans National Financial Services, LLC ("ENFS"), which owns 100% of the membership interests in The Evans Agency, LLC ("TEA"), which sells various premium-based insurance policies on a commission basis. At December 31, 2016, the Bank represented 99% and ENFS represented 1% of the consolidated assets of the Company. Further discussion of our segments is included in Note 18 to the Company's Consolidated Financial Statements included under Item 8 of this Annual Report on Form 10-K.

Evans Bank

The Bank is a nationally chartered bank that has its headquarters at One Grimsby Drive, Hamburg, NY, and a total of 14 full-service banking offices in Erie County, Niagara County, and Chautauqua County, NY.

At December 31, 2016, the Bank had total assets of $1.1 billion, investment securities of $97 million, net loans of $929 million, deposits of $940 million and stockholders' equity of $90 million, compared with total assets of $933 million, investment securities of $99 million, net loans of $761 million, deposits of $803 million and stockholders' equity of $86 million at December 31, 2015. The Bank offers deposit products, which include checking and negotiable order of withdrawal ("NOW") accounts, savings accounts, and certificates of deposit, as its principal source of funding. The Bank's deposits are insured up to the maximum permitted by the Deposit Insurance Fund of the Federal Deposit Insurance Corporation ("FDIC"). The Bank offers a variety of loan products to its customers, including commercial and consumer loans and commercial and residential mortgage loans.

As is the case with banking institutions generally, the Bank's operations are significantly influenced by general economic conditions and by related monetary and fiscal policies of banking regulatory agencies, including the Federal Reserve Board ("FRB") and FDIC. The Bank is also subject to the supervision, regulation and examination of the Office of the Comptroller of the Currency of the United States of America (the "OCC").

The Evans Agency, LLC

TEA, a property and casualty insurance agency, is a wholly-owned subsidiary of ENFS. TEA is headquartered in Hamburg, NY, with offices located throughout Western New York. TEA is a full-service insurance agency offering personal, commercial and financial services products. For the year ended December 31, 2016, TEA had total revenue of $6 million.

TEA's primary market area is Erie, Chautauqua, Cattaraugus and Niagara counties. Most lines of personal insurance are provided, including automobile, homeowners, boat, recreational vehicle, landlord, and umbrella coverage. Commercial insurance products are also provided, consisting of property, liability, automobile, inland marine, workers compensation, bonds, crop and umbrella insurance. TEA also provides the following financial services products: life and disability insurance, Medicare supplements, long term care, annuities, mutual funds, retirement programs and New York State Disability.

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Other Subsidiaries

In addition to the Bank and TEA, the Company has the following direct and indirect wholly-owned subsidiaries:

Evans National Holding Corp. (“ENHC”). ENHC, a wholly-owned subsidiary of the Bank, operates as a real estate investment trust that holds commercial real estate loans and residential mortgages, providing additional flexibility and planning opportunities for the business of the Bank.

Evans National Financial Services, LLC (“ENFS”). ENFS is a wholly-owned subsidiary of the Company. ENFS's primary business is to own the business and assets of the Company’s non-banking financial services subsidiaries.

Frontier Claims Services, Inc. (“FCS”). FCS is a wholly-owned subsidiary of TEA and provides claims adjusting services to various insurance companies.

Evans National Leasing, Inc. (“ENL”). ENL, a wholly-owned subsidiary of the Bank, provided direct financing leasing of commercial small-ticket general business equipment to companies located throughout the contiguous 48 United States. The Company exited the leasing business in 2009 and currently has only minimal activity, primarily collecting recoveries of previously charged-off leases.

The Company also has two special purpose entities: Evans Capital Trust I, a statutory trust formed in September 2004 under the Delaware Statutory Trust Act, solely for the purpose of issuing and selling certain securities representing undivided beneficial interests in the assets of the trust, investing the proceeds thereof in certain debentures of the Company and engaging in those activities necessary, advisable or incidental thereto; and ENB Employers Insurance Trust, a Delaware trust company formed in February 2003 for the sole purpose of holding life insurance policies under the Bank’s bank-owned life insurance (“BOLI”) program.

The Company operates in two operating segments – banking activities and insurance agency activities. See Note 18 to the Company’s Consolidated Financial Statements included under Item 8 of this Annual Report on Form 10-K for more information on the Company’s operating segments.

MARKET AREA

The Company's primary market area is Erie County, Niagara County, northern Chautauqua County and northwestern Cattaraugus County, NY. This primary market area is the area where the Bank principally receives deposits and makes loans and TEA sells insurance.

MARKET RISK

For information about, and a discussion of, the Company's "Market Risk," see Part II, Item 7 "Management's Discussion and Analysis of Financial Condition and Results of Operations - Market Risk" of this Annual Report on Form 10-K.

COMPETITION

All phases of the Company's business are highly competitive. The Company competes actively with local, regional and national financial institutions, as well as with bank branches and insurance agency offices in the Company's primary market area of Erie County, Niagara County, northern Chautauqua County, and northwestern Cattaraugus County, NY. These Western New York counties have a high density of financial institutions, many of which are significantly larger and have greater financial resources than the Company. The Company faces competition for loans and deposits from other commercial banks, savings banks, internet banks, savings and loan associations, mortgage banking companies, credit unions, and other financial services companies. The Company faces additional competition from non-depository competitors such as the mutual fund industry, securities and brokerage firms, and insurance companies and brokerages. In the personal insurance area, the majority of TEA's competition comes from direct writers, as well as some small local agencies located in the same towns and villages in which TEA has offices. In the commercial business segment, the majority of the competition comes from larger agencies located in and around Buffalo, NY. By offering the large number of carriers which it has available to its customers, TEA has attempted to remain competitive in all aspects of its business.

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As an approximate indication of the Company’s competitive position, the Bank had the sixth most deposits in the Buffalo, NY metropolitan statistical area according to the FDIC’s annual deposit market share report as of June 30, 2016 with 2% of the total market’s deposits of $43 billion. By comparison, the market leaders, M&T Bank and Key Bank, had 82% of the county’s deposits combined. The Company attempts to be generally competitive with all financial institutions in its service area with respect to interest rates paid on time and savings deposits, service charges on deposit accounts, and interest rates charged on loans.

SUPERVISION AND REGULATION

Bank holding companies and banks are extensively regulated under both federal and state laws and regulations that are intended to protect depositors and customers. Additionally, because the Company is a public company with shares traded on the NYSE MKT, it is subject to regulation by the Securities and Exchange Commission, as well as the listing standards required by NYSE MKT. To the extent that the following summary describes statutory and regulatory provisions, it is qualified in its entirety by reference to the particular statutory and regulatory provisions. Any change in the applicable law or regulation, or a change in the way such laws or regulations are interpreted by regulatory agencies or courts, may have a material adverse effect on the Company's business, financial condition and results of operations.

Bank Holding Company Regulation (BHCA)

As a financial holding company registered under the BHCA, the Company and its non-banking subsidiaries are subject to regulation and supervision under the BHCA by the FRB. The FRB requires periodic reports from the Company, and is authorized by the BHCA to make regular examinations of the Company and its subsidiaries.

The Company is required to obtain the prior approval of the FRB before merging with or acquiring all or substantially all of the assets of, or direct or indirect ownership or control of more than 5% of the voting shares of, a bank or bank holding company. The FRB will not approve any acquisition, merger or consolidation that would have a substantial anti-competitive result, unless the anti-competitive effects of the proposed transaction are outweighed by a greater public interest in meeting the needs and convenience of the public.

Subject to various exceptions, the BHCA and the Change in Bank Control Act of 1978, together with related regulations, require FRB approval before any person or company acquires “control” of a bank holding company. Control is conclusively presumed to exist if an individual or company acquires 25% or more of any class of voting securities of the bank holding company. Rebuttable control is presumed to exist if a person or company acquires 10% or more, but less than 25%, of any class of the bank holding company’s voting securities.

The FRB also considers managerial, capital and other financial factors in acting on acquisition or merger applications. A bank holding company may not engage in, or acquire direct or indirect control of more than 5% of the voting shares of any company engaged in any non-banking activity, unless such activity has been determined by the FRB to be closely related to banking or managing banks. The FRB has identified by regulation various non-banking activities in which a bank holding company may engage with notice to, or prior approval by, the FRB.

The FRB has enforcement powers over financial holding companies and their subsidiaries, among other things, to enjoin activities that represent unsafe or unsound practices or constitute violations of law, rule, regulation, administrative orders, or written agreements with a federal bank regulator. These powers may be exercised through the issuance of cease and desist orders, civil monetary penalties or other actions.

Under Regulation Y, a bank holding company must serve as a source of financial and managerial strength for its subsidiary banks and must not conduct its operations in an unsafe or unsound manner. Additionally, Regulation Y requires a bank holding company to give the FRB prior notice of any redemption or repurchase of its own equity securities, if the consideration to be paid, together with the consideration paid for any repurchases in the preceding year, is equal to 10% or more of the company's consolidated net worth. The FRB may oppose the transaction if it believes that the transaction would constitute an unsafe or unsound practice or would violate any law or regulation. There is an exception for bank holding companies that are well-managed, well capitalized, and not subject to any unresolved supervisory issues. To date, the Company has qualified for this exception. As another example, a bank holding company may not impair its subsidiary bank's soundness by causing it to make funds available to non-banking subsidiaries or their customers if the FRB believed it would not be prudent to do so.

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Bank holding companies and their subsidiary banks are also subject to the provisions of the Community Reinvestment Act ("CRA"). Under the terms of the CRA, the FRB (or other appropriate bank regulatory agency, in the case of the Bank, the OCC) is required, in connection with its examination of a bank, to assess such bank's record in meeting the credit needs of the communities served by that bank, including low and moderate-income neighborhoods. Furthermore, such assessment is taken into account in evaluating any application made by a bank holding company or a bank for, among other things, approval of a branch or other deposit facility, office relocation, a merger or an acquisition of bank shares.

Supervision and Regulation of Bank Subsidiaries

The Bank is a nationally chartered banking corporation subject to supervision, examination and regulation by the FRB, the FDIC and the OCC. These regulators have the power to enjoin "unsafe or unsound practices," require affirmative action to correct any conditions resulting from any violation or practice, issue an administrative order that can be judicially enforced, direct an increase in capital, restrict the growth of a bank, assess civil monetary penalties, and remove a bank's officers and directors.

The operations of the Bank are subject to numerous statutes and regulations. Such statutes and regulations relate to required reserves against deposits, investments, loans, mergers and consolidations, issuance of securities, payment of dividends, establishment of branches, and other aspects of the Bank's operations. Various consumer laws and regulations also affect the operations of the Bank, including state usury laws, laws relating to fiduciaries, consumer credit and equal credit, fair credit reporting, and privacy of non-public financial information.

The Bank is subject to Sections 23A and 23B of the Federal Reserve Act and Regulation W thereunder, which govern certain transactions, such as loans, extensions of credit, investments and purchases of assets between member banks and their affiliates, including their parent holding companies. These restrictions limit the transfer from its subsidiaries, including the Bank, of funds to the Company in the form of loans, extensions of credit, investments or purchases of assets (collectively, "Transfers"), and they require that the Bank's transactions with the Company be on terms no less favorable to the Bank than comparable transactions between the Bank and unrelated third parties. Transfers by the Bank to any affiliate (including the Company) are limited in amount to 10% of the Bank's capital and surplus, and transfers to all affiliates are limited in the aggregate to 20% of the Bank's capital and surplus. Furthermore, such loans and extensions of credit are also subject to various collateral requirements. These regulations and restrictions may limit the Company's ability to obtain funds from the Bank for its cash needs, including funds for acquisitions, and the payment of dividends, interest and operating expenses.

The Bank is prohibited from engaging in certain tying arrangements in connection with any extension of credit, lease or sale of property or furnishing of services. For example, the Bank may not generally require a customer to obtain other services from the Bank or the Company, and may not require the customer to promise not to obtain other services from a competitor as a condition to an extension of credit. The Bank is also subject to certain restrictions imposed by the Federal Reserve Act on extensions of credit to executive officers, directors, principal stockholders or any related interest of such persons. Extensions of credit: (i) must be made on substantially the same terms (including interest rates and collateral) as those prevailing at the time for, and following credit underwriting procedures that are not less stringent than those applicable to, comparable transactions with persons not covered above and who are not employees, and (ii) must not involve more than the normal risk of repayment or present other unfavorable features. The Bank is also subject to certain lending limits and restrictions on overdrafts to such persons. A violation of these restrictions may result in the assessment of substantial civil monetary penalties on the Bank or any officer, director, employee, agent or other person participating in the conduct of the affairs of the Bank or the imposition of a cease and desist order.

As insurer, the FDIC imposes deposit insurance premiums and is authorized to conduct examinations of and to require reporting by, insured institutions. It may also prohibit an insured institution from engaging in any activity the FDIC determines by regulation or order to pose a serious threat to the FDIC. The FDIC also has the authority to initiate enforcement actions against insured institutions. The FDIC may terminate the deposit insurance of any insured depository institution, including the Bank, if it determines after a hearing that the institution has engaged or is engaging in unsafe or unsound practices, is in an unsafe or unsound condition to continue operations, or has violated any applicable law, regulation, order or any condition imposed by an agreement with the FDIC.

The FDIC has adopted a risk-based premium system that provides for quarterly assessments based on an insured institution’s ranking in one of four risk categories based on their examination ratings and capital ratios. In addition, all FDIC-insured institutions are required to pay assessments to the FDIC to fund interest payments on bonds issued by the Financing

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Corporation ("FICO"), a mixed-ownership Federal government corporation established to recapitalize the Federal Savings and Loan Insurance Corporation. The current annualized assessment rate is 0.56 basis points, or approximately 0.14 basis points per quarter. These assessments will continue until the Financing Corporation bonds mature in 2019. Pursuant to the Dodd-Frank Act, the deposit insurance assessment base was redefined in 2011 to reflect consolidated total assets less average tangible equity. The result is that larger financial institutions, which have more assets leveraged with non-deposit wholesale funds, generally have paid a greater percentage of the aggregate insurance assessment and smaller banks, including the Bank, have paid less.

Regulations promulgated by the FDIC pursuant to the Federal Deposit Insurance Corporation Improvement Act of 1991 place limitations on the ability of certain insured depository institutions to accept, renew or rollover deposits by offering rates of interest which are significantly higher than the prevailing rates of interest on deposits offered by other depository institutions having the same type of charter in such depository institutions' normal market area. Under these regulations, well-capitalized institutions may accept, renew or rollover such deposits without restriction, while adequately capitalized institutions may accept, renew or rollover such deposits with a waiver from the FDIC (subject to certain restrictions on payment of rates). Undercapitalized institutions may not accept, renew or rollover such deposits.

Under the Financial Institutions Reform, Recovery and Enforcement Act of 1989, a depository institution insured by the FDIC can be held liable for any loss incurred by, or reasonably expected to be incurred by, the FDIC in connection with: (i) the default of a commonly controlled FDIC-insured depository institution, or (ii) any assistance provided by the FDIC to a commonly controlled FDIC-insured institution in danger of default. "Default" is defined generally as the appointment of a conservator or receiver, and "in danger of default" is defined generally as the existence of certain conditions indicating that, in the opinion of the appropriate banking agency, a "default" is likely to occur in the absence of regulatory assistance.

In addition to the foregoing, federal regulators have adopted regulations and examination procedures promoting the safety and soundness of institutions by specifically addressing, among other things: (i) internal controls, information systems and internal audit systems; (ii) loan documentation; (iii) credit underwriting; (iv) interest rate exposure; (v) asset growth; (vi) ratio of classified assets to capital; (vii) minimum earnings; and (viii) compensation and benefits standards for management officials. FRB regulations, for example, generally require a bank holding company to give the FRB prior notice of any redemption or repurchase of the bank holding company's equity securities, if the consideration to be paid, together with the consideration paid for any repurchases or redemptions in the preceding year, is equal to 10% or more of the company's consolidated net worth. The Federal Reserve Board has broad authority to prohibit activities of bank holding companies and their non-banking subsidiaries which represent unsafe and unsound banking practices or which constitute violations of laws or regulations, and can assess civil money penalties for certain activities conducted on a knowing and reckless basis, if those activities caused a substantial loss to a depository institution.

Dividends paid by the Bank have been the Company's primary source of operating funds and are expected to be for the foreseeable future. Capital adequacy requirements serve to limit the amount of dividends that may be paid by the Bank. Under OCC regulations, the Bank may not pay a dividend, without prior OCC approval, if the total amount of all dividends declared during the calendar year, including the proposed dividend, exceed the sum of its retained net income to date during the calendar year and its retained net income over the preceding two years. As of December 31, 2016, approximately $12 million was available for the payment of dividends without prior OCC approval. The Bank's ability to pay dividends is also subject to the Bank being in compliance with regulatory capital requirements. As indicated below, at December 31, 2016, the Bank was in compliance with these requirements.

Because the Company is a legal entity separate and distinct from the Bank, the Company's right to participate in the distribution of assets of the Bank in the event of the Bank's liquidation or reorganization would be subject to the prior claims of the Bank's creditors. In the event of a liquidation or other resolution of an insured depository institution, the claims of depositors and other general or subordinated creditors are entitled to a priority of payment over the claims of unsecured, non-deposit creditors, including a parent bank holding company (such as the Company) or any shareholder or creditor thereof.

The FRB, the OCC and other federal banking agencies have broad enforcement powers, including the power to terminate deposit insurance, to impose substantial fines and other civil and criminal penalties, and to appoint a conservator or receiver for the assets of a regulated entity. Failure to comply with applicable laws, regulations and supervisory agreements could subject the Company or its subsidiaries, as well as officers, directors and other institution-affiliated parties of these organizations, to administrative sanctions and potential civil monetary penalties.

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Capital Adequacy

The Company and its subsidiary bank are required to comply with applicable capital adequacy standards established by the federal banking agencies. The risk-based capital standards that were applicable to the Company and its subsidiary bank through December 31, 2014 were based on the 1988 Capital Accord, known as Basel I, of the Basel Committee on Banking Supervision (the "Basel Committee"). However, in July 2013, the Federal Reserve Board, the OCC, and the FDIC approved final rules (the "New Capital Rules") establishing a new comprehensive capital framework for U.S. banking organizations. These rules went into effect as to the Company and its subsidiary bank on January 1, 2015, subject to phase-in periods for certain components and other provisions.

Basel III and the New Capital Rules. The New Capital Rules generally implement the Basel Committee's December 2010 final capital framework referred to as "Basel III" for strengthening international capital standards. The New Capital Rules substantially revise the risk-based capital requirements applicable to bank holding companies and their depository institution subsidiaries, including Evans Bancorp, Inc., and Evans Bank N.A., as compared to the U.S. general risk-based capital rules that were applicable to the Company through December 31, 2014. The New Capital Rules revise the definitions and the components of regulatory capital, as well as address other issues affecting the numerator in banking institutions' regulatory capital ratios. The New Capital Rules also address asset risk weights and other matters affecting the denominator in banking institutions' regulatory capital ratios.

Among other matters, the New Capital Rules: (i) introduce a new capital measure called "Common Equity Tier 1" ("CET1") and related regulatory capital ratio of CET1 to risk-weighted assets; (ii) specify that Tier 1 capital consists of CET1 and "Additional Tier 1 capital" instruments meeting certain revised requirements; (iii) mandate that most deductions/adjustments to regulatory capital measures be made to CET1 and not to the other components of capital; and (iv) expand the scope of the deductions from and adjustments to capital as compared to the previous regulations.

Pursuant to the New Capital Rules, the minimum capital ratios as of January 1, 2015 (subject to the phase-in of additional requirements as described below) were as follows:

4.5% CET1 to risk-weighted assets;

6.0% Tier 1 capital (that is, CET1 plus Additional Tier 1 capital) to risk-weighted assets;

8.0% Total capital (that is, Tier 1 capital plus Tier 2 capital) to risk-weighted assets; and

4.0% Tier 1 capital to average consolidated assets as reported on the consolidated financial statements (known as the "leverage ratio").

The New Capital Rules also introduce a new "capital conservation buffer," composed entirely of CET1, on top of the minimum risk-weighted asset ratios described above, and is designed to absorb losses during periods of economic stress. Banking institutions with a ratio of CET1 to risk-weighted assets above the minimum but below the capital conservation buffer will face constraints on dividends, equity and other capital instrument repurchases and compensation based on the amount of the shortfall. The implementation of the capital conservation buffer began on January 1, 2016 at 0.625% and is scheduled to increase by 0.625% on each subsequent January 1 through January 1, 2019. Thus, when fully phased-in on January 1, 2019, the capital standards applicable to the Company will include an additional capital conservation buffer of 2.5% of CET1, effectively resulting in minimum ratios inclusive of the capital conservation buffer of (i) CET1 to risk-weighted assets of at least 7%, (ii) Tier 1 capital to risk-weighted assets of at least 8.5%; (iii) Total capital to risk-weighted assets of at least 10.5% and (iv) a minimum leverage ratio of 4%, calculated as the ratio of Tier 1 capital to average assets.

The New Capital Rules provide for a number of deductions from and adjustments to CET1. These include, for example, the requirement that mortgage servicing rights, deferred tax assets arising from temporary differences that could not be realized through net operating loss carrybacks and significant investments in non-consolidated financial entities be deducted from CET1 to the extent that any one such category exceeds 10% of CET1 or all such items, in the aggregate, exceed 15% of CET1.

In addition, the New Capital Rules include certain exemptions to address concerns about the regulatory burden on community banks. For example, banking organizations with less than $15 billion in consolidated assets as of December 31, 2009 are permitted to include in Tier 1 capital trust preferred securities and cumulative perpetual preferred stock issued and included in Tier 1 capital prior to May 19, 2010 on a permanent basis, without any phase out (subject to a limit of 25% of Tier 1 capital). Also, community banks were able to elect on a one time basis in their March 31, 2015 quarterly filings to opt-out of

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the onerous requirement to include most accumulated other comprehensive income ("AOCI") components in the calculation of common equity Tier 1 capital and, in effect, retain the AOCI treatment under the current capital rules. Under the New Capital Rules, the Company made a one-time, permanent election to continue to exclude AOCI from capital.

The Federal Deposit Insurance Act (the "FDIA") establishes a system of regulatory remedies to resolve the problems of undercapitalized institutions, referred to as the prompt corrective action. The federal banking regulators have established five capital categories ("well-capitalized," "adequately capitalized," "undercapitalized," "significantly undercapitalized" and "critically undercapitalized") and must take certain mandatory supervisory actions, and are authorized to take other discretionary actions, with respect to institutions which are undercapitalized, significantly undercapitalized or critically undercapitalized. The severity of these mandatory and discretionary supervisory actions depends upon the capital category in which the institution is placed. Generally, subject to a narrow exception, the FDIA requires the banking regulator to appoint a receiver or conservator for an institution that is critically undercapitalized. The FDIC has specified by regulation the relevant capital levels for each category, which are printed below. The Federal Reserve Board and the OCC have specified the same or similar levels for each category.

"Well-Capitalized" CET1 ratio of 6.5% Leverage Ratio of 5%, Tier 1 Capital ratio of 8%, Total Capital ratio of 10%, and Not subject to a written agreement, order, capital directive or regulatory remedy directive requiring a specific capital level.	"Adequately Capitalized" CET1 ratio of 4.5% Leverage Ratio of 4%, Tier 1 Capital ratio of 6%, and Total Capital ratio of 8%.
"Undercapitalized" CET1 Ratio of less than 4.5% Leverage Ratio less than 4%, Tier 1 Capital ratio less than 6%, or Total Capital ratio less than 8%.	"Significantly Undercapitalized" CET1 Ratio of less than 3% Leverage Ratio less than 3%, Tier 1 Capital ratio less than 4%, or Total Capital ratio less than 6%.
"Critically undercapitalized"	

Tangible equity to total assets less than 2%.

For purposes of these regulations, the term "tangible equity" includes core capital elements counted as Tier 1 Capital for purposes of the risk-based capital standards plus the amount of outstanding cumulative perpetual preferred stock (including related surplus), minus all intangible assets with certain exceptions.

An institution that is classified as well-capitalized based on its capital levels may be classified as adequately capitalized, and an institution that is adequately capitalized or undercapitalized based upon its capital levels may be treated as though it were undercapitalized or significantly undercapitalized, respectively, if the appropriate federal banking agency, after notice and opportunity for hearing, determines that an unsafe or unsound condition or an unsafe or unsound practice warrants such treatment.

An institution that is categorized as undercapitalized, significantly undercapitalized or critically undercapitalized is required to submit an acceptable capital restoration plan to its appropriate federal banking regulator. Under the FDIA, in order for the capital restoration plan to be accepted by the appropriate federal banking agency, a BHC must guarantee that a subsidiary depository institution will comply with its capital restoration plan, subject to certain limitations. The BHC must also provide appropriate assurances of performance. The obligation of a controlling BHC under the FDIA to fund a capital restoration plan is limited to the lesser of 5.0% of an undercapitalized subsidiary's assets or the amount required to meet regulatory capital requirements. An undercapitalized institution is also generally prohibited from increasing its average total assets, making acquisitions, establishing any branches or engaging in any new line of business, except in accordance with an accepted capital restoration plan or with the approval of the FDIC. Institutions that are significantly undercapitalized or

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undercapitalized and either fail to submit an acceptable capital restoration plan or fail to implement an approved capital restoration plan may be subject to a number of requirements and restrictions, including orders to sell sufficient voting stock to become adequately capitalized, requirements to reduce total assets and cessation of receipt of deposits from correspondent banks. Critically undercapitalized depository institutions failing to submit or implement an acceptable capital restoration plan are subject to appointment of a receiver or conservator.

The Company's regulatory capital ratios under risk-based capital rules in effect through December 31, 2016 are presented in Note 20 of Notes to Financial Statements filed herewith in Part II, Item 8, "Financial Statements and Supplementary Data".

Dodd-Frank Wall Street Reform and Consumer Protection Act

The Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act"), enacted in 2010, is widely regarded as the most sweeping change to financial regulation since the Great Depression. The law was intended to promote robust supervision and regulation of financial firms; establish comprehensive supervision of financial markets; protect consumers and investors from financial abuse; provide the government with the tools to manage a financial crisis; and raise international regulatory standards and improve international cooperation. Some of the most significant aspects of The Dodd-Frank Act include:

I. The creation of a new oversight regulator, the Financial Stability Oversight Council. The council of regulators monitors the financial system for systemic risk and will determine which entities pose significant systemic risk and should be subject to greater federal regulation and oversight.

II. The Collins Amendment, which requires the federal banking agencies to establish minimum leverage capital and risk-based capital requirements for insured depository institutions, depository institution holding companies and non-bank financial companies supervised by the FRB (also known as systemically significant financial institutions). The Collins Amendment provides that certain hybrid financial instruments, such as trust preferred securities, issued on or after May 19, 2010, will be excluded from Tier 1 capital. For certain large depository institution holding companies (greater than $15 billion in assets at December 31, 2009), hybrid financial instruments issued before May 19, 2010 must be phased out of Tier 1 capital over a three-year period beginning January 1, 2013. The Company was well below this threshold at December 31, 2009. At December 31, 2016, the Company had $11.3 million in trust preferred securities included in Tier 1 capital.

III. The Durbin Amendment, which provided that interchange fees that a card issuer or payment network receives or charges for debit transactions will now be regulated by the FRB and must be "reasonable and proportional" to the cost incurred by the card issuer in authorizing, clearing and settling the transaction. The pricing provisions of the Durbin Amendment apply to card issuing financial institutions with more than $10 billion in assets. The Durbin Amendment also prohibits all issuers and networks from restricting the number of networks over which electronic debit transactions may be processed to less than two unaffiliated networks, and prohibits issuers and networks from inhibiting a merchant's ability to direct the routing of the electronic debit transaction over any network that the issuer has enabled to process them. Although the Bank is exempt from the pricing provisions of the Durbin Amendment, it has been indirectly impacted as it competes with other institutions who are directly impacted by the Durbin Amendment.

IV. A number of deposit insurance reforms, which have generally benefited the Bank. First, the Dodd-Frank Act redefined the deposit insurance assessment base to reflect consolidated total assets less average tangible equity. The result is that larger financial institutions, which have more assets leveraged with non-deposit wholesale funds, have paid a greater percentage of the aggregate insurance assessment, while smaller banks (such as the Bank) have paid less than they would have under the prior rules. The Dodd-Frank Act also increased the minimum reserve ratio of the Deposit Insurance Fund from 1.15% to 1.35%, but exempted institutions with assets less than $10 billion from funding the cost of the increase. The title also permanently increased deposit insurance coverage to $250,000 per account (subject to certain limitations).

V. A permanent exemption from the provisions of Section 404(b) of the Sarbanes-Oxley Act (“SOX”), which requires that public companies receive an opinion from their external auditors as to the effectiveness of their internal control over financial reporting, for companies with a public market capitalization under $75 million. As an accelerated filer, the Company does not qualify for this exemption.

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VI. Establishment of the Consumer Financial Protection Bureau (the "CFPB"), an independent agency with the authority to prohibit practices that it finds to be unfair, deceptive, or abusive, in addition to requiring certain disclosures.

VII. The imposition of new regulations on mortgage loan originators, including the imposition of new disclosure requirements and appraisal reforms, such as: the creation of a mortgage originator duty of care; the establishment of certain underwriting requirements designed to ensure that at the time of origination the consumer has a reasonable ability to repay the loan; the creation of document requirements intended to eliminate "no document" and "low document" loans; the prohibition of steering incentives for mortgage originators; a prohibition on yield spread premiums and prepayment penalties in some cases; and a provision that allows borrowers to assert as a foreclosure defense a contention that the lender violated the anti-steering restrictions or the reasonable repayment requirements.

VIII. In December 2013, five federal agencies (including the FRB and the OCC) adopted a final regulation implementing the "Volcker Rule" provision of the Dodd-Frank Act. The Volcker Rule generally prohibits insured banks and their affiliates from proprietary trading or from acquiring or retaining any equity, partnership or other ownership interest in, sponsoring or having certain other relationships with a hedge fund or a private equity fund, subject to certain exceptions. The Volcker Rule did not have an impact on the operations of the Company or the Bank, as they do not engage in the activities prohibited by the Volcker Rule.

Regulation of Insurance Agency Subsidiary

TEA is regulated by the New York State Insurance Department. As of the date of this report, TEA meets and maintains all licensing and continuing education requirements required by the State of New York.

Monetary Policy and Economic Control

The commercial banking business is affected not only by general economic conditions, but also by the monetary policies of the FRB. Changes in the discount rate on member bank borrowing, availability of borrowing at the "discount window," open market operations, the imposition of changes in reserve requirements against member banks' deposits and assets of foreign branches and the imposition of and changes in reserve requirements against certain borrowings by banks and their affiliates are some of the instruments of monetary policy available to the FRB. These monetary policies are used in varying combinations to influence overall growth and distributions of bank loans, investments and deposits, and this use may affect interest rates charged on loans or paid on deposits. The monetary policies of the FRB have had a significant effect on the operating results of commercial banks and are expected to continue to do so in the future. The monetary policies of these agencies are influenced by various factors, including inflation, unemployment, and short-term and long-term changes in the international trade balance and in the fiscal policies of the United States Government. Future monetary policies and the effect of such policies on the future business and earnings of the Company cannot be predicted.

Consumer Laws and Regulations

In addition to the laws and regulations discussed herein, the Bank is also subject to certain consumer laws and regulations that are designed to protect consumers in transactions with banks. These laws and regulations include, but are not limited to, the USA PATRIOT Act of 2001, the Bank Secrecy Act, the Truth in Lending Act, the Truth in Savings Act, the Electronic Funds Transfer Act, the Expedited Funds Availability Act, the Equal Credit Opportunity Act, the Fair Housing Act, the Home Mortgage Disclosure Act, the Real Estate Settlement Procedures Act, Federal Financial Privacy Laws, Interagency Guidelines Establishing Information Security Standards, the Right to Financial Privacy Act, and the Fair and Accurate Credit Transactions Reporting Act. These laws and regulations regulate the manner in which financial institutions must deal with customers when taking deposits or making loans to such customers.

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EMPLOYEES

As of December 31, 2016, the Company had no direct employees. As of December 31, of the years indicated, the following table summarizes the employment rosters of the Company’s subsidiaries using full-time equivalent employees:

	2016	2015	2014	2013	2012
Bank	206	206	201	196	183
ENL	-	-	-	-	2
TEA	44	48	46	41	49
FCS	4	4	4	4	4
	254	258	251	241	238

Management believes that the Company’s subsidiaries have good relationships with their employees.

AVAILABLE INFORMATION

The Company's Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and amendments to those reports filed or furnished by the Company pursuant to Section 13(a) or 15(d) of the Exchange Act are available without charge on the Company's website, www.evansbancorp.com - SEC filings section, as soon as reasonably practicable after they are electronically filed with or furnished to the SEC. The Company is providing the address to its Internet site solely for the information of investors. The Company does not intend its Internet address to be an active link or to otherwise incorporate the contents of the website into this Annual Report on Form 10-K or into any other report filed with or furnished to the SEC.

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Item 1A.RISK FACTORS

The following factors identified by the Company's management represent significant potential risks that the Company faces in its operations.

The Company’s Business May Be Adversely Affected by Conditions in the Financial Markets and Economic Conditions Generally

The Company’s financial performance generally, and in particular the ability of borrowers to pay interest on and repay principal of outstanding loans and the value of collateral securing those loans, is highly dependent upon the business environment in the markets where the Company operates, in Western New York and in the United States as a whole. A favorable business environment is generally characterized by, among other factors, economic growth, efficient capital markets, low inflation, high business and investor confidence, and strong business earnings. Unfavorable or uncertain economic and market conditions can be caused by: declines in economic growth, declines in housing and real estate valuations, business activity or investor or business confidence; limitations on the availability or increases in the cost of credit and capital; increases in inflation or interest rates; natural disasters; or a combination of these or other factors.

Economic conditions in the United States remained positive in 2016, which included national and local unemployment rates of 4.7% and 5.3%, respectively, as of December 31, 2016. Although conditions in Western New York and the United States are currently good, a slowdown of the economy could occur in 2017. The last recession ended in 2009 and has been followed by 90 months of economic expansion. In the post-World War II era, the average period of economic expansion has been 57 months. This could indicate that we are in a longer than normal period of economic expansion and that there is increased risk of recession.   Even though the Company is a community institution servicing a local market, in a global economy, any deteriorating conditions in other parts of the world could affect the United States economically. Such conditions could materially adversely affect the credit quality of the Company’s loans, and therefore, the Company’s results of operations and financial condition.

Commercial Real Estate and Commercial Business Loans Expose the Company to Increased Credit Risks

At December 31, 2016, the Company's portfolio of commercial real estate loans totaled $556 million, or 59% of total loans outstanding, and the Company's portfolio of commercial and industrial (“C&I”) loans totaled $197 million, or 21% of total loans outstanding. The Company plans to continue to emphasize the origination of commercial loans as they generally earn a higher rate of interest than other loan products offered by the Bank. However, commercial loans generally expose a lender to greater risk of non-payment and loss than one-to four-family residential mortgage loans because repayment of commercial real estate and C&I loans often depends on the successful operations and the income stream of the borrowers. Commercial mortgages are collateralized by real property while C&I loans are typically secured by business assets such as equipment and accounts receivable. Commercial loans typically involve larger loan balances to single borrowers or groups of related borrowers compared to one-to four-family residential mortgage loans. Also, many of the Company's commercial borrowers have more than one commercial real estate or C&I loan outstanding with the Company. Consequently, an adverse development with respect to one loan or one credit relationship can expose the Company to a significantly greater risk of loss compared to an adverse development with respect to a one-to four-family residential mortgage loan. Commercial real estate loans in non-accrual status at December 31, 2016 were $6.1 million, compared with $7.8 million at December 31, 2015. C&I loans in non-accrual status at December 31, 2016 were $3.1 million, compared with $5.3 million at December 31, 2015. Increases in the delinquency levels of commercial real estate and C&I loans could result in an increase in non-performing loans and the provision for loan losses, which could have a material adverse effect on the Company's results of operations and financial condition.

Continuing Concentration of Loans in the Company's Primary Market Area May Increase the Company's Risk

Unlike larger banks that are more geographically diversified, the Company provides banking and financial services to customers located primarily in western New York State ("WNY"). Therefore, the Company's success depends primarily on the general economic conditions in WNY. The Company's business lending and marketing strategies focus on loans to small and medium-sized businesses in this geographic region. Moreover, the Company's assets are heavily concentrated in mortgages on properties located in WNY. Accordingly, the Company's business and operations are vulnerable to downturns in the economy of WNY. The concentration of the Company's loans in this geographic region subjects the Company to the risk that a downturn in the economy or recession in this region could result in a decrease in loan originations and increases in delinquencies and foreclosures, which would more greatly affect the Company than if the Company's lending were more geographically diversified. In addition, the Company may suffer losses if there is a decline in the value of properties underlying the Company's mortgage loans which would have a material adverse impact on the Company's operations.

In the Event the Company's Allowance for Loan Losses is Not Sufficient to Cover Actual Loan Losses, the Company's Earnings Could Decrease

The Company maintains an allowance for loan losses in order to capture the probable losses inherent in its loan portfolio. There is a risk that the Company may experience significant loan losses which could exceed the allowance for loan losses. In determining the amount of the Company's recorded allowance, the Company makes various assumptions and judgments about the collectability of its loan portfolio, including the creditworthiness of its borrowers, the effect of changes in the local economy on the value of the real estate and other assets serving as collateral for the repayment of loans, the effects on the Company's loan portfolio of current economic indicators and their probable impact on borrowers, and the Company's loan quality reviews. The emphasis on the origination of commercial real estate and C&I loans is a significant factor in evaluating the allowance for loan losses. As the Company continues to increase the amount of these loans in the portfolio, additional or increased provisions for loan losses may be necessary and would adversely affect the results of operations. In addition, bank regulators periodically review the Company's loan portfolio and credit underwriting procedures, as well as its allowance for loan losses, and may require the Company to increase its provision for loan losses or recognize further loan charge-offs. At December 31, 2016, the Company had a gross loan portfolio of $943 million and the allowance for loan losses was $13.9 million, which represented 1.48% of the total amount of gross loans. If the Company's assumptions and judgments prove to be incorrect or bank regulators require the Company to increase its provision for loan losses or recognize further loan charge-offs, the Company may have to increase its allowance for loan losses or loan charge-offs which could have an adverse effect on the Company's operating results and financial condition. Additionally, there can be no assurances that the Company's allowance for loan losses will be adequate to protect the Company against loan losses that it may incur.

Changes in Interest Rates Could Adversely Affect the Company's Business, Results of Operations and Financial Condition

The Company's results of operations and financial condition are significantly affected by changes in interest rates. The Company's results of operations depend substantially on its net interest income, which is the difference between the interest income earned on its interest-earning assets and the interest expense paid on its interest-bearing liabilities. Because the Company's interest-bearing liabilities generally re-price or mature more quickly than its interest-earning assets, an increase in interest rates could result in a decrease in its net interest income.

Changes in interest rates also affect the value of the Company's interest-earning assets, and in particular, the Company's securities portfolio. Generally, the value of securities fluctuates inversely with changes in interest rates. At December 31, 2016, the Company's securities available for sale totaled $95 million. Net unrealized losses on securities available for sale, net of tax, amounted to $0.4 million and are reported in accumulated other comprehensive income in stockholders' equity. Decreases in the fair value of securities available for sale, therefore, could have an adverse effect on stockholders' equity or earnings.

The Company also is subject to reinvestment risk associated with changes in interest rates. Changes in interest rates may affect the average life of loans and mortgage-related securities. Decreases in interest rates can result in increased prepayments of loans and mortgage-related securities, as borrowers refinance to reduce borrowing costs. Under these circumstances, the Company is subject to reinvestment risk to the extent that it is unable to reinvest the cash received from such prepayments at rates that are comparable to the rates on existing loans and securities. Additionally, increases in interest rates may decrease loan demand and make it more difficult for borrowers to repay adjustable rate loans.

Easy monetary policy by the FRB may increase the interest rate risk for the Company by lowering interest rates over the near term, but also by inadvertently causing inflation to rise at a rapid pace. High inflation rates are usually accompanied by an increase in interest rates.

The FRB's accommodative stance has resulted in extraordinarily low interest rates during the past five years and played a part in compressing the Company's net interest margin. Further margin compression could have a material adverse effect on the Company's results of operations and financial condition.

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The Company May Be Adversely Affected by the Soundness of Other Financial Institutions

Financial services institutions are interrelated as a result of counterparty relationships. The Company has exposure to many different industries and counterparties, and routinely executes transactions with counterparties in the financial services industry. As a result, defaults by, or even rumors or questions about, one or more financial services institutions, or the financial services industry generally, could lead to losses or defaults by us or by other institutions and impact our business. Many of these transactions expose us to credit risk in the event of default of our counterparty or customer. In addition, our credit risk may be further increased when the collateral held by us cannot be relied upon or is liquidated at prices not sufficient to recover the full amount of the financial instrument exposure due to us. Any such losses could materially and adversely affect our results of operations.

The most important counterparty for the Company, in terms of liquidity, is the Federal Home Loan Bank of New York ("FHLBNY"). The Company uses FHLBNY as its primary source of borrowed overnight funds and also has several long-term advances with FHLBNY. At December 31, 2016, the Company had a total of $28 million in borrowed funds with FHLBNY. The Company has placed sufficient collateral in the form of commercial and residential real estate loans at FHLBNY. As a member of the Federal Home Loan Bank System, the Bank is required to hold stock in FHLBNY. The Bank held FHLBNY stock with a fair value of $2.2 million as of December 31, 2016.

There are 12 branches of the FHLB, including New York. If a branch were at risk of breaching risk-based capital requirements, it could suspend dividends, cut dividend payments, and/or not buy back excess FHLB stock that members hold. FHLBNY has stated that they expect to be able to continue to pay dividends, redeem excess capital stock, and provide competitively priced advances in the future. Nonetheless, the 12 FHLB branches are jointly liable for the consolidated obligations of the FHLB system. To the extent that one FHLB branch cannot meet its obligations to pay its share of the system's debt; other FHLB branches can be called upon to make the payment.

Systemic weakness in the FHLB could result in higher costs of FHLB borrowings, reduced value of FHLB stock, and increased demand for alternative sources of liquidity that are more expensive, such as brokered time deposits, the discount window at the Federal Reserve, or lines of credit with correspondent banks First Tennessee Bank and M&T Bank.

A Decline in the Value of the Company's Deferred Tax Assets Could Adversely Affect the Company's Operating Results and Regulatory Capital Ratios.

The Company's tax strategies depend on the ability to generate taxable income in future periods. The Company's tax strategies will be less effective in the event the Company fails to generate anticipated amounts of taxable income. The value of the Company's deferred tax assets is subject to an evaluation of whether it is more likely than not that they will be realized for financial statement purposes. In making this determination, management considers all positive and negative evidence available, including the Company's historical levels of taxable income, the opportunity for net operating loss carrybacks, and projections for future taxable income over the statutory tax loss carryover period. If the Company were to conclude that a significant portion of deferred tax assets were not more likely than not to be realized, the required valuation allowance could adversely affect the Company's financial position, results of operations and regulatory capital ratios. In addition, the value of the Company’s deferred tax assets could be adversely affected by a change in statutory tax rates.

Strong Competition Within the Company's Market Area May Limit the Company’s Growth and Profitability

Competition in the banking and financial services industry is intense. The Company competes with commercial banks, savings institutions, mortgage brokerage firms, credit unions, finance companies, mutual funds, insurance companies, and brokerage and investment banking firms operating locally within the Company's market area and elsewhere. Many of these competitors (whether regional or national institutions) have substantially greater resources and lending limits than the Company does, and may offer certain services that the Company does not or cannot provide. The Company's profitability depends upon its continued ability to successfully compete in this market area.

Expansion of the Company’s Branch Network May Adversely Affect its Financial Results

The Company cannot assure that the opening of new branches will be accretive to earnings or that it will be accretive to earnings within a reasonable period of time. Numerous factors contribute to the performance of a new branch, such as suitable location, qualified personnel, and an effective marketing strategy. Additionally, it takes time for a new branch to gather sufficient loans and deposits to generate income sufficient to cover its operating expenses. Difficulties the Company experiences in opening new branches may have a material adverse effect on the Company's financial condition and results of operations. The Company opened a new branch in Lockport, NY in 2016.

The Company Operates in a Highly Regulated Environment and May Be Adversely Affected By Changes in Laws and Regulations

The Company and its subsidiaries are subject to regulation, supervision and examination by the OCC, FRB, and by the FDIC, as insurer of its deposits. Such regulation and supervision govern the activities in which a bank and its holding company may engage and are intended primarily for the protection of the deposit insurance funds and depositors. Regulatory requirements affect the Company's lending practices, capital structure, investment practices, dividend policy and growth. These regulatory authorities have extensive discretion in connection with their supervisory and enforcement activities, including the imposition of restrictions on the operation of a bank, the imposition of deposit insurance premiums and other assessments, the classification of assets by a bank and the adequacy of a bank's allowance for loan losses. Any change in such regulation and oversight, particularly through the new rules and regulations expected to be established by the Dodd-Frank Act and Basel III, could have a material adverse impact on the Bank, the Company and its business, financial condition and results of operations. The election of a new President of the United States in 2016 further increases the uncertainty of future changes in regulatory requirements.

Lack of System Integrity or Credit Quality Related to Funds Settlement Could Result in a Financial Loss

The Bank settles funds on behalf of financial institutions, other businesses and consumers and receives funds from clients, card issuers, payment networks and consumers on a daily basis for a variety of transaction types. Transactions facilitated by the Bank include debit card, credit card and electronic bill payment transactions, supporting consumers, financial institutions and other businesses. These payment activities rely upon the technology infrastructure that facilitates the verification of activity with counterparties and the facilitation of the payment. If the continuity of operations or integrity of processing were compromised this could result in a financial loss to the Bank, and therefore the Company, due to a failure in payment facilitation. In addition, the Bank may issue credit to consumers, financial institutions or other businesses as part of the funds settlement. A default on this credit by a counterparty could result in a financial loss to the Bank, and therefore to the Company.

Financial Services Companies Depend on the Accuracy and Completeness of Information about Customers and Counterparties

In deciding whether to extend credit or enter into other transactions, the Company may rely on information furnished by or on behalf of customers and counterparties, including financial statements, credit reports, and other financial information. The Company may also rely on representations of those customers, counterparties, or other third parties, such as independent auditors, as to the accuracy and completeness of that information. Reliance on inaccurate or misleading financial statements, credit reports, or other financial information could cause the Company to enter into unfavorable transactions, which could have a material adverse effect on the Company's financial condition and results of operations.

Loss of Key Employees May Disrupt Relationships with Certain Customers

The Company's business is primarily relationship-driven in that many of the key employees of the Bank and TEA have extensive customer relationships. Loss of a key employee with such customer relationships may lead to the loss of business if the customers were to follow that employee to a competitor. While management believes that the Company's relationships with its key business producers are good, the Company cannot guarantee that all of its key personnel will remain with the organization. Loss of such key personnel, particularly if they enter into an employment relationship with one of the Company's competitors, could result in the loss of some of the Company's customers. Such losses could have a material adverse effect on the Company's business, financial condition and results of operations.

Future FDIC Insurance Premium Increases May Adversely Affect the Company's Earnings

The Company is generally unable to control the amount of premiums that it is required to pay for FDIC insurance. If there are additional bank or financial institution failures or other similar occurrences, the FDIC may again increase the premiums assessed upon insured institutions. Such increases and any future increases or required prepayments of FDIC insurance premiums may adversely impact the Company's results of operations.

The Company is a Financial Holding Company and Depends on Its Subsidiaries for Dividends, Distributions and Other Payments

The Company is a legal entity separate and distinct from its banking and other subsidiaries. The Company's principal source of cash flow, including cash flow to pay dividends to the Company's stockholders and principal and interest on its outstanding debt, is dividends from the Bank. There are statutory and regulatory limitations on the payment of dividends by the Bank, as well as the payment of dividends by the Company to its stockholders. Regulations of the OCC affect the ability of the Bank to pay dividends and other distributions and to make loans to the Company. If the Bank is unable to make dividend payments and sufficient capital is not otherwise available, the Company may not be able to make dividend payments to its common stockholders or principal and interest payments on its outstanding debt.

Because the Nature of the Financial Services Business Involves a High Volume of Transactions, the Company Faces Significant Operational Risks

The Company relies on the ability of its employees and systems to process a high number of transactions. Operational risk is the risk of loss resulting from the Company's operations, including but not limited to, the risk of fraud by employees or persons outside of the Company, the execution of unauthorized transactions by employees, errors relating to transaction processing and technology, breaches of the internal control system and compliance requirements, and business continuation and disaster recovery. This risk of loss also includes the potential legal actions that could arise as a result of an operational deficiency or as a result of noncompliance with applicable regulatory standards, adverse business decisions or their implementation, and customer attrition due to potential negative publicity. In the event of a breakdown in the internal control system, improper operation of systems or improper employee actions, the Company could suffer financial loss, face regulatory action and suffer damage to its reputation, any of which could have a material adverse effect on the Company's financial condition or results of operation.

The Company's Information Systems May Experience an Interruption or Breach in Security

The Company relies heavily on communications and information systems to conduct its business. Any failure, interruption, or breach in security or operational integrity of these systems could result in failures or disruptions in the Company's customer relationship management, general ledger, deposit, loan, and other systems. There can be no assurance that failures, interruptions, or security breaches of the Company's information systems will not occur or, if they do occur, that they will be adequately addressed. If personal, nonpublic, confidential, or proprietary information of customers in the Company’s possession were to be mishandled or misused, we could suffer significant regulatory consequences, reputational damage, and financial loss. Such mishandling or misuse could include, for example, if such information were erroneously provided to parties who are not permitted to have the information, either by fault of the Company’s systems, employees or counterparties, or where such information is intercepted or otherwise inappropriately taken by third parties. The occurrence of any failures, interruptions, or security breaches of the Company’s information systems could damage the Company’s reputation, result in a loss of customer business, subject the Company to additional regulatory scrutiny, or expose the Company to civil litigation and possible financial liability, any of which could have a material adverse effect on the Company’s financial condition and results of operations.

The Potential for Business Interruption Exists Throughout the Company’s Organization

Integral to the Company’s performance is the continued efficacy of our technical systems, operational infrastructure, relationships with third parties and the vast array of associates and key executives in the Company’s day-to-day and ongoing operations. Failure by any or all of these resources subjects the Company to risks that may vary in size, scale and scope. This includes, but is not limited to, operational or technical failures, pandemics, ineffectiveness or exposure due to interruption in third party support as expected, as well as the loss of key individuals or failure on the part of key individuals to perform properly. The occurrence of any such event could have a material adverse effect on the Company’s business, which, in turn, could have a material adverse effect on its financial condition and results of operations.

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Environmental Factors May Create Liability

In the course of its business, the Bank has acquired and may acquire in the future, property securing loans that are in default. There is a risk that the Bank could be required to investigate and clean-up hazardous or toxic substances or chemical releases at such properties after acquisition by the Bank in a foreclosure action, and that the Bank may be held liable to a governmental entity or third parties for property damage, personal injury and investigation and clean-up costs incurred by such parties in connection with such contamination. The Bank may in the future be required to perform an investigation or clean-up activities in connection with environmental claims. Ay such occurrence could have a material adverse effect on our business, financial condition, and results of operations.

Anti-Takeover Laws and Certain Agreements and Charter Provisions May Adversely Affect Share Value

Certain provisions of the Company’s certificate of incorporation and state and federal banking laws, including regulatory approval requirements, could make it more difficult for a third party to acquire control of the Company without approval of the Company’s board of directors. Under federal law, subject to certain exemptions, a person, entity or group must notify the FRB before acquiring control of a bank holding company. Acquisition of 10% or more of any class of voting stock of a bank holding company, including shares of the Company’s common stock, creates a rebuttable presumption that the acquiror “controls” the bank holding company. Also, a bank holding company must obtain the prior approval of the FRB before, among other things, acquiring direct or indirect ownership or control of more than 5% of the voting shares of any bank, including the Bank. There also are provisions in the Company’s certificate of incorporation that may be used to delay or block a takeover attempt. Taken as a whole, these statutory provisions and provisions in the Company’s certificate of incorporation could result in the Company being less attractive to a potential acquiror and thus could adversely affect the market price of the Company’s common stock.

Damage to the Company’s Reputation Could Adversely Impact our Business

The Company’s business reputation is important to its success. The ability to attract and retain customers, investors, employees and advisors may depend upon external perceptions of the Company. Damage to the Company’s reputation could cause significant harm to its business and prospects and may arise from numerous sources, including litigation or regulatory actions, failing to deliver minimum standards of service and quality, compliance failures, unethical behavior and the misconduct of employees, advisors and counterparties. Negative perceptions or publicity regarding these matters could damage the Company’s reputation among existing and potential customers, investors, employees and advisors. Adverse developments with respect to the financial services industry may also, by association, negatively impact the Company’s reputation or result in greater regulatory or legislative scrutiny or litigation against the Company. Preserving and enhancing the Company’s reputation also depends on maintaining systems and procedures that address known risks and regulatory requirements, as well as its ability to identify and mitigate additional risks that arise due to changes in businesses and the marketplaces in which the Company operates, the regulatory environment and client expectations. If any of these developments has a material effect on the Company’s reputation, its business could suffer.

Item 1B.UNRESOLVED STAFF COMMENTS

None.

Item 2.PROPERTIES

At December 31, 2016, the Bank conducted its business from its administrative office and 14 branch offices. The Bank's administrative office is located at One Grimsby Drive in Hamburg, NY. The administrative office facility is 26,000 square feet and is owned by the Bank. This facility is occupied by the Office of the President and Chief Executive Officer of the Company, as well as the Administrative and Loan Divisions of the Bank. The Bank also owns a building on Sunset Drive in Hamburg, NY that houses its Operations Center.

The Bank has 14 branch locations. The Bank owns the building and land for five locations. Of the remaining branch locations, eight are leased by the Bank and one is leased by TEA.

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TEA operates from a 10,000 square foot office located at 6834 Erie Road, Derby, NY, which is owned by the Bank. TEA has 7 retail locations. TEA leases one of the locations. The Bank owns three of the locations, the Bank leases two of the locations, and TEA owns the remaining building.

Item 3.LEGAL PROCEEDINGS

The nature of the Company’s business generates a certain amount of litigation involving matters arising in the ordinary course of business.

In the opinion of management, there are no proceedings pending to which the Company is a party or to which its property is subject, which, if determined adversely, would have a material effect on the Company’s financial statements.

Item 4.MINE SAFETY DISCLOSURES

Not applicable.

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PART II

Item 5.MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED

STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Market Information. The Company's common stock is listed on the NYSE MKT under the symbol EVBN.

The following table shows, for the periods indicated, the high and low sales prices per share of the Company's common stock for fiscal 2016 and 2015 as reported on the NYSE MKT.

	2016		2015	
QUARTER	High	Low	High	Low
FIRST	$ 26.10	$ 23.55	$ 25.75	$ 23.26
SECOND	$ 25.48	$ 22.87	$ 25.06	$ 23.75
THIRD	$ 27.87	$ 24.41	$ 24.95	$ 22.75
FOURTH	$ 37.67	$ 25.90	$ 25.75	$ 22.85

Holders. The approximate number of holders of record of the Company's common stock as of February 14, 2017 was 1,227.

Cash Dividends. The Company paid the following cash dividends on shares of the Company's common stock during 2016 and 2015:

- A cash dividend of $0.38 per share on October 4, 2016 to shareholders of record on September 13, 2016.
- A cash dividend of $0.38 per share on April 5, 2016 to shareholders of record on March 15, 2016.
- A cash dividend of $0.36 per share on October 6, 2015 to shareholders of record on September 15, 2015.
- A cash dividend of $0.36 per share on April 7, 2015 to shareholders of record on March 17, 2015.

The amount and type (cash or stock), if any, of future dividends will be determined by the Company's Board of Directors and will depend upon the Company's earnings, financial conditions and other factors considered by the Board of Directors to be relevant. The Bank pays a dividend to the Company to provide funds for: debt service on the junior subordinated debentures, a portion of the proceeds of which were contributed to the Bank as capital; dividends the Company pays; treasury stock repurchases; and other Company expenses. As discussed above under "Item 1A. Risk Factors," the Company is dependent upon cash flow from its subsidiaries in order to fund its dividend payments. There are various legal limitations with respect to the Bank's ability to supply funds to the Company. In particular, under Federal banking law, the approval of the FRB and OCC may be required in certain circumstances, prior to the payment of dividends by the Company or the Bank. As of December 31, 2016, approximately $12 million was available for the payment of dividends without prior OCC approval. See Note 20 to the Company's Consolidated Financial Statements included in Part II, Item 8 of this Annual Report on Form 10-K for additional information concerning contractual and regulatory restrictions on the payment of dividends.

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PERFORMANCE GRAPH

The following Performance Graph compares the Company's cumulative total stockholder return on its common stock for a five-year period (December 31, 2011 to December 31, 2016) with the cumulative total return of the NYSE MKT Composite Index and NASDAQ Bank Index. The comparison for each of the periods assumes that $100 was invested on December 31, 2011 in each of the Company's common stock and the stocks included in the NYSE MKT Composite Index and NASDAQ Bank Index and that all dividends were reinvested without commissions. This table does not forecast future performance of the Company's stock.

Compare 5-Year Cumulative Total Return Among

Evans Bancorp, Inc.,

NYSE MKT Composite Index and NASDAQ Bank Index

Index	12/31/11	12/31/12	12/31/13	12/31/14	12/31/15	12/31/16
Evans Bancorp, Inc.	100.00	135.95	187.62	222.26	242.29	305.84
NYSE MKT - Composite Index	100.00	106.61	113.71	117.99	106.95	118.33
NASDAQ Bank	100.00	118.69	168.21	176.48	192.08	265.02

In accordance with and to the extent permitted by applicable law or regulation, the information set forth above under the heading "Performance Graph" shall not be deemed to be "soliciting material" or to be "filed" with the SEC under the Securities Act or the Exchange Act, or subject to the liabilities of Section 18 of the Exchange Act, except to the extent that we specifically request that such information be treated as soliciting material or specifically incorporate it by reference into such a filing.

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Purchases of Equity Securities by the Issuer and Affiliated Purchasers. In March 2013, the Company announced it had been authorized by its Board of Directors to purchase up to 100,000 shares of the Company's outstanding common stock. The Company repurchased 3,280 shares pursuant to this repurchase program during 2016. During the fourth quarter of 2016, the Company did not purchase any shares of its common stock under this program or otherwise.

Issuer Purchases of Equity Securities

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs (1)	Maximum Number of Shares that may yet be Purchased Under the Plans or Programs
October 2016:				
October 1, 2016 - October 31, 2016	-	$ -	-	15,212
November 2016:				
November 1, 2016 - November 30, 2016	-	$ -	-	15,212
December 2016:				
December 1, 2016 - December 31, 2016	-	$ -	-	15,212
Total:	-	$ -	-	15,212

(1) On March 25, 2013, the Board of Directors authorized the Company to repurchase up to 100,000 shares of the Company's common stock. The repurchase program has no fixed expiration date but may be suspended or discontinued at any time. The maximum number of shares that may be purchased under this program as of December 31, 2016 was 15,212.

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Item 6.SELECTED FINANCIAL DATA

	As of and for the year ended December 31,				
	2016	2015	2014	2013	2012
	(in thousands, except for per share data)				
Balance Sheet Data					
Assets	$ 1,100,709	$ 939,107	$ 846,809	$ 833,498	$ 809,676
Interest-earning assets	1,030,113	873,450	785,302	767,629	750,287
Investment securities	97,205	98,758	97,132	102,049	95,807
Loans and leases, net	928,596	761,101	683,131	635,493	573,163
Deposits	939,974	802,982	707,635	706,612	678,992
Borrowings	49,689	32,151	38,808	33,681	42,441
Stockholders' equity	96,748	91,256	85,788	80,712	74,828
Income Statement Data					
Net interest income	$ 35,248	$ 31,804	$ 31,099	$ 28,347	$ 27,780
Non-interest income	11,252	13,720	10,273	12,161	12,823
Non-interest expense	35,096	32,698	31,252	29,380	28,792
Net income	8,272	7,843	8,187	7,857	8,132
Per Share Data					
Earnings per share - basic	$ 1.93	$ 1.85	$ 1.96	$ 1.88	$ 1.96
Earnings per share - diluted	1.90	1.82	1.92	1.85	1.95
Cash dividends	0.76	0.72	0.65	0.26	0.68
Book value	22.50	21.44	20.41	19.21	17.94
Performance Ratios					
Return on average assets	0.80 %	0.87 %	0.98 %	0.96 %	1.04 %
Return on average equity	8.74 %	8.82 %	9.84 %	10.06 %	11.20 %
Net interest margin	3.67 %	3.80 %	4.01 %	3.74 %	3.84 %
Efficiency ratio *	74.03 %	71.83 %	70.83 %	71.98 %	70.05 %
Dividend payout ratio	39.38 %	38.92 %	33.16 %	13.83 %	34.69 %
Capital Ratios					
Tier 1 capital to average assets	9.49 %	10.45 %	10.84 %	10.36 %	9.69 %
Equity to assets	8.79 %	9.72 %	10.13 %	9.68 %	9.24 %
Asset Quality Ratios					
Total non-performing assets to total assets	1.09 %	1.71 %	1.25 %	1.65 %	1.02 %
Total non-performing loans and leases to total loans and leases	1.28 %	2.07 %	1.52 %	2.12 %	1.41 %
Net charge-offs (recoveries) to average loans and leases	0.02 %	0.12 %	0.03 %	(0.04) %	0.29 %

Allowance for loan and lease losses to total loans and leases	1.48	%	1.66	%	1.80	%	1.78	%	1.67	%

* The calculation of the efficiency ratio excludes amortization of intangibles and gains and losses on tax credit investments, for comparative purposes.

See Item 7, “Management’s Discussion and Analysis of Financial Condition and Results of Operations,” and Item 8, “Consolidated Financial Statements and Supplementary Data,” of this Report on Form 10-K for further information and analysis of changes in the Company's financial condition and results of operations.

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

OVERVIEW

This discussion is intended to compare the performance of the Company for the years ended December 31, 2016, 2015 and 2014. The review of the information presented should be read in conjunction with Part I, Item 1: "Business" and Part II, Item 6: "Selected Financial Data" and Item 8: "Financial Statements and Supplementary Data" of this Annual Report on Form 10-K.

The Company is a financial holding company registered under the BHCA. The Company currently conducts its business through its two direct wholly-owned subsidiaries: the Bank, and the Bank's subsidiaries, ENL and ENHC; and ENFS and its subsidiary, TEA. The Company does not engage in any other substantial business. Unless the context otherwise requires, the term "Company" refers collectively to Evans Bancorp, Inc. and its subsidiaries.

Summary

Net income in 2016 was $8.3 million, a 5% increase from 2015 net income of $7.8 million, and 1% higher than 2014 net income of $8.2 million. There were several large items that impacted the 2016, 2015, and 2014 results. As a result of tax credit investments in community-based projects, in 2016 and 2014 the Company realized losses recorded in non-interest income that were more than offset by corresponding tax credit benefits, resulting in a higher income tax provision in 2015. The Company recorded $1.0 million in litigation expense in 2014 related to the Company's litigation with the New York State Attorney General's office (the "NYAG Litigation"), which was partially reversed in 2015 and 2016. A gain on insurance proceeds of $0.7 million was recorded in 2015 related to a fire at one of the Bank's branch locations.

The primary driver of the increase in the Company's earnings has been the higher net interest income resulting from the Company's significant loan and deposit growth. Net interest income was $35.2 million in 2016, an 11% increase from 2015 and 13% higher than 2014. Average loans grew from $657 million in 2014 to $841 million in 2016 while total average deposits increased from $711 million in 2014 to $868 million in 2016.

The increase in net interest income in 2016 when compared with 2015 and 2014 was partially offset by increases in non-interest expenses and decreases in non-interest income while the provision for loan losses remained approximately flat for the past three years. The increases in loans and deposits required an investment in talent as the Company's employee base is critical to the Company's growth strategy. Salaries and benefits expense, the largest component of non-interest expenses, increased 9% in each of the past two years. The largest component of the Company's non-interest income, insurance service revenue, declined to $6.5 million in 2016 from $7.2 million in 2015 and $7.1 million in 2014, primarily due to declines in financial services and insurance claims services revenue in 2016.

Strategy

The Company's goal is to continue to increase market share and achieve scale while improving profitability and returning value to shareholders. The Company's biggest strength and earnings driver is commercial and small business lending. The Company expects to continue to focus on building on this competitive advantage by adding personnel in this area. Management plans to look to expand other revenue opportunities in non-interest income in areas such as employee benefits and financial services. Additionally, management anticipates continued disruption in the Company's market area in 2017 due to recent merger activity among competitors and expects that this will create additional opportunities to increase market share and secure new customer relationships. In addition, management intends to continue to develop strategies to deepen existing customer relationships with tailored product sets that reward the Company's most loyal customers.

The Company's strategies are designed to direct tactical investment decisions supporting its financial objectives. While the Company intends to focus its efforts on the pursuit of these strategies, there can be no assurance that the Company will successfully implement these strategies or that the strategies will produce the desired results. The Company's most significant revenue source continues to be net interest income, defined as total interest income less interest expense. Net interest income accounted for 76% of total revenue in 2016. To produce net interest income and consistent earnings growth over the long-term, the Company must generate loan and deposit growth at acceptable margins within its market area. To generate and grow loans and deposits, the Company must focus on a number of areas including, but not limited to, sales practices, customer and employee satisfaction and retention, competition, evolving customer behavior, technology, product innovation, interest rates, credit performance of its customers and vendor relationships.

The Company also considers non-interest income important to its continued financial success. Fee income generation is partly related to the Company's loan and deposit operations, such as deposit service charges, as well as to its financial products, such as commercial and personal insurance sold through TEA. Improved performance in non-interest income can help increase capital ratios because most of the non-interest income is generated without recording assets on the balance sheet. The Company has and will continue to face challenges in increasing its non-interest income as the regulatory environment changes.

The Company has focused its efforts on targeted groups in its community such as (1) smaller businesses with smaller credit needs but rich in deposits and other service needs; (2) middle market commercial businesses; (3) commercial real estate lending; and (4) retail customers. In 2017, the Company intends to expand its targeted groups to include municipal customers. The overarching goal is to cross-sell between our insurance, financial services and banking lines of business to deepen our relationships with all of our customers. The Company believes that these efforts resulted in growth in the commercial loan portfolio and core deposits during fiscal 2016.

The Company strives to provide a personal touch to customer service and is committed to maintaining a local, community-based philosophy. The Bank has emphasized hiring local branch and lending personnel with strong ties to the specific local communities it serves.

The Bank serves its market through 14 banking offices in Western New York. The Company's principal source of funding is through deposits, which it reinvests in the community in the form of loans and investments. Deposits are insured up to the maximum permitted by the Deposit Insurance Fund of the FDIC. The Bank is regulated by the OCC.

APPLICATION OF CRITICAL ACCOUNTING ESTIMATES

The Company's Consolidated Financial Statements are prepared in accordance with U.S. generally accepted accounting principles ("GAAP") and follow general practices within the industries in which it operates. Application of these principles requires management to make estimates, assumptions and judgments that affect the amounts reported in the Company's Consolidated Financial Statements and Notes. These estimates, assumptions and judgments are based on information available as of the date of the Consolidated Financial Statements. Accordingly, as this information changes, the Consolidated Financial Statements could reflect different estimates, assumptions and judgments. Certain policies inherently have a greater reliance on the use of estimates, assumptions and judgments, and as such, have a greater possibility of producing results that could be materially different than originally reported.

The most significant accounting policies followed by the Company are presented in Note 1 to the Consolidated Financial Statements included in Item 8 of this Annual Report on Form 10-K. These policies, along with the disclosures presented in the other Notes to the Company's Consolidated Financial Statements contained in this Annual Report on Form 10-K and in this financial review, provide information on how significant assets and liabilities are valued in the Company’s Consolidated Financial Statements and how those values are determined.

Estimates, assumptions and judgments are necessary when assets and liabilities are required to be recorded at fair value, when a decline in the value of an asset not carried on the financial statements at fair value warrants an impairment write-down or valuation reserve to be established, or when an asset or liability needs to be recorded contingent upon a future event. Carrying assets and liabilities at fair value inherently results in more financial statement volatility. The fair values and the information used to record valuation adjustments for certain assets and liabilities are based either on quoted market prices or are provided by other third-party sources, when available. When third-party information is not available, valuation adjustments are estimated in good faith by management primarily through the use of internal cash flow modeling techniques.

Based on the valuation techniques used and the sensitivity of financial statement amounts to the methods, assumptions and estimates underlying those amounts, management has identified the determination of the allowance for loan losses and valuation of goodwill to be the accounting areas that require the most subjective or complex judgments, and as such, could be most subject to revision as new information becomes available.

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Allowance for Loan Losses

The allowance for loan losses represents management's estimate of probable losses in the Bank's loan portfolio. Determining the amount of the allowance for loan losses is considered a critical accounting estimate because it requires significant judgment on the part of management and the use of estimates related to the amount and timing of expected future cash flows on impaired loans, estimated losses on pools of homogeneous loans based on historical loss experience and consideration of current economic trends and conditions, all of which may be susceptible to significant change. The loan portfolio also represents the largest asset type on the Company's consolidated balance sheets.

Management methodology and policy in determining the allowance for loan losses can be found in Note 1 to the Consolidated Financial Statements included in Item 8 of this Annual Report on Form 10-K. The activity in the allowance for loan losses is depicted in supporting tables in Note 3 to the Consolidated Financial Statements included in Item 8 of this Annual Report on Form 10-K

Goodwill and Intangible Assets

The amount of goodwill reflected in the Company's Consolidated Financial Statements is required to be tested by management for impairment on at least an annual basis. The test for impairment of goodwill in an identified reporting unit is considered a critical accounting estimate because it requires judgment on the part of management and the use of estimates related to the growth assumptions and market multiples used in the valuation model. As of December 31, 2016, TEA had $8.1 million in goodwill. The banking reporting unit does not have any goodwill. All of the goodwill at TEA stems from the acquisition of various insurances agencies, not the purchase of diverse companies in which goodwill was subjectively allocated to different reporting units. Therefore, total market capitalization reconciliation was not performed because not all of the reporting units had goodwill. As a result, such an analysis would not be meaningful.

Management valued TEA, the reporting unit with goodwill, using cash flow modeling and earnings multiple techniques. When using the cash flow models, management considered historical information, the operating budget for 2017, economic and insurance market cycles, and strategic goals in projecting net income and cash flows for the next five years. The fair value calculated substantially exceeded the book value of TEA. The value based on a multiple to earnings before interest, taxes, depreciation, and amortization ("EBITDA") was higher, a result of conservative growth assumptions used by the Company in the cash flow model as well as an implied control premium in the multiple. The multiple used was based on industry data and consistent with the previous year's assumption.

While the fair values determined in the impairment tests were substantially higher than the carrying value for TEA, the risk of a future impairment charge still exists. Management used growth rates that are achievable over the long run through both soft and hard insurance cycles. Decline in TEA's revenue in 2016 was largely attributable to its insurance claims business, which experienced an abnormally strong 2015 and lower claims activity in 2016. Also, for the second straight year, TEA's profit sharing revenue was lower than historical norms. TEA's largest revenue source, its commercial insurance commissions, experienced solid growth in 2016 which is expected to continue while profit sharing revenue and insurance claims are expected to rebound to more normal historical levels.

For further discussion of the Company's accounting for goodwill and other intangible assets, see Note 1 to the Consolidated Financial Statements included in Item 8 of this Annual Report on Form 10-K.

RECENT ACCOUNTING PRONOUNCEMENTS AND DEVELOPMENTS

Below are accounting policies recently issued or proposed but not yet required to be adopted. To the extent management believes the adoption of new accounting standards materially affects the Company's financial condition, results of operations, or liquidity, the impacts are discussed below.

Accounting Standards Update ("ASU") 2014-09, Revenue from Contracts with Customers. The objective of this ASU is to require entities to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. This ASU will replace most existing revenue recognition guidance under U.S. GAAP when it becomes effective. The amendments in this ASU are effective for annual reporting periods beginning after December 15, 2016, including interim periods within that reporting period. The Company does not expect the standard to have a material impact on its ongoing financial reporting.

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ASU 2016-01, Recognition and Measurement of Financial Assets and Financial Liabilities. The main objective of this ASU is to enhance the reporting model for financial instruments to provide users of financial statements with more decision-useful information. The amendments in this ASU are effective for annual reporting periods beginning after December 15, 2017, including interim periods within those fiscal years. The ASU will not impact results of operations or the financial position of the Company, but will impact its fair value disclosures in the notes to the financial statements.

ASU 2016-02, Leases. The objective of this ASU is to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements to meet that objective. The main difference between previous GAAP and this ASU is the recognition of lease assets and lease liabilities by lessees for those leases classified as operating leases under previous GAAP. Under this new guidance, a lessee should recognize in the statement of financial position a liability to make lease payments and a right-of-use asset representing its right to use the underlying asset for the lease term. The recognition, measurement, and presentation of expenses and cash flows arising from a lease by a lessee have not significantly changed from previous GAAP. Information about the Company's operating lease obligations is disclosed in Note 16 to the Company's Consolidated Financial Statements included in Item 8 of this Annual Report on Form 10-K. The amendments in this ASU are effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. The Company is currently evaluating the impact of the standard on its financial reporting.

ASU 2016-09, Improvements to Employee Share-Based Payment Accounting. This ASU is part of the FASB's Simplification Initiative. The areas for simplification in this Update involve several aspects of the accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. Some of the areas of simplification apply only to nonpublic entities. Although the impact on the Company's financial statements is not expected to be material, the area of this ASU that will impact the Company is the elimination of the concept of a tax windfall pool. Currently, an entity must determine for each award whether the difference between the deduction for tax purposes and the compensation cost recognized for financial reporting purposes results in either an excess benefit or a tax deficiency. Excess tax benefits are recognized in additional paid-in-capital; tax deficiencies are recognized either as an offset to accumulated excess tax benefits, if any, or in the income statement. Excess tax benefits are not recognized until the deduction reduces taxes payable. Under the new standard, all excess tax benefits and tax deficiencies will be recognized as income tax expense or benefit in the income statement. The amendments in this ASU are effective for annual periods beginning after December 15, 2016, and interim periods within those annual periods.

ASU 2016-13, Financial Instruments – Credit Losses: Measurement of Credit Losses on Financial Instruments. Current GAAP requires an "incurred loss" methodology for recognizing credit losses that delays recognition until it is probable a loss has been incurred. Both financial institutions and users of their financial statements expressed concern that current GAAP restricts the ability to record credit losses that are expected, but do not yet meet the "probable" threshold. The main objective of this ASU (commonly known as the Current Expected Credit Loss Impairment Model, or CECL, in the industry) is to provide financial statement users with more decision-useful information about the expected credit losses on financial instruments and other commitments to extend credit held by a reporting entity at each reporting date. To achieve this objective, the amendments in CECL replace the incurred loss impairment methodology in current GAAP with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to inform credit loss estimates. The amendments in CECL are effective for the Company for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. The FASB expects that an entity will be able to leverage its current systems and methods for recording the allowance for credit losses. However, many financial institutions, particularly community banks similar in size to the Company and industry groups like the American Bankers Association, have expressed concern about the impact of CECL. The life of loan loss concept presents complexities that can decrease capital, and add both volatility to ALLL estimates and additional costs. CECL may increase the ALLL, though many factors will determine the impact for each bank. Changes in expectations of future economic conditions play a large role in CECL and can significantly affect the credit loss estimate. While OCC estimates made in 2012 projected a 30% to 50% increase in the ALLL, more recent bank analyst projections were far lower. A challenge for the Company could be the operational impact. Costly new systems and process to track loan performance may need to be purchased or developed. Significant procedural challenges may be faced both in implementation and on an ongoing basis. The total impact of CECL to the Company's financial statements is unknown but may be material. Implementation of CECL will be a significant project for the Company through the projected implementation date of January 1, 2020.

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RESULTS OF OPERATIONS FOR THE YEARS ENDED DECEMBER 31, 2016 AND DECEMBER 31, 2015

Net Income

Net income of $8.3 million in 2016 consisted of $7.5 million related to the Company’s banking activities and $0.8 million related to the Company’s insurance agency activities. The total net income of $8.3 million was a 5% increase from $7.8 million in 2015. Earnings per diluted share for 2016 of $1.90 were 4% higher than the earnings per diluted share of $1.82 for 2015.

Net Interest Income

Net interest income, the difference between interest income and fee income on earning assets, such as loans and securities, and interest expense on deposits and borrowings, provides the primary basis for the Company’s results of operations.

Net interest income is dependent on the amounts and yields earned on interest earning assets as compared to the amounts of and rates paid on interest bearing liabilities.

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AVERAGE BALANCE SHEET INFORMATION

The following table presents the significant categories of the assets and liabilities of the Company, interest income and interest expense, and the corresponding yields earned and rates paid in 2016, 2015, and 2014. The assets and liabilities are presented as daily averages. The average loan balances include both performing and non-performing loans. Interest income on loans does not include interest on loans for which the Bank has ceased to accrue interest. Available-for-sale securities are stated at fair value. Interest and yield are not presented on a tax-equivalent basis.

	2016 Average Outstanding Balance (in thousands)	Interest Earned/ Paid	Yield/ Rate	2015 Average Outstanding Balance (in thousands)	Interest Earned/ Paid	Yield/ Rate	2014 Average Outstanding Balance (in thousands)	Interest Earned/ Paid	Yield/ Rate
ASSETS									
Interest-earning assets:									
Loans, net	$ 841,443	$ 37,330	4.44 %	$ 705,404	$ 32,638	4.63 %	$ 657,494	$ 31,899	4.85 %
Taxable securities	71,000	1,652	2.33 %	68,156	1,935	2.84 %	71,508	1,816	2.54 %
Tax-exempt securities	38,014	926	2.44 %	37,076	991	2.67 %	32,766	967	2.95 %
Interest bearing deposits at banks	9,333	47	0.50 %	26,170	64	0.24 %	14,100	33	0.23 %
Total interest-earning assets	959,790	$ 39,955	4.16 %	836,806	$ 35,628	4.26 %	775,868	$ 34,715	4.47 %
Non interest-earning assets:									
Cash and due from banks	13,157			12,591			12,365		
Premises and equipment, net	11,350			10,448			10,982		
Other assets	43,671			42,211			39,971		
Total Assets	$ 1,027,968			$ 902,056			$ 839,186		
LIABILITIES & STOCKHOLDERS' EQUITY									
Interest-bearing liabilities:									
NOW	$ 87,215	$ 262	0.30 %	$ 78,801	$ 322	0.41 %	$ 72,034	$ 316	0.44 %
Regular savings	478,252	2,318	0.48 %	418,020	1,591	0.38 %	378,247	1,010	0.27 %
Time deposits	117,682	1,460	1.24 %	102,711	1,426	1.39 %	111,521	1,730	1.55 %

Other borrowed funds	26,011	270	1.04 %	9,655	136	1.41 %	8,579	212	2.47 %
Junior subordinated debentures	11,330	372	3.28 %	11,330	327	2.89 %	11,330	322	2.84 %
Securities sold U/A to repurchase	12,884	25	0.19 %	11,495	22	0.19 %	13,956	26	0.19 %
Total interest-bearing liabilities	733,374	$ 4,707	0.64 %	632,012	$ 3,824	0.61 %	595,667	$ 3,616	0.61 %
Noninterest-bearing liabilities:									
Demand deposits	185,029			166,611			148,827		
Other	14,942			14,529			11,529		
Total liabilities	$ 933,345			$ 813,152			$ 756,023		
Stockholders' equity	94,623			88,904			83,163		
Total Liabilities and Equity	$ 1,027,968			$ 902,056			$ 839,186		
Net interest earnings		$ 35,248			$ 31,804			$ 31,099	
Net interest margin			3.67 %			3.80 %			4.01 %
Interest rate spread			3.52 %			3.65 %			3.86 %

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The following table segregates changes in interest earned and paid for the past two years into amounts attributable to changes in volume and changes in rates by major categories of assets and liabilities. The change in interest income and expense due to both volume and rate has been allocated in the table to volume and rate changes in proportion to the relationship of the absolute dollar amounts of the change in each.

	2016 Compared to 2015 Increase (Decrease) Due to (in thousands)			2015 Compared to 2014 Increase (Decrease) Due to		
	Volume	Rate	Total	Volume	Rate	Total
Interest earned on:						
Loans	$ 6,081	$ (1,389)	$ 4,692	$ 2,259	$ (1,520)	$ 739
Taxable securities	78	(361)	(283)	(88)	207	119
Tax-exempt securities	25	(90)	(65)	120	(96)	24
Interest-bearing deposits at banks	(58)	41	(17)	29	2	31
Total interest-earning assets	$ 6,126	$ (1,799)	$ 4,327	$ 2,320	$ (1,407)	$ 913
Interest paid on:						
NOW accounts	$ 32	$ (92)	$ (60)	$ 29	$ (23)	$ 6
Savings deposits	251	476	727	115	466	581
Time deposits	195	(161)	34	(131)	(173)	(304)
Other borrowed funds	241	(59)	182	(22)	(53)	(75)
Total interest-bearing liabilities	$ 719	$ 164	$ 883	$ (9)	$ 217	$ 208

Net interest income increased by $3.4 million, or 11%, to $35.2 million in 2016 from $31.8 million in 2015. As indicated in the preceding table, this increase primarily resulted from increased loan volume, partially offset by lower yields earned on loans and investment securities. Overall, the increased volume of interest-earning assets and interest-bearing liabilities positively impacted net interest income by $5.4 million, while the rates earned and paid on those respective assets and liabilities had a negative impact of $2.0 million.

The Company has invested in adding to its commercial loan portfolio significantly in the past several years by adding several commercial loan officers while existing loan officers have increased production. The total commercial loan portfolio balance, including commercial real estate and C&I loans, increased $123 million, or 22%, from a $556 million average balance in 2015 to a $679 million average balance in 2016. Consumer loans increased 8% from a $162 million average balance in 2015 to a $175 million average balance in 2016.

On the funding side, the Company has continued to be successful in attracting new deposit customers, with most of that success coming from growth in retail savings deposits and commercial demand deposit products. The Company marketed attractive retail savings and time deposit products to fund the strong commercial loan growth. The Company's increasing C&I loan production has resulted in a corresponding increase in commercial demand deposits. Total average deposits increased $102 million, or 13%, year over year to $868 million in 2016. The largest component of that growth was in average savings deposits of $60 million. Average demand deposits increased $18 million, including $15 million in commercial demand deposits, from 2015 to 2016. Average time deposits grew $15 million from 2015 to 2016.

The FRB executed on a monetary policy designed to keep interest rates at all time lows from the second half of 2008 until the fourth quarter of 2015. The target overnight rate had been between 0.00% and 0.25% since the end of 2008 until the FRB raised its target rate to between 0.25% and 0.50% in December 2015. The target rate was raised again in December 2016 to

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between 0.50% and 0.75%. The impact of the FRB decision to raise its targeted overnight rate in December 2015 had a positive impact on the Company's 2016 results while the increase in late 2016 had minimal impact on the Company's 2016 results. The FRB has also executed on other quantitative easing strategies, including the purchase of mortgage-backed securities, in an attempt to depress longer-term market interest rates. Although the FRB has stopped its asset purchases, its accommodation policy kept rates historically low during the same period. This interest rate environment resulted in lower interest yields earned on assets as well as lower rates paid on liabilities. Assets have continued to re-price into lower yields as older loans and securities mature, and new loans are originated and securities purchased at lower yields than those they are replacing.

Net interest spread, or the difference between yield on interest-earning assets and rate on interest-bearing liabilities, decreased from 3.65% in 2015 to 3.52% in 2016. The yield on interest-earning assets decreased 10 basis points from 4.26% in 2015 to 4.16% in 2016, while the cost of interest-bearing liabilities increased 3 basis points to 0.64% over the same time periods. The decline in interest-earning asset yields is a result of the continued asset re-pricing described above. The increase in the cost of interest-bearing liabilities reflects the continued shift in the savings deposit portfolio to higher rate products. The Company has very low cost core savings deposits that are more mature in their life cycle and did not grow in 2016. Simultaneously, the Company has offered attractive rates on certain savings products in an effort to fund the Company's strong loan growth.

The Company's net interest margin decreased from 3.80% in 2015 to 3.67% in 2016, reflecting the changes to the net interest spread. Several factors could put additional pressure on the Company's net interest margin in the future, including further flattening of the yield curve and increased pricing competition for loans and deposits.

The Bank regularly monitors its exposure to interest rate risk. Management believes that the proper management of interest-sensitive funds will help protect the Bank's earnings against changes in interest rates. The Bank's Asset/Liability Management Committee ("ALCO") meets monthly for the purpose of evaluating the Bank's short-term and long-term liquidity position and the potential impact on capital and earnings of changes in interest rates. The Bank has adopted an asset/liability policy that specifies minimum limits for liquidity and capital ratios. This policy includes setting ranges for the negative impact acceptable on net interest income and on the fair value of equity as a result of a shift in interest rates. The asset/liability policy also includes guidelines for investment activities and funds management. At its monthly meetings, ALCO reviews the Bank's status and formulates its strategies based on current economic conditions, interest rate forecasts, loan demand, deposit volatility and the Bank's earnings objectives.

Provision for Loan Losses

The Company's provision for loan losses was $1.2 million in both 2016 and 2015. The provision was flat year over year as increases in reserves for impaired loans, the level of criticized loans, and loan growth were offset by the impact of the sustained low level of historical losses in the portfolio. The allowance for loan loss allocation for impaired loans increased from $1.7 million at the end of 2015 to $2.0 million at December 31, 2016. The higher reserve for impaired loans reflected an increase in reserve on the Company's largest impaired loan after a new appraisal was obtained in 2016 that demonstrated a decrease in the value of the collateral securing the loan. As noted in Note 1 to the Consolidated Financial Statements included in Item 8 of this Annual Report on Form 10-K, the Company reserves a specific allocation on impaired loans and a higher percentage on criticized loans, or those loans risk-rated 5 or higher. At December 31, 2016, criticized loans (i.e. loans risk-rated 5 or higher) that were collectively evaluated for impairment were $28.1 million, compared with $26.7 million at December 31, 2015. Overall, total loans collectively evaluated for impairment increased $173 million to $927 million at the end of 2016 from $754 million as of December 31, 2015. Offsetting the increase in the provision for loan losses related to these factors was a reduction in the Company's allowance related to its historical loss experience. The Company has sustained historical loss experience at extremely low levels for a period of time sufficient that management determined that it was appropriate to lower the allowance allocation determined by historical losses in accordance with the Bank's allowance for loan losses policy.

A description of how the allowance for loan losses is determined along with tabular data depicting the key factors in calculating the allowance is set forth in Notes 1 and 3 of the Notes to Consolidated Financial Statements included in Part II, Item 8 of this Annual Report on Form 10-K.

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Non-accrual, Past Due and Restructured Loans

The following table summarizes the Bank's non-accrual and accruing loans 90 days or more past due as of the dates listed below. See Note 3 of the Notes to Consolidated Financial Statements included in Part II, Item 8 of this Annual Report on Form 10-K for further information about the Company's non-accrual, past due and restructured loans.

	At December 31,				
	2016	2015	2014	2013	2012
	(in thousands)				
Non-accruing loans and leases:					
Mortgage loans on real estate:					
Residential mortgages	$ 862	$ 1,400	$ 1,296	$ 1,376	$ 1,443
Commercial and multi-family	1,874	3,574	3,162	8,873	4,309
Construction-residential	-	-	-	-	-
Construction-commercial	4,178	4,187	-	-	729
Home equities	1,261	1,058	415	447	618
Total mortgage loans on real estate	8,175	10,219	4,873	10,696	7,099
Direct financing leases	-	-	-	47	171
Commercial and industrial loans	3,106	5,312	5,500	2,970	914
Consumer and other loans	17	14	17	20	44
Total non-accruing loans and leases	$ 11,298	$ 15,545	$ 10,390	$ 13,733	$ 8,228
Accruing loans 90+ days past due	722	497	201	-	-
Total non-performing loans and leases	$ 12,020	$ 16,042	$ 10,591	$ 13,733	$ 8,228
Total non-performing loans and leases to total assets	1.09 %	1.71 %	1.25 %	1.65 %	1.02 %
Total non-performing loans and leases to total loans and leases	1.28 %	2.07 %	1.52 %	2.12 %	1.41 %

Non-performing loans decreased $4.0 million from $16.0 million at December 31, 2015 to $12.0 million at December 31, 2016. The decrease in 2016 was primarily driven by one large commercial loan relationship of $3.6 million being upgraded to performing status.

Non-accruing loans decreased $4.2 million from $15.5 million at December 31, 2015 to $11.3 million at December 31, 2016. Accruing loans categorized as 90 days past due increased from $0.5 million at December 31, 2015 to $0.7 million at December 31, 2016. The decrease in non-accruing loans was across several loan types including commercial and multi-family real estate, C&I loans, and residential mortgages. The decrease in non-accruing commercial real estate loans was attributable to the payoff of a $1.9 million loan to a medical facility. The decline in C&I loans was due to the upgrade of a $3.6 million commercial loan relationship with a commercial contractor, partially offset by the downgrade to nonaccrual status of other C&I loan relationships.

The Company had $5.1 million in loans that were restructured and deemed to be a troubled debt restructuring (“TDR”) at December 31, 2016 with $1.3 million of those balances in non-accrual status, compared with $5.8 million and $1.8 million, respectively, at December 31, 2015. Any TDR that is placed on non-accrual is not returned to accruing status until the borrower makes timely payments as contracted for at least six months and future collection under the revised terms is probable. All of the restructurings were allowed in an effort to maximize the Company’s ability to collect on loans where borrowers were experiencing financial difficulty. Modifications made to loans in a troubled debt restructuring did not have a

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material impact on the Company's net income for the years ended December 31, 2016 and 2015. The reserve for a TDR is based upon the present value of the future expected cash flows discounted at the loan's original effective rate or upon the fair value of the collateral less costs to sell, if the loan is deemed collateral dependent. This reserve methodology is used because all TDR loans are considered impaired.

The following table presents the Company's TDR loans as of December 31, 2016:

	December 31, 2016 (in thousands)			
	Total	Nonaccruing	Accruing	Related Allowance
Commercial and industrial	$ 599	$ 557	$ 42	$ 147
Residential real estate:				
Residential	1,949	227	1,722	-
Construction	-	-	-	-
Commercial real estate:				
Commercial and multi-family	1,617	313	1,304	-
Construction	257	-	257	-
Home equities	667	175	492	1
Consumer and other loans	26	-	26	26
Total troubled restructured loans	$ 5,115	$ 1,272	$ 3,843	$ 174

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Allowance for Loan and Lease Losses

The following table summarizes the Bank's allowance for loan losses and changes in the allowance for loan and lease losses by categories:

	ANALYSIS OF THE ALLOWANCE FOR LOAN AND LEASE LOSSES				
	2016	2015	2014	2013	2012
	(in thousands)				
BALANCE AT THE BEGINNING OF THE YEAR	$ 12,883	$ 12,533	$ 11,503	$ 9,732	$ 11,495
CHARGE-OFFS:					
Residential mortgages	-	(66)	-	(39)	(12)
Commercial and multi-family	-	(139)	(57)	(460)	(900)
Home equities	-	-	(2)	(128)	(114)
Direct financing leases	-	-	-	-	-
Commercial and industrial loans	(360)	(799)	(957)	(20)	(862)
Consumer installment and other loans	(47)	(43)	(46)	(64)	(32)
TOTAL CHARGE-OFFS	(407)	(1,047)	(1,062)	(711)	(1,920)
RECOVERIES:					
Residential mortgages	2	2	18	2	1
Commercial and multi-family	59	44	58	444	15
Home equities	3	-	-	1	6
Direct financing leases	-	-	173	242	-
Commercial and industrial loans	151	126	574	240	184
Consumer installment and other loans	16	9	40	13	19
TOTAL RECOVERIES	231	181	863	942	225
NET (CHARGE-OFFS) RECOVERIES	(176)	(866)	(199)	231	(1,695)
PROVISION FOR LOAN AND LEASE LOSSES	1,209	1,216	1,229	1,540	(68)
BALANCE AT THE END OF YEAR	$ 13,916	$ 12,883	$ 12,533	$ 11,503	$ 9,732
RATIO OF NET CHARGE-OFFS (RECOVERIES) TO AVERAGE NET LOANS AND LEASES OUTSTANDING	0.02 %	0.12 %	0.03 %	(0.04) %	0.29 %

RATIO OF ALLOWANCE FOR LOAN AND LEASE LOSSES TO TOTAL LOANS AND LEASES	1.48	%	1.66	%	1.80	%	1.78	%	1.67	%

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Net charge-offs decreased from $0.9 million in 2015 to $0.2 million in 2016. The ratio of net charge-offs to average net loans outstanding correspondingly decreased from 0.12% in 2015 to 0.02% in 2016. The largest charge-off in 2016 occurred in the fourth quarter for $0.2 million in the C&I loan portfolio due to the deterioration in a commercial loan to a retail business.

An allocation of the allowance for loan and lease losses by portfolio type over the past five years follows:

	Balance at 12/31/2016 attributable to: (in thousands)	Percent of loans in each category to total loans:	Balance at 12/31/2015 attributable to:	Percent of loans in each category to total loans:	Balance at 12/31/2014 attributable to:	Percent of loans in each category to total loans:	Balance at 12/31/2013 attributable to:	Percent of loans in each category to total loans:	Balance at 12/31/2012 attributable to:	Percent of loans in each category to total loans:
Residential mortgages*	$ 769	13 %	$ 909	14 %	$ 941	14 %	$ 1,038	15 %	$ 662	12 %
Commercial mortgages*	7,890	59 %	7,135	59 %	5,650	58 %	4,912	59 %	4,493	61 %