



A N N U A L 2 0 1 6 R E P O R T



A photograph of a sailboat at sunset. The boat is in the foreground, its mast and rigging silhouetted against the bright orange and yellow sky. The water is calm, reflecting the colors of the sunset. In the background, there are silhouettes of trees and a few lights on the shore.

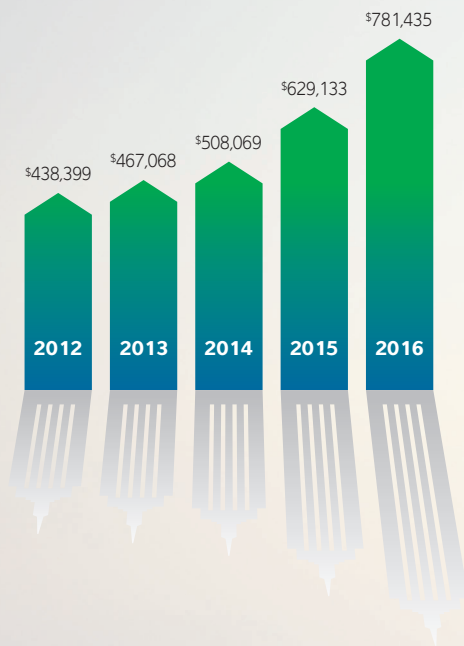
O U R M I S S I O N

To offer the community banking products and services shaped by emerging ideas and technologies, combined with time-honored values of trust, integrity, and commitment; to provide the highest quality service with a sense of urgency.

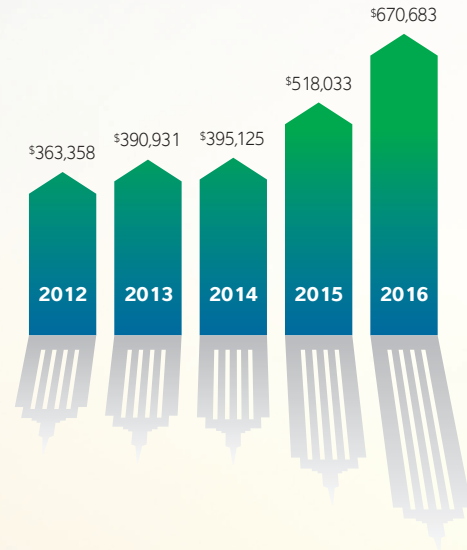
SELECTED FINANCIAL DATA

(dollars in thousands)

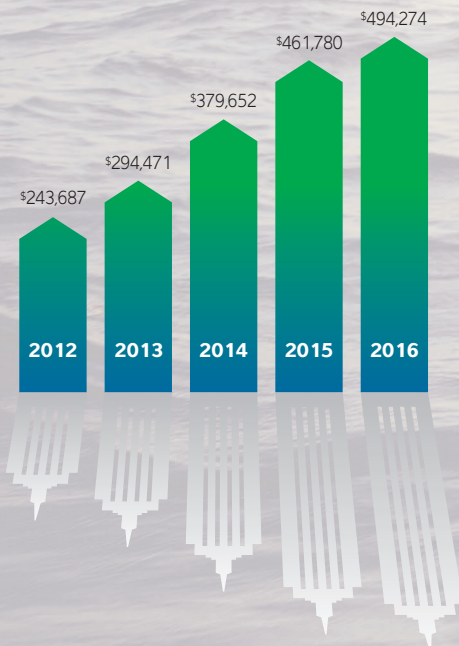
TOTAL ASSETS



TOTAL DEPOSITS



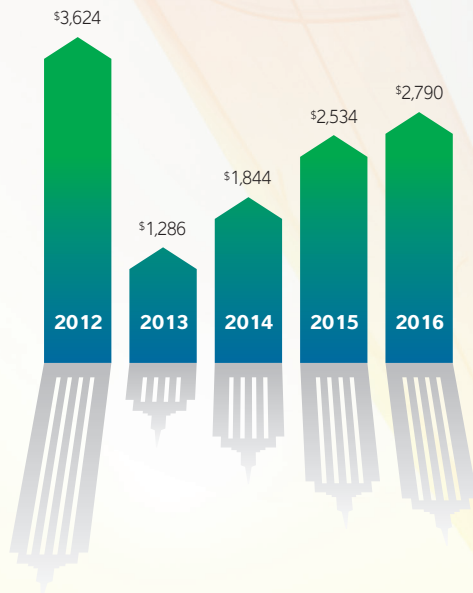
TOTAL LOANS



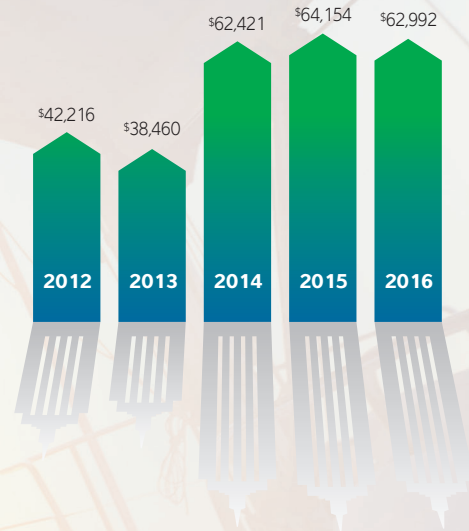
NON-PERFORMING LOANS TO TOTAL LOANS



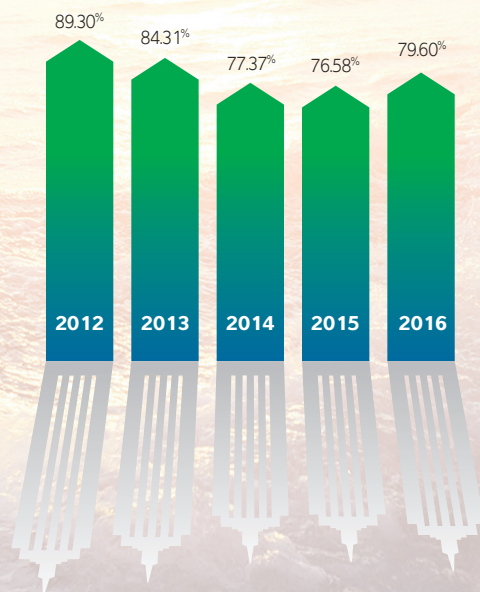
NET INCOME



TOTAL STOCKHOLDER'S EQUITY



OPERATING EFFICIENCY RATIO



NET INTEREST MARGIN



FINANCIAL HIGHLIGHTS

(in thousands, except per share data and financial ratios)

For the year ended December 31,

	2016	2015	2014	2013	2012
FINANCIAL CONDITION DATA:					
Total Assets	\$781,435	\$629,133	\$508,069	\$467,068	\$438,399
Total Loans	\$494,274	\$461,780	\$379,652	\$294,471	\$243,687
Total Deposits	\$670,683	\$518,033	\$395,125	\$390,931	\$363,358
Total Demand Deposits	\$177,299	\$189,200	\$189,204	\$177,252	\$172,165
Total Stockholders' Equity	\$ 62,992	\$ 64,154	\$ 62,421	\$ 38,460	\$ 42,216

SELECTED STATISTICAL DATA:

Net Interest Margin	3.05%	3.75%	3.55%	3.29%	3.48%
Return on Average Assets	0.39%	0.47%	0.38%	0.29%	0.90%
Return on Average Equity	4.19%	3.98%	4.43%	3.19%	8.90%
Efficiency Ratio	79.60%	76.58%	77.37%	84.31%	89.30%

RATIOS:

Net Charge-offs to Average Loans	0.02%	0.03%	0.01%	0.08%	0.01%
Non-performing Loans to Total Loans	0.48%	0.12%	0.31%	0.81%	1.09%
Non-performing Assets to Total Assets	0.30%	0.09%	0.23%	0.51%	0.61%
Allowance for Loan Losses to Total Loans	1.17%	1.14%	1.17%	1.44%	1.84%
Tier 1 Leverage Capital Ratio	10.22%	12.22%	12.65%	9.01%	9.52%
Common Equity Tier 1 Risk-Based Capital Ratio	16.26%	16.83%	–	–	–
Tier 1 Risk-Based Capital Ratio	16.26%	16.83%	16.02%	12.78%	14.65%
Total Risk-Based Capital Ratio	17.46%	18.01%	17.17%	14.03%	15.90%

OPERATING DATA:

Net Interest Income	\$ 21,567	\$ 19,815	\$ 16,863	\$ 14,437	\$ 13,428
Provision for Loan Losses	\$ 632	\$ 867	\$ 243	–	\$ 285
Other Income	\$ 1,477	\$ 1,005	\$ 1,033	\$ 898	\$ 1,941
Other Expense	\$ 18,068	\$ 15,998	\$ 13,825	\$ 13,054	\$ 12,532
Net Income	\$ 2,790	\$ 2,534	\$ 1,844	\$ 1,286	\$ 3,624

PER SHARE DATA:

Diluted Earnings Per Share	\$ 0.40	\$ 0.37	\$ 0.41	\$ 0.29	\$ 0.83
Book Value	\$ 9.07	\$ 9.32	\$ 9.07	\$ 8.78	\$ 9.64

NOTE: Selected financial data and financial highlights from 2013 through 2016 were derived from the audited consolidated financial statements of Empire Bancorp, Inc. Selected financial data and financial highlights for periods prior to 2013 were derived from the audited financial statements of Empire National Bank. Regulatory capital ratios presented on bank-only basis.

DEAR SHAREHOLDER

Net income, measured on a consolidated basis, for 2016 increased \$256 thousand, or 10.1%, to \$2.8 million from 2015. Total assets exceeded \$781 million, a 24.2% increase from our footings one year earlier, and a 78.2% increase from our closing assets at our fiscal year end five years ago. As we continue our growth trek towards one billion dollars in assets, we are working on improving operating efficiency and growing into our existing infrastructure. Emphasis will be on improving returns for our shareholders while tempering the pace of our growth. Building shareholder value remains our underlying prime objective, and we are cognizant of the impact of our business decisions as we continue to build our book value.

We absorbed a full year of debt service at the parent level relative to the 2015 subordinated debt raise, yet net interest income increased \$1.8 million, or 8.8%, for the year ended December 31, 2016 over the prior year. The low rate environment for most of 2016 weighed on our net interest margin of 3.05%, a decrease from 3.75% for the year ended December 31, 2015. The heightened loan prepayment pressure we experienced in 2015 lessened with the uptick in interest rates as the ten year benchmark rate increased one hundred basis points between July and the end of November. A substantial decline in the revenues from prepayment fees in 2016, as compared to 2015, contributed to the decrease in the average yield on loans year over year.

Our risk management processes throughout the bank remain integral to our success. The year 2016 saw a slowdown in the amount of commercial real estate mortgages written within our market area. Capitalization rates, which were reaching precariously low levels, began to normalize—perhaps as a result of heightened scrutiny of banking regulators that began heating up in 2015, as we noted a break in the quantity of multi-family properties refinanced.



*Douglas C. Manditch, Chairman & Chief Executive Officer (left)
with Thomas M. Buonaio, President & Chief Operating Officer*

Competition for these loans changed as some financial institutions took a more measured approach in financing these deals. Pricing improved slightly and we observed a return toward more sensible structuring of these credits. Our risk monitoring process of commercial real estate loans is comprehensive. Concentration thresholds are strictly monitored, and the loan portfolio is regularly stress tested. Recent evidence suggests a slight move toward a renter's market in Manhattan and Brooklyn. Landlords, in some cases, are offering concessions to draw renters, and vacancy rates on luxury style apartments have increased, primarily due to new construction coming to market and the time it takes to absorb it. In regard to commercial real estate originations, including multi-family properties, we look for reasonable projects with non-speculative business purposes. We keep a close watch on rental trends, maintain a clear understanding of our borrowers, and stay within our comfortable space in the market. We avoid the luxury market, watching from the sidelines as production causes supply to outpace demand initially.

While maintaining conservative underwriting standards we grew the loan portfolio 7.0% to \$494.3 million from \$461.8 million at December 31, 2015. Preserving future asset credit quality remains our priority. We continued to realign our loan mix to manage credit concentrations. Loan origination volume was high for both years although it was offset by loan satisfactions and pay downs. Recorded provision for loan losses was \$632 thousand for the year ended December 31, 2016 as compared to \$867 thousand recorded for the previous fiscal year. Our allowance for loan and lease losses as of year-end was 1.17% of total loans. Our loan default rates remain low with a ratio of non-performing loans to total loans of 0.48%. The slight uptick in non-performing loans is attributable to loans in Nassau and Suffolk Counties and not attributable to our multi-family portfolio. Loans are considered non-performing based on management's assessment of the borrower's ability to make contractually agreed upon payments under the terms of original agreement.

Under such circumstances of default, we strive to work with the borrower to minimize the strain and monetary loss for all parties.

The net interest margin was adversely impacted by the cost of subordinated debentures issued in December 2015 at the holding company level. To expand our interest earning assets we added investment securities, representing a greater percentage of the earning asset mix in 2016 as compared to the prior year. The increase in investment securities was funded by significant growth in deposits, primarily public funds. Using these public funds to manage our deposit pricing and mix, we reduced our average cost of funds on deposits for 2016 as compared to 2015. Our loan to deposit ratio leaves room for additional assets to be deployed into loans. Although we have seen the Federal Reserve Bank raise short term interest rates twice prior to year end, there is yet to be a notable increase in deposit costs within our market. As we enter a rising rate environment managing sensitivity to interest rate risk will include corresponding adjustments to our balance sheet mix. We expect two or three rate increases from the Federal Reserve in 2017, the first of which already occurred in March 2017.

After raising capital in the form of a subordinated debt offering in 2015, we chose to keep a portion of the proceeds at the parent. We remain "well capitalized" by regulatory standards, and our earnings are trending upward. Our bank regulatory ratios are strong with the Tier One leverage capital ratio over ten percent at year end. We are cautiously optimistic about the changes in Washington D.C. that may lead to an easing of the overbearing regulations that weigh down our organization as well as all community banks throughout the nation. An overhaul of the Dodd Frank requirements may reduce the tremendous amount of unnecessary paperwork in the industry. Regulations in the last three years increased exponentially, and the bulk of the oversight requirements directly impact our customer base. For 2016 we estimate we spent close to \$3.1 million on our costs for compliance due to

regulation, an increase from an estimated \$2.7 million in 2015, and \$2.5 million in 2014. As a percentage of total revenue, the expense totaled 12% in both 2016 and 2015. A decrease in the corporate tax rate would defer a portion of these costs allowing us to redeploy resources into cultivating our core business.

By continuing to enhance our products and services, we are optimizing the customer experience. Our excellent reputation for customer service is further complemented by our commitment to offering electronic products and services that make banking easier and more convenient for our customers. Millennials also demand banking on their own terms, forcing the industry to constantly improve its delivery methods. Everyday banking service revolves around the user experience – both in person and through electronic channels. We are pleased to announce that mobile remote deposit capture for businesses and person to person payments (P2P) for consumers are now available for our customers. We also recently implemented lockbox services, not a new innovation but one important to many commercial and municipal customers.

Cybersecurity remains at the forefront of concern for all companies but especially for financial institutions. Over the past two years email attacks alone have surged as the attackers became more sophisticated, targeted and proficient. The attacks come in many forms, including malware, phishing and ransomware. As a Company, we are obligated to keep our customer data safe by earmarking the appropriate human and financial resources to this ongoing effort.

Our service culture remains the cornerstone of our corporate culture. Over the past year we watched with incredulity as a bigger, and more powerful, competitor was caught in a web of deceiving customers to meet sales goals. Our Company strives to develop its people into well rounded bankers, professionals that can meet the needs of our customers while maintaining honesty and integrity. We are proud of our leaders, managers, officers and staff who are skilled, educated and eager to please.

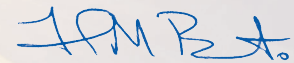
The stock market as a whole benefited from the “Trump Bump” since the election. Across our nation investors are reacting with confidence to the current administration’s agenda, one which speaks to reversing government regulation with the intent to make it easier for businesses to operate in our country. It is our hope that the Congress will come together and work towards legislation based on compromise in an effort to ease regulation; create a thriving economy; invest in the military to protect our nation; as well as address the needs of the middle class which has been struggling for so long. So far in the first three months of 2017 that seems to be a naïve hope. It seems to us, more than ever, that term limits for Congress may be the only way to get our elected officials to understand that they work for all of us and not for individual segments of our citizens. Term limits will allow for a faster turnover of lawmakers so new ideas and less acrimony could exist bringing fresh leadership while eliminating lifelong agendas which hurt our nation.

Once again, on behalf of our Board of Directors and management team, we close by thanking our shareholders, employees and other stakeholders for their support and dedication to our success. We look forward to seeing you at our shareholder meeting on May 18, 2017, being held at the Hyatt Regency Long Island, 1717 Motor Parkway, Hauppauge, New York.

God bless the United States of America.



Douglas C. Manditch
Chairman and Chief Executive Officer



Thomas M. Buonaiuto
President and Chief Operating Officer



FORWARD LOOKING STATEMENTS

This Annual Report contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and 21E of the Securities Exchange Act of 1934. These forward-looking statements include statements that reflect the current views of our senior management with respect to our financial performance and future events with respect to our business and the banking industry in general. These statements are often, but not always, made through the use of words or phrases such as “may,” “should,” “could,” “predict,” “potential,” “believe,” “will likely result,” “expect,” “will continue,” “anticipate,” “seek,” “estimate,” “intend,” “plan,” “projection,” “would” and “outlook,” and similar expressions of a future or forward-looking nature. These statements involve estimates, assumptions, risks and uncertainties. Accordingly, there are or will be important factors that could cause our actual results to differ materially from those indicated in these statements.

We believe that these factors include, but are not limited to the following: our ability to successfully implement our growth strategy; the accuracy of the assumptions underlying the elements of our growth strategy; changes in the strength of the United States economy in general, as well as the economy in our local market areas, and the corresponding impact of those changes on the ability of our customers to transact business with us on profitable terms, including the ability of our borrowers to repay their loans according to their terms or the sufficiency of any related collateral; changes in interest rates and market prices and the corresponding impact of those changes on our net interest margin, asset valuations and expense expectations; changes in the levels of loan prepayments and the resulting effects on the value of our loan portfolio; increased competition for deposits and loans adversely affecting rates and terms; our ability to adequately measure and monitor the credit risk inherent in our loan and securities portfolios; the failure of assumptions underlying our allowance for credit losses; a determination or downgrade in the credit quality and credit agency ratings of the securities in our securities portfolio; increased asset levels and changes in the composition of assets and the resulting impact on our capital levels and regulatory capital ratios; changes in the availability of funds resulting in increased costs or reduced liquidity; the loss of senior management or operating personnel and the potential inability to hire qualified personnel at reasonable compensation levels; our ability to adequately manage the risks associated with technology and security; our ability to access capital markets on acceptable terms as necessary to support the continued growth and safety and soundness of our organization; legislative or regulatory developments, including changes in laws and regulations concerning taxes, banking, securities, insurance and other aspects of the financial securities industry, such as the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”), and the extensive rule making undertaken by various regulatory agencies under the Dodd-Frank Act; further government intervention in the U.S. financial system; changes in statutes and government regulations or their interpretations applicable to us, including changes in tax requirements and tax rates; acts of terrorism, an outbreak of hostilities or other international or domestic calamities, weather or other acts of God and other matters beyond our control; and other risks and uncertainties listed from time to time in our reports and documents filed with the Office of the Comptroller of the Currency (“OCC”).

The foregoing factors should not be construed as exhaustive and should be read together with the other cautionary statements included in this Annual Report. If one or more events related to these or other risks or uncertainties materialize, or if our underlying assumptions prove to be incorrect, actual results may differ materially from what we anticipate. Accordingly, you should not place undue reliance on any such forward-looking statements. Any forward-looking statement speaks only as of the date on which it is made, and we do not undertake any obligation to update any forward-looking statement to reflect events or circumstances after the date on which the statement is made or to reflect the occurrence of unanticipated events. New factors emerge from time to time, and we cannot predict all such factors. In addition, we cannot assess the impact of each factor on our business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements.

Unless we state otherwise or the context otherwise requires, references in this management’s discussion and analysis to “we,” “our” and “us” are to Empire Bancorp, Inc. and Empire National Bank, on a consolidated basis, and references to “Bank” or “the bank” are to Empire National Bank, on a bank-only basis.

SELECTED HISTORICAL FINANCIAL INFORMATION

The following table sets forth selected historical financial and operating data regarding our organization. As the holding company reorganization was completed on August 22, 2013, the historical financial information for 2012 is presented on a bank-only basis, while 2013 through 2016 information is presented on a consolidated basis. You should review this information together with the discussion that follows and the audited financial statements and related notes included elsewhere in this Annual Report. Substantially all average balances were computed based on daily balances. Our historical results may not be indicative of our future performance. All dollars are in thousands, except per share data.

	As of and for the year ended December 31,				
	2016	2015	2014	2013	2012
Income Statement Data:					
Interest income	\$ 24,868	\$ 21,504	\$ 18,540	\$ 16,216	\$ 15,696
Interest expense	3,301	1,689	1,677	1,779	2,268
Net interest income	21,567	19,815	16,863	14,437	13,428
Provision for loan losses	632	867	243	-	285
Net interest income after provision	20,935	18,948	16,620	14,437	13,143
Other income	1,477	1,005	1,033	898	1,941
Other expense	18,068	15,998	13,825	13,054	12,532
Income before income taxes	4,344	3,955	3,828	2,281	2,552
Income tax expense (benefit)	1,554	1,421	1,984	995	(1,072)
Net income	2,790	\$ 2,534	\$ 1,844	\$ 1,286	\$ 3,624
Period-End Balance Sheet Data:					
Investment securities, available-for-sale	\$ 264,734	\$ 151,043	\$ 100,617	\$ 152,639	\$ 180,202
Loans, net of allowance for loan losses	488,475	456,512	375,199	290,227	239,211
Allowance for loan losses	5,799	5,268	4,453	4,244	4,476
Total assets	781,435	629,133	508,069	467,068	438,399
Noninterest-bearing deposits	177,299	189,200	189,204	177,252	172,165
Interest-bearing deposits	493,384	328,833	205,921	213,679	191,193
Stockholders' equity	62,992	64,154	62,421	38,460	42,216
Per Share Data:					
Diluted earnings	\$ 0.40	\$ 0.37	\$ 0.41	\$ 0.29	\$ 0.83
Basic earnings	0.40	0.42	0.42	0.29	0.83
Book value, as converted ⁽¹⁾	9.07	9.32	9.07	8.78	9.64
Performance Ratios:					
Return on average equity	4.19 %	3.98 %	4.43 %	3.19 %	8.90 %
Return on average assets	0.39	0.47	0.38	0.29	0.90
Net interest margin	3.05	3.75	3.55	3.29	3.48
Efficiency ratio ⁽²⁾	79.60	76.58	77.37	84.31	89.30
Asset Quality Ratios:					
Nonperforming assets to total assets ⁽³⁾	0.30 %	0.09 %	0.23 %	0.51 %	0.61 %
Nonperforming loans to total loans ⁽³⁾	0.48	0.12	0.31	0.81	1.09
Allowance for loan losses to total loans	1.17	1.14	1.17	1.44	1.84
Net charge-offs to average loans	0.02	0.03	0.01	0.08	0.01
Capital Ratios (bank level only)⁽⁴⁾:					
Tier 1 leverage capital	10.22 %	12.22 %	12.65 %	9.01 %	9.52 %
Common equity tier 1 risk-based capital	16.26	16.83	-	-	-
Tier 1 risk-based capital	16.26	16.83	16.02	12.78	14.65
Total risk-based capital	17.46	18.01	17.17	14.03	15.90

(1) For the year ended December 31, 2014, book value, as converted, treats the Series A preferred stock as having been converted into common stock because it has been structured as a nonvoting common stock equivalent.

(2) Efficiency ratio is the ratio of noninterest expense to net interest income and noninterest income.

(3) For the periods presented, nonperforming assets consist solely of nonperforming loans and nonperforming loans consist solely of nonaccrual loans.

(4) Capital ratios at December 31, 2016 and 2015 are calculated under Basel III guidelines.

OUR BUSINESS

Overview

We are a bank holding company, headquartered in Islandia, New York, which offers a broad range of financial services through our wholly-owned banking subsidiary, Empire National Bank. Our primary market is the counties of Suffolk, Nassau, Kings, Queens, Bronx and New York in the State of New York, which we serve from our main office located at 1707 Veterans Highway, Islandia, New York, three branch offices located in Shirley, Port Jefferson Station and Mineola, New York and a loan and private banking-style branch office located in Manhattan, New York. We believe that our market presents attractive demographic attributes and favorable competitive dynamics, providing long-term growth opportunities for our organization.

We are led by a team of experienced bankers, all of whom have substantial banking experience and relationships on Long Island and throughout New York City. We believe that our management's long-standing presence in the area gives us insight into the local market and, as a result, the ability to tailor our products and services, particularly the structure of our loans, more closely to the needs of our targeted customers. We seek to develop comprehensive, long-term banking relationships by cross-selling loans and core deposits, offering a diverse array of products and services and delivering high quality customer service.

Our operating strategy

Our business model focuses on a traditional, relationship-based, community bank structure guided by the following principles: disciplined risk management; responsive, high-quality service; focus on building long-term relationships; credibility within our communities; and efficiency. We believe our flexible organizational structure, service philosophy, and depth of market knowledge acquired by our management over their banking careers differentiates us from other financial institutions. Our operating strategy focuses on steady, long-term growth and increased profitability.

To execute our business model, we have implemented a number of operating strategies, including:

- Hiring and retaining qualified banking officers with extensive experience in our market;
- Utilizing technology and strategic outsourcing to provide a broad array of secure and convenient products and services in a cost-effective manner;
- Developing a suite of focused products and services tailored for professional practice customers in our market;
- Operating from highly visible and accessible banking offices in close proximity to a concentration of targeted commercial businesses and professionals;
- Expanding our geographic footprint within our primary market through additional branch locations;
- Providing individualized attention with consistent, prompt local decision-making authority; and
- Leveraging the diverse community involvement, client referrals and professional expertise of our directors and officers.

Our competitive strengths

We believe that we are well-positioned to create value for our shareholders, particularly as a result of the following competitive strengths:

Each member of our senior management team has experience at growing financial institutions in the New York metropolitan area.

Cohesive core management team with extensive local banking experience. Our executive and senior management team is comprised of seasoned local bankers. For many in this group, their entrepreneurial skills steered them to our organization, attracted to the opportunity to grow and develop a de novo start up national bank. Several of them started before, or shortly after, the official opening of our bank in February 2008 while others joined as our growth demanded more leaders with different proficiencies. Our entire senior management team has experience in all facets of banking having worked at various other financial institutions that were mostly located in our market area on and around Long Island and in New York City. Their areas of expertise include strategic and tactical planning, capital management, commercial and industrial lending, real estate lending and consumer lending, as well as accounting and finance, branch and back office operations, financial technology, business development, municipal banking, human resources, risk management and regulatory compliance.

Stable and scalable platform. Throughout our operating history, we have maintained a stable banking platform with strong capital levels and sound asset quality. Because we have total consolidated assets of less than \$1 billion, our regulatory capital levels are evaluated on a bank-only basis. At December 31, 2016, the Bank had a 10.22% tier 1 leverage capital ratio, a 16.26% common equity tier 1 risk-based capital ratio, a 16.26% tier 1 risk-based capital ratio and a 17.46% total risk-based capital ratio. Contributing to our stability is our track record of sound asset quality. Our highest annual rate of net loan charge-offs to average loans over the past five years was 0.08%, or \$232 thousand, in 2013, and our average annual rate of net loan charge-offs to average loans over the same period was 0.03%. Utilizing the prior experience of our management team at larger banks operating within our primary market, we believe that we have built a scalable corporate infrastructure, including technology and banking processes, capable of supporting continued growth, while improving operational efficiencies. We enhanced our capital strength during the fourth quarter of 2014 when we completed a private placement of our capital stock, generating \$18.7 million in net proceeds. We believe that our strong capital and asset quality levels will allow us to grow and that our operating platform will allow us to manage that growth effectively, resulting in greater efficiency and improved profitability.

Growing deposit base. A significant driver of our franchise is the growth and stability of our deposits, which we use to fund our loans and investment portfolio. At December 31, 2016, our total deposits were \$670.7 million, representing a compounded annual growth rate of 18.4% since December 31, 2012. Our deposit growth has been driven significantly by the growth in our savings, N.O.W. and money market deposits primarily from new municipal banking relationships. Savings, N.O.W. and money market deposits represented approximately 69.5% of our total deposits at December 31, 2016, up from 35.6% of our total deposits at December 31, 2012. Active solicitation of municipal deposits over the past two years significantly contributed to total deposit growth. The shift in deposit mix over this period resulted in lowering the average cost of our deposit liability. We seek to cross-sell deposit products at loan origination, which provide a basis for expanding our banking relationships and a stable source of funding.

Our challenges

In implementing our business model, we have faced, and expect to continue to face, a number of challenges that could impact our financial condition, operating results and prospects in future periods. We believe that the most consequential risks to our business include the following:

- Our business is concentrated on Long Island and in certain boroughs of New York City, and we are more sensitive than our more geographically diversified competitors to adverse changes in the local economy;
- We face significant competition to attract and retain customers;

- We operate in a highly regulated environment, which could restrain our growth and profitability;
- We depend heavily on our information technology and telecommunications systems, which are subject to systems failures, interruptions and security risks;
- We may not be able to adequately measure and limit our credit risk, which could impact our profitability; and
- Our profitability largely depends on our ability to manage our assets and liabilities during periods of changing interest rates. Accordingly, the fair value of our investment securities can fluctuate due to factors outside of our control.

Our market

Our primary market is the counties of Suffolk County and Nassau County, New York, although we also conduct significant business in the counties of Kings, Queens, Bronx and New York in the State of New York. The economy of our markets reflects a diverse cross section of employment sectors, with a mix of services; wholesale/retail trade; federal, state and local government; healthcare; banking and education.

Our primary market is diverse, in terms of educational attainment, income level and ethnic background. According to data provided by the U.S. Census Bureau, the population of Suffolk County was approximately 1,501,587 residents as of July 1, 2015, which represents a 0.5% increase in population since April 1, 2010. Similarly, the population of Nassau County was approximately 1,361,350 residents as of July 1, 2015, which represents a 1.6% increase in population since April 1, 2010. This population growth has attracted businesses to the area and led to growth in the local service economy, and, while it is not certain, we expect that this trend will continue. In addition, as of 2015, the median household incomes in Suffolk County and Nassau County were \$88,663 and \$99,465, compared to a New York state household income median of \$53,373. Further, according to data provided by the FDIC, between June 30, 2010 and June 30, 2016, FDIC-insured deposits in Suffolk County and Nassau County have increased by approximately 51.8% and 28.5%, respectively. We believe that our primary market area presents attractive growth opportunities with a diversified and growing customer base. As a community bank, we are focused on serving the needs of the small-and medium-sized businesses, professionals, nonprofit organizations, municipalities, real estate investors and consumers.

We compete with a wide range of financial institutions in our market, including local, regional and national commercial banks, thrifts and credit unions. Consolidation activity involving financial institutions based outside of Long Island has altered the competitive landscape in our market within recent years. As of June 30, 2016, less than 30% of the deposits in Suffolk and Nassau counties were held in banks that were based on Long Island, due in large part to the acquisitions of locally-based financial institutions by larger banks based outside of our primary market area. Although competition within our market area is strong, we believe that the customer disruption associated with these acquisitions, as well as the loss of in-market decision-making and relationship-based banking, will continue to provide us with additional growth opportunities. We also compete with mortgage companies, investment banking firms, brokerage houses, mutual fund managers, investment advisors, and other “non-bank” companies for certain of our products and services. Some of our competitors are not subject to the degree of supervision and regulatory restrictions that we are.

Interest rates, both on loans and deposits, and prices on fee-based services are significant competitive factors among financial institutions generally. Many of our competitors are much larger financial institutions that have greater financial resources than we do and that compete aggressively for market share. These competitors attempt to gain market share through their financial product mix, pricing strategies and banking center locations. Due to the benefits of scale, our larger regional and national bank competitors can, in many cases; offer pricing that is more attractive than that which we can offer, although this pricing has historically been reserved for customers of a size for which we generally would not compete. Other important competitive factors in our market area include office locations and hours, quality of customer service, community reputation, continuity of personnel and services, capacity and willingness to extend credit, and ability to offer sophisticated cash management and other commercial banking services. Many of our competitors are organized along lines of business and use efficient but impersonal

approaches to providing products and services to customers. While we seek to be competitive with respect to rates, we believe that we compete most successfully on the basis of our service and relationship-based culture.

Loans

General. Lending has the highest priority for our asset utilization. Our primary lending focus is to serve small and medium-sized businesses, professionals, nonprofit organizations, and other organizations in our primary market with a variety of financial products and services, while maintaining strong and disciplined credit policies and procedures. We offer a full array of commercial and consumer lending products to serve the needs of our customers. Commercial lending products include commercial real estate loans, multi-family loans, real estate construction and development loans and general commercial loans (such as business term loans, equipment financing and lines of credit). Consumer lending products include home equity loans, lines of credit and consumer installment loans, such as loans to purchase cars, boats and other recreational vehicles. We do not engage in a material amount of consumer lending, which is offered primarily as an accommodation to our commercial customers and their executives and employees. In addition, our lending policies do not provide for any loans that are highly speculative, sub-prime, or that have high loan-to-value ratios.

We market our lending products and services to qualified borrowers through conveniently located banking offices, relationship networks and high touch personal service. Our relationship managers actively target long-standing businesses operating in the communities we serve. We seek to attract new lending customers through professional service, relationship networks and competitive pricing.

Commercial real estate loans. We offer real estate loans for commercial property that is owner-occupied as well as commercial property owned by real estate investors. Commercial real estate loan terms generally are limited to ten to twenty years or less, although payments may be structured on a longer amortization basis. The interest rates on our commercial real estate loans may be fixed or adjustable, although rates typically are not fixed for a period exceeding five to ten years. We generally charge a documentation or loan processing fee for our services. With the exception of our multi-family lending, which is generally non-recourse, we require personal guarantees from the principal owners of the business supported by a review of the principal owners' personal financial statements. We may not require personal guarantees when lending to not-for-profit entities, religious organizations, condominium associations, financial institutions and municipal entities. We make efforts to limit our risks with respect to commercial real estate loans by analyzing borrowers' cash flow and collateral value. The real estate securing our existing commercial real estate loans includes a wide variety of property types, such as offices/warehouses/production facilities, office buildings, hotels, mixed-use residential/commercial, retail centers and multi-family properties.

Construction loans. We finance the construction of owner occupied and income producing properties. Construction financing generally requires preapproved permanent financing, unless made on a speculative basis. Construction and development loans are generally made with a term of one to two years and interest is paid monthly. The ratio of the loan principal to the value of the collateral, as established by independent appraisal, typically will not exceed industry standards. Any speculative loans are based on the borrower's financial strength and ability to generate cash flow. Loan proceeds are disbursed based on the percentage of completion and only after the project has been inspected by an experienced construction lender or third-party inspector.

Commercial loans. We offer a wide range of commercial loans, including business term loans, equipment financing and lines of credit. Our target commercial loan market is professional establishments and small to medium-sized businesses. The terms of these loans vary by purpose and by type of underlying collateral, if any. Our commercial loans primarily are underwritten on the basis of the borrower's ability to service the loan from cash flow. We make equipment loans with conservative margins generally for a term of five years or less at fixed or variable rates, with the loan fully amortizing over the term. Loans to support working capital typically have terms not exceeding one year and usually are secured by accounts receivable, inventory and personal guarantees of the principals of the business. For loans secured by accounts receivable or inventory, principal typically is repaid as the assets securing the loan are converted into cash, and for loans secured with other types of collateral, principal amortizes over the term of the loan. The quality of the commercial borrower's management and its ability both to properly evaluate changes in the supply and demand characteristics affecting its markets for products and services and to effectively respond to such changes are significant factors in a commercial borrower's creditworthiness. Although most loans

are made on a secured basis, loans may be made on an unsecured basis where warranted by the overall financial condition of the borrower.

Consumer loans. We make a variety of loans to individuals for personal purposes, including secured and unsecured installment loans and home equity lines of credit. The amortization of second mortgages generally does not exceed fifteen years and the rates generally are not fixed for over twelve months. Consumer loans secured by depreciable assets, such as boats, cars and trailers, are typically amortized over the useful life of the asset. We review the borrower's past credit history, past income level, debt history and, when applicable, cash flow and evaluate the impact of all these factors on the ability of the borrower to make future payments as agreed.

Investments

In addition to our lending activities, we purchase investment securities that are principally either direct debt obligations of the United States Treasury or one of the agencies of the United States government. We may also invest in mortgage-backed securities issued by the Government National Mortgage Association, the Federal National Mortgage Association, the Federal Home Loan Mortgage Corporation, the Federal Home Loan Bank and the Federal Farm Credit Bureau. Each of these issuer's securities are backed by mortgages conforming to its underwriting guidelines and each issuer guarantees the timely payment of principal and interest on its securities. Our approved policies also allow for investment in both tax exempt and taxable municipal securities, corporate securities and certain equity securities as might be required to deal with various government agencies or banking associations. We regularly evaluate the composition of this category as changes occur with respect to the interest rate yield curve. Overall investment goals are established by the Bank's Investment Committee, which reviews the investment portfolio on a periodic basis, and monitors and makes adjustments as necessary based upon current market interest rates and the economic environment, as well as our established policies and strategies. The Bank's investment strategies seek to maximize long-term investment earnings through managing securities gains and losses as well as interest income. Day-to-day activities pertaining to the investment portfolio are conducted under the supervision of the Bank's President and Chief Operating Officer.

Deposits

Deposits are our primary source of funds to support our earning assets. We offer traditional depository products, including checking, savings, money market and certificates of deposit with a variety of rates. Deposit products are structured to be competitive with rates, fees, and features offered by other local institutions. The primary sources of core deposits are professional practice monies, small to medium-sized businesses and their employees, and consumers located within our primary market. We generate deposits through our business development efforts as well as referrals from our existing customers, officers and directors as well as various marketing campaigns. In 2014, we joined ICS®, an Insured Cash Sweep® service to provide an additional collateral product for our growing public fund deposit base. In 2012, we met the requirements established by the United States Trustee for deposits of bankruptcy funds. In addition, we participate in the Certificate of Deposit Account Registry Service, or CDARS®, which allows us to provide unlimited FDIC insurance for depositors by placing the portion of the deposit in excess of FDIC insurance limits with other FDIC-insured institutions that are members of the CDARS® network.

Supervision and regulation

We are subject to extensive regulation and supervision that govern almost all aspects of our operations at the holding company and bank levels. We are regulated by the Federal Reserve at the holding company level and by the Office of the Comptroller of the Currency at the bank level. Banking laws, regulations and policies, and the supervisory framework that oversees their administration, are primarily intended to protect consumers, depositors, the Deposit Insurance Fund and the banking system as a whole, and not shareholders and counterparties. In addition, these laws, regulations and policies are subject to continual review by governmental authorities, and changes to these laws, regulations and policies, including changes in their interpretation or implementation, or the adoption of new laws, regulations or policies, can affect us in substantial and unpredictable ways.

In the aftermath of the most recent recession, new legislation has been enacted, and new regulations promulgated, that were designed to strengthen the financial system as a whole. These laws and regulations have imposed significant additional costs on all financial institutions and impacted the banking industry in numerous other ways.

A number of the most significant changes in laws and regulations affecting the banking industry are discussed below. However, the discussion that follows is only a brief summary of certain of these laws and regulations, and there are many other laws and regulations that affect our operations, other than those discussed below.

Dodd-Frank Act

The Dodd-Frank Act, enacted on July 21, 2010, aimed to restore responsibility and accountability to the financial system by significantly altering the regulation of financial institutions and the financial services industry. The Act, among other things: (i) established the Consumer Financial Protection Bureau, an independent organization within the Federal Reserve dedicated to promulgating and enforcing consumer protection laws applicable to all entities offering consumer financial products or services; (ii) established the Financial Stability Oversight Council, tasked with the authority to identify and monitor institutions and systems that pose a systemic risk to the financial system, and to impose standards regarding capital, leverage, liquidity, risk management, and other requirements for financial firms; (iii) changed the base for FDIC insurance assessments; (iv) increased the minimum reserve ratio for the Deposit Insurance Fund from 1.15% to 1.35%; (v) permanently increased federal deposit insurance coverage from \$100,000 to \$250,000; (vi) directed the Federal Reserve to establish interchange fees for debit cards pursuant to a restrictive “reasonable and proportional cost” per transaction standard; (vii) limited the ability of banking organizations to sponsor or invest in private equity and hedge funds and to engage in proprietary trading; (viii) granted the U.S. government authority to liquidate or take emergency measures with respect to troubled nonbank financial companies that fall outside the existing resolution authority of the FDIC; (ix) increased regulation of asset-backed securities; (x) increased regulation of consumer protections regarding mortgage originations, including originator compensation, minimum repayment standards, and prepayment considerations; and (xi) established new disclosure and other requirements relating to executive compensation and corporate governance.

Some of these provisions have the consequence of increasing our expenses, decreasing our revenues, and changing the activities in which we choose to engage. The specific impact on our current activities or new financial activities that we may consider in the future, our financial performance and the markets in which we operate will depend on the manner in which the relevant agencies develop and implement the required rules and the reaction of market participants to these regulatory developments. Many aspects of the Dodd-Frank Act are subject to rulemaking that will take effect over the next several years, making it difficult to anticipate the overall financial impact on the financial industry, in general, and on us.

Regulatory capital requirements

Effective January 1, 2015, we became subject to new rules designed to implement the recommendations with respect to regulatory capital standards, commonly known as Basel III, approved by the International Basel Committee on Banking Supervision. The Basel III framework is applicable to all top tier bank holding companies with consolidated assets of \$1.0 billion or more and all banks, regardless of size. Accordingly, at this time, we are subject to Basel III only at the bank level.

The new Basel III rules establish the following minimum regulatory capital ratios:

- A leverage ratio of 4.0%;
- A new ratio of common equity tier 1 capital to total risk-weighted assets of not less than 4.5%;
- A tier 1 risk-based capital ratio of 6.0% (an increase from 4.0%); and
- A total risk-based capital ratio of 8.0%.

The Basel III rules also changed the regulatory capital requirements for purposes of the prompt corrective action regulations. Accordingly, to be categorized as well capitalized, the bank must have a minimum leverage capital ratio of at least 5.0%, common equity tier 1 capital ratio of at least 6.5%, a tier 1 risk-based capital ratio of at least 8.0%, and a total risk-based capital ratio of at least 10.0%. The rules also implemented a requirement for all banking organizations to maintain a capital conservation buffer above the minimum capital requirements to avoid certain restrictions on capital distributions and discretionary bonus payments to executive officers. The capital

conservation buffer is being phased in over a three year period, beginning January 1, 2019. The capital conservation buffer must be composed of common equity tier 1 capital. The capital conservation buffer requirement will effectively require banking organizations to maintain regulatory capital ratios at least 50 basis points higher than well capitalized levels with respect to the risk-weighted capital measures to avoid the restrictions on capital distributions and discretionary bonus payments to executive officers. In addition, the final rule establishes more conservative standards for including instruments in regulatory capital and imposes certain deductions from and adjustments to the measure of tier 1 capital and tier 2 capital. The final rule alters the method under which banking organizations must calculate risk-weighted assets in an effort to make the calculation of risk-weighted assets more risk-sensitive, to better account for risk mitigation techniques, and to create substitutes for credit ratings (in accordance with the Dodd-Frank Act).

Although management is continuing to evaluate the impact the final rule will have on our organization, we were in compliance with all applicable minimum regulatory capital requirements as of December 31, 2016 and expect to meet all minimum regulatory capital requirements under the final rule, as if fully phased in.

The final Basel III framework also requires banks and bank holding companies to measure their liquidity against specific liquidity tests. However, under the proposed rules, the Basel III liquidity framework applies only to banking organizations with \$250 billion or more in consolidated assets or \$10 billion or more in foreign exposures. As a result, unless modified, the Basel III liquidity framework does not apply to us.

MANAGEMENT'S DISCUSSION OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis presents management's perspective on our financial condition and results of operations on a consolidated basis. However, because we conduct all of our material business operations through Empire National Bank, the discussion and analysis relates to activities primarily conducted at the subsidiary level. The discussion is intended to highlight and supplement other data and information presented elsewhere in this annual report, including our audited consolidated financial statements and the related notes. Please note that the performance related to the prior periods described in this annual report may not be indicative of our future financial performance.

As a bank holding company that operates through one segment, community banking, we generate most of our revenue from interest on loans and investments, service charges and gains on the sale of investment securities. Our primary source of funding for our loans is deposits, and our largest expenses are interest of these deposits and salaries and related employee benefits. We measure our performance through our net income, net interest margin, return on average assets and return on average equity, while maintaining appropriate regulatory leverage and risk-based capital ratios.

Performance summary

Our total assets increased \$152.3 million, or 24.2%, to \$781.4 million as of December 31, 2016, compared to \$629.1 million as of December 31, 2015. Our asset growth was largely driven by loan growth of \$32.5 million, or 7.0% and an increase of \$113.7 million or 75.3% in securities available for sale. Asset quality remained strong, with total nonperforming loans comprising 0.48% of total loans as of December 31, 2016, compared to 0.12% as of December 31, 2015. Total deposits increased \$152.7 million, or 29.5%, to \$670.7 million as of December 31, 2016, compared to \$518.0 million as of December 31, 2015. Our deposit growth was driven primarily by savings, N.O.W. and money market growth of \$179.3 million or 62.5% to \$465.9 million as of December 31, 2016. The growth in these deposits was driven in large part by new and existing municipal banking relationships, which were largely invested in the investment securities portfolio and classified as available for sale. Noninterest-bearing deposits, which represent our lowest cost of funding, decreased \$11.9 million or 6.3% to \$177.3 million as of December 31, 2016, compared to \$189.2 million as of December 31, 2015. The average balance of noninterest-bearing deposits increased minimally from \$191.3 million at December 31, 2015 to \$192.1 million at December 31, 2016. The percentage of noninterest-bearing deposits to total deposits declined from 36.5% to 26.4% due to the growth in savings, N.O.W. and money market accounts, comprised of primarily public fund deposits, outpacing the growth in noninterest-bearing deposits. Short-term borrowings, which represent advances from the Federal Home Loan Bank of New York, increased \$0.4 million from \$26.1 million as of December 31, 2015 to \$26.5 million as of December 31, 2016. Total stockholders' equity decreased \$1.2 million to \$63.0 million as of December 31, 2016, from \$64.2 million as of December 31, 2015. Stockholders' equity was impacted by an increase of \$4.3 million in accumulated other comprehensive loss, partially offset by our operating earnings of \$2.8 million. The increase in accumulated other comprehensive loss was a result of a negative change in the fair value of our securities available for sale, net of applicable taxes.

Net income for the year ended December 31, 2016 was \$2.8 million or \$0.40 per diluted share, compared to net income of \$2.5 million, or \$0.37 per diluted share, in 2015, an increase of \$256 thousand, or 10.1%. The increase in net income during 2016 was positively impacted by an increase in net interest income of \$1.8 million, or 8.8%, to \$21.6 million. Other income increased year over year by \$472 thousand, or 47.0%, to \$1.5 million for year ended December 31, 2016 primarily as a result of the net increase of \$417 thousand for net securities gains/losses. Other expenses increased \$2.1 million, or 12.9%, as compared to the year ended December 31, 2015. The increase in other expense was primarily attributable to an increase in salaries and employee benefits expense of \$1.5 million, or 18.6%, over the previous year, due primarily to the hiring of new employees to support growth and strategic plans as well as the implementation of a recognition and retention plan for key employees. Net occupancy and equipment costs increased \$245 thousand, or 9.5%, over the same period last year, primarily as a result of the increased footprint of the bank's main office lease and the opening of a loan and deposit production office in Manhattan. Costs associated with the collateralization of higher municipal deposits increased \$97 thousand over the same period last year. Advertising and business development expense increased \$191 thousand, or 24.1%, as compared to the same period in 2015 primarily as a result of expanding sponsorships and delivery channels. FDIC insurance

increased \$51 thousand, or 16.9%, during 2016 as compared to same period in 2015, as a direct result of the increase in average assets.

Increases in non-interest expenses year over year were the principal reason for the efficiency ratio increase to 79.60% from 76.58% from the year ended December 31, 2015. Basic and diluted earnings per share for the year ended December 31, 2016 were \$0.40, compared to \$0.42 and \$0.37, respectively, for 2015. Our return on average assets was 0.39% for 2016, as compared to 0.47% for 2015, and our return on average equity was 4.19% for 2016, as compared to 3.98% for 2015.

Comparison of operating results for the years ended December 31, 2016 and 2015

Analysis of net interest income

Net interest income, the primary contributor to our earnings, represents the difference between the income that we earn on our interest-earning assets and the cost to us of our interest-bearing liabilities. Our net interest income depends upon the volume of interest-earning assets and interest-bearing liabilities and the interest rates that we earn or pay on them.

The following table presents, for the periods indicated, the average balances of our interest-earning assets and interest-bearing liabilities, average yields and costs, and certain other information. Nonaccrual loans are included in loans, and interest on nonaccrual loans is included only to the extent reflected in the consolidated statements of income.

	Year Ended December 31,					
	2016			2015		
	Average Balance	Interest Earned/Paid	Average Yield/Cost	Average Balance	Interest Earned/Paid	Average Yield/Cost
	(dollars in thousands)					
Interest earning assets:						
Loans (including fee income) ⁽¹⁾	\$ 470,380	\$ 20,275	4.31 %	\$ 408,794	\$ 19,012	4.65 %
Securities, taxable ⁽²⁾	227,689	4,545	2.00	110,547	2,468	2.23
Deposits with banks	9,014	48	0.53	9,284	24	0.26
Federal funds sold	80	-	-	5	-	-
Total interest-earning assets	707,163	24,868	3.52	528,630	21,504	4.07
Non interest-earning assets:						
Cash and due from banks	7,826			7,511		
Other assets	6,735			6,131		
Total assets	\$ 721,724			\$ 542,272		
Interest bearing liabilities:						
Savings, N.O.W. and money market deposits	\$ 394,230	\$ 1,740	0.44%	\$ 207,410	\$ 992	0.48%
Certificates of deposit of \$100,000 or more	27,741	290	1.05	40,471	375	0.93
Other time deposits	10,079	118	1.17	15,121	203	1.34
Subordinated debentures	14,717	1,092	7.42	611	46	7.53
Borrowed funds	9,420	61	0.65	18,888	73	0.39
Total interest-bearing liabilities	456,187	3,301	0.72	282,501	1,689	0.60
Non interest-bearing liabilities:						
Demand deposits	192,121			191,265		
Other liabilities	6,866			4,806		
Total liabilities	655,174			478,572		
Stockholders' equity	66,550			63,700		
Total liabilities and stockholders' equity	\$ 721,724			\$ 542,272		
Net interest income		\$ 21,567			\$ 19,815	
Net interest spread ⁽³⁾			2.80 %			3.47 %
Net interest earning assets	\$ 250,976			\$ 246,129		
Net interest margin ⁽⁴⁾			3.05 %			3.75 %

(1) Amounts are net of deferred origination costs/(fees) and the allowance for loan loss.

(2) Unrealized gains / (losses) on securities available for sale are included in other assets.

(3) Net interest spread is the weighted average yield on interest-earning assets minus the weighted average rate on interest-bearing liabilities.

(4) Net interest margin is net interest income divided by average interest-earning assets.

Net interest income increased \$1.8 million, or 8.8%, for the year ended December 31, 2016 over the prior year. Interest from loans and securities available for sale were primarily responsible for the growth in total interest income while the cost of the subordinated debentures and savings, N.O.W., and money market deposits made up the growth of total interest expense. Net interest margin was 3.05% for 2016, a decrease from 3.75% from the year ended December 31, 2015. The decrease in net interest margin was primarily attributable to a decrease of 55 basis points in our yield on average earning assets for 2016, driven largely by two factors. First, the average yield on loans decreased to 4.31% for 2016 from 4.65% for 2015, primarily due to loan prepayment fees being materially lower in 2016, as the significant refinancing activity that occurred in 2015 slowed in 2016. Second, we shifted the mix of our asset composition in 2016. The average balance of investment securities, a lower yielding investment than loans, increased to \$227.7 million for the year ended December 31, 2016 or 106.0% from the prior year. Consequently, for year ended December 31, 2016, average loans represented 66.5% of our average interest-earning assets as compared to 77.3% for the year ended December 31, 2015. For the year ended December 31, 2016 average investment securities represented 32.2% of average earning assets as compared to 20.9% for the year ended December 31, 2015. Notwithstanding the decrease in the yield on average earning assets for 2016, total interest income for 2016 increased \$3.4 million over the same period in 2015, as a result of the increase of average earning assets by \$178.5 million, or 33.8%.

The decrease in net interest margin also was impacted by an increase of 12 basis points in the cost of average interest-bearing liabilities to 0.72% for the year ended December 31, 2016 from 0.60% for the prior year. This increase was primarily attributable to the issuance of subordinated debentures in December of 2015 at the holding company level with a weighted average cost of 7.42%. Interest expense on the subordinated debentures totaled \$1.1 million for year ended December 31, 2016 as compared to \$46 thousand for the prior year. While the average cost of savings, N.O.W. and money market deposits decreased to 0.44% for 2016 from 0.48% for the same period in 2015, the increase in the average volume of these accounts was the primary driver in the increase in interest expense by \$748 thousand year over year. Average savings, N.O.W. and money market deposits increased 90.1% to \$394.2 million over the prior year average, reflecting the large increase in public funds. The average balance of noninterest-bearing demand deposits for the year ended December 31, 2016 remained relatively flat when compared to the prior year average balance.

Rate/volume analysis

The following table analyzes the dollar amount of changes in interest income and interest expense for the primary components of interest-earning assets and interest-bearing liabilities. The table shows the amount of the change in interest income or expense caused by either changes in outstanding balances (volume) or changes in interest rates. The effect of a change in volume is measured by applying the average rate during the first period to the volume change between the two periods. The effect of changes in rate is measured by applying the change in rate between the two periods to the average volume during the first period. Changes attributable to both rate and volume that cannot be segregated have been allocated proportionately to the absolute value of the change due to volume and the change due to rate.

	Year Ended December 31, 2016 Over 2015		
	Increase/(Decrease) Due To		
	Average Volume	Average Rate	Net Change
		(in thousands)	
Interest income on interest-earning assets:			
Loans (including fee income)	\$ 2,723	\$ (1,460)	\$ 1,263
Securities, taxable	2,302	(225)	2,077
Deposits with banks	(1)	25	24
Total increase (decrease) in interest income	<u>5,024</u>	<u>(1,660)</u>	<u>3,364</u>
Interest expense on interest-bearing liabilities:			
Savings, N.O.W. and money market deposits	830	(82)	748
Certificates of deposit of \$100,000 or more	(129)	44	(85)
Other time deposits	(61)	(24)	(85)
Borrowed money	(47)	35	(12)
Subordinated debentures	1,047	(1)	1,046
Total increase (decrease) in interest expense	<u>1,640</u>	<u>(28)</u>	<u>1,612</u>
Total increase (decrease) in net interest income	<u>\$ 3,384</u>	<u>\$ (1,632)</u>	<u>\$ 1,752</u>

Provision for loan losses

We consider a number of factors in determining the required level of our allowance for loan losses and the provision required to achieve that level, including loan growth, loan quality rating trends, nonperforming loan levels, delinquencies, net charge-offs, industry concentrations and economic trends in our market and throughout the nation. We recorded a \$632 thousand provision for loan losses for the year ended December 31, 2016 and an \$867 thousand provision for loan losses for the year ended December 31, 2015.

Other income

Total other income, which was comprised of customer-related fees and service charges, net securities gains/losses and other operating income, increased \$472 thousand for the year ended December 31, 2016, as compared to the same period in 2015, primarily as a result of the net increase of \$417 thousand in net securities gains/losses. We experienced a decrease in customer-related fees and service charges of \$10 thousand, as well as an increase in other operating income of \$42 thousand, which were associated with miscellaneous service charges and fees that include revenues such as electronic funds transfer fees, assignment fees on loans, and wire transfer fees.

Other expense

Our other expense consists primarily of salary and employee benefits, occupancy and other expenses related to our operation and expansion. Other operating expenses also reflect both New York State and New York City capital based taxes, which were enacted in 2015. Other expense increased by approximately \$2.1 million, or 12.9%, during 2016, as compared to 2015, primarily from expenses associated with our continued growth. The biggest component of the growth in other expense was salaries and benefits, which increased \$1.5 million, or 18.6%, during 2016, largely due to base salary, short term incentive and long-term incentive increases, new employees hired to support growth and branch expansion and an increase in employee benefit costs. Assets per employee increased to \$10.9 million as of December 31, 2016 from \$8.7 million as of December 31, 2015. Net occupancy and equipment costs increased \$245 thousand, or 9.5%, primarily resulting from the expenses associated with the expansion of office space in the Bank's main office and the opening of a loan and deposit production office in Manhattan. As a result of our continual growth, advertising and business development increased \$191 thousand or 24.1%; FDIC insurance expense increased \$51 thousand or 16.9% and costs associated with the collateralization of municipal deposits increased \$97 thousand over the same period last year.

Provision for income taxes

Income tax expense for the year ended December 31, 2016 was approximately \$1.6 million, as compared to \$1.4 million for the year ended December 31, 2015. For years ended December 31, 2016 and 2015, we were subject to New York State and New York City capital taxes. Because of legislation enacted in 2014 and 2015, we do not expect to be in a taxable income position for the foreseeable future in New York State and New York City. As a result, we determined that it was not more likely than not that we would be able to utilize state and city deferred tax assets. Accordingly, we maintain a valuation allowance against all state and city deferred tax assets. We believe that the revisions to the New York State and New York City corporate income tax laws will continue to decrease our future state and local income tax liability. Our combined effective tax rate for 2016 and 2015 was 35.8% and 35.9%, respectively.

Financial condition

Our total assets increased \$152.3 million, or 24.2%, to \$781.4 million as of December 31, 2016, compared to \$629.1 million as of December 31, 2015. Net loans increased \$32.0 million, or 7.0%, to \$488.5 million as of December 31, 2016, compared to \$456.5 million as of December 31, 2015. As a result of management's assessment of the credit quality of the loan portfolio, the allowance for loan losses to total loans was 1.17%, or \$5.8 million, at December 31, 2016 as compared to 1.14%, or \$5.3 million, as of December 31, 2015. Securities available for sale increased \$113.7 million, or 75.3%, to \$264.7 million as of December 31, 2016, from \$151.0 million as of December 31, 2015.

Our asset growth for the year ended December 31, 2016 was funded primarily by deposit growth. Total deposits increased \$152.7 million, or 29.5%, to \$670.7 million as of December 31, 2016, compared to \$518.0 million as of December 31, 2015. Demand deposits, which represent a value funding source, decreased \$11.9 million or 6.3% to \$177.3 million as of December 31, 2016, compared to \$189.2 million as of December 31, 2015. The average balance of these noninterest-bearing deposits remained relatively flat. Savings, N.O.W. and money market deposits increased \$179.3 million, or 62.6%, to \$465.9 million as of December 31, 2016. The growth in these deposits was driven in large part by new and existing municipal banking relationships. Certificates of deposit of \$100,000 or more decreased \$13.7 million, or 43.1%, to \$18.1 million while other time deposits decreased by \$1.0 million, or 9.7%, to \$9.4 million as of December 31, 2016. These represent our highest cost deposits and were replaced by lower costing municipal interest bearing deposits. As of December 31, 2016, our loan to deposit ratio was 73.7%, as compared to 89.1% as of December 31, 2015. This decrease is largely due to our rapid growth in public fund deposits over the past year. The balance of subordinated debentures, net of debt issuance costs, remained relatively unchanged at \$14.7 million, from 2015 to 2016.

Total stockholders' equity decreased \$1.2 million to \$63.0 million as of December 31, 2016, from \$64.2 million as of December 31, 2015. Stockholders' equity was impacted by an increase of \$4.3 million in accumulated other comprehensive loss, partially offset by our operating earnings of \$2.8 million. The increase in accumulated other comprehensive loss was a result of a negative change in the fair value of our securities available for sale, net of applicable taxes. As of December 31, 2016, the Bank was "well capitalized" under applicable regulatory capital guidelines and was in compliance with all applicable regulatory capital standards, with leverage, common equity tier 1, tier 1 risk-based and total risk-based capital ratios of 10.22%, 16.26%, 16.26% and 17.46%, respectively.

Loans

Our primary source of income is interest on loans. Our primary target market is small and medium-sized businesses and real estate investors in our market area. Our loan portfolio consists primarily of commercial and industrial loans and real estate loans secured by multi-family and commercial real estate properties located in our primary area. Our loan portfolio represents the highest yielding component of our earning asset base.

The following table sets forth the amount of loans, by category, as of the respective periods

	December 31, 2016		December 31, 2015	
	Amount	Percent	Amount	Percent
	(dollars in thousands)			
Commercial real estate - multi-family	\$ 192,168	38.9 %	\$ 187,885	40.7 %
Commercial real estate mortgages	133,432	27.0	121,330	26.3
Commercial and industrial	87,649	17.7	70,630	15.3
One-to-four family	59,801	12.1	54,277	11.8
Real estate - construction	13,540	2.7	19,970	4.3
Home equity lines of credit	5,068	1.0	4,217	0.9
Lease financing	2,319	0.5	2,505	0.5
Installment/consumer	297	0.1	966	0.2
Total	494,274	100.0 %	461,780	100.0 %
Allowance for loan losses	(5,799)		(5,268)	
Net loans	<u>\$ 488,475</u>		<u>\$ 456,512</u>	

We continued to experience growth in our loan portfolio, and the composition of our loan portfolio continues to evolve while maintaining a primary focus on commercial real estate mortgages and multi-family lending, to also increase the percentage of commercial and industrial loans as well as one-to-four family loans in our overall mix.

The following table sets forth the contractual maturity ranges, and the amount of loans with fixed and variable rates, in each maturity range as of December 31, 2016:

	Within One	After One But	After Five	Total
	Year	Within Five	Years	
	(in thousands)			
Commercial real estate - multi-family	\$ 237	\$ 22,311	\$ 169,620	\$ 192,168
Commercial real estate mortgages	4,463	33,599	95,370	133,432
Commercial and industrial	46,828	26,156	14,665	87,649
One-to-four family	789	7,383	51,629	59,801
Real estate - construction	13,540	-	-	13,540
Home equity lines of credit	-	2,991	2,077	5,068
Lease financing	254	2,065	-	2,319
Installment/consumer	142	155	-	297
Total	<u>\$ 66,253</u>	<u>\$ 94,660</u>	<u>\$ 333,361</u>	<u>\$ 494,274</u>
Rate provisions:				
Amounts with variable interest rates	\$ 60,442	\$ 50,515	\$ 313,829	\$ 424,786
Amounts with fixed interest rates	5,811	44,145	19,532	69,488
Total	<u>\$ 66,253</u>	<u>\$ 94,660</u>	<u>\$ 333,361</u>	<u>\$ 494,274</u>

Asset Quality

The Corporation has identified certain assets as risk elements. These assets include nonaccrual loans, other real estate owned, loans that are contractually past due 90 days or more as to principal or interest payments and still accruing and troubled debt restructurings (“TDRs”). These assets present more than the normal risk. Information about the Corporation’s risk elements is set forth below:

	December 31,	
	2016	2015
	(dollars in thousands)	
Nonaccrual loans		
Troubled debt restructuring	\$ 317	\$ 548
Other	2,033	-
Total nonaccrual loans	2,350	548
Loans past due 90 days or more and still accruing	-	100
Other real estate owned	-	-
Total nonperforming assets	2,350	648
Troubled debt restructurings - performing	2,198	2,218
Total risk elements	<u>\$ 4,548</u>	<u>\$ 2,866</u>

Gross interest income on nonaccrual loans and troubled debt restructurings:

Amount that has not been paid or recorded during the year under original terms	\$ 49	\$ 52
Actual amount recorded during the year	273	202

The allowance for loan losses to total loans (reserve coverage ratio) was 1.17% at December 31, 2016 compared to 1.14% at year-end 2015. The reserve coverage ratio increased primarily due to an increase in specific reserves on loans individually deemed to be impaired as well as an increase in the general allocation based on volume of growth as well as a greater percentage of commercial and industrial loans in the portfolio. The credit quality of the Bank’s loan portfolio remained excellent at December 31, 2016, with nonaccrual loans amounting to \$2.4 million, or 0.48% of total loans outstanding. Troubled debt restructurings totaled \$2.5 million at December 31, 2016. Of this amount, \$2.2 million were performing in accordance with their modified terms and \$316 thousand were nonaccrual and included in the aforementioned amount of nonaccrual loans.

The credit quality of our securities portfolio also remained excellent at December 31, 2016. The portfolio consisted of U.S. government agency obligations and mortgage-backed securities backed by the full faith and credit

obligations of the U.S. government, or by obligations of U.S. government sponsored entities. The portfolio contained one corporate debt obligation as of December 31, 2016.

We have maintained low levels of nonperforming assets since our inception in 2008. Our nonaccrual loans comprised 0.48% of total loans as of December 31, 2016, compared to 0.12% as of December 31, 2015. We believe that our historically low level of nonperforming assets reflects our long-term knowledge and relationships with a significant percentage of our borrowers, management's experience and knowledge with respect to our market and our underwriting discipline. In 2016, we had charge-offs of \$111 thousand and recoveries of \$10 thousand. We had net charge-offs of \$101 thousand and \$52 thousand for the years ended December 31, 2016 and 2015, respectively. However, historical performance is not necessarily an indicator of future performance, particularly considering our limited operating history. Future results could differ materially. However, management believes, based upon known factors, management's judgment and regulatory methodologies, that the current methodology used to determine the adequacy of the allowance for loan losses is reasonable. An analysis of our allowance for loan losses and net charge-offs is presented in the notes to our consolidated financial statements, which are included in this Annual Report.

Allowance for Loan Losses

We maintain an allowance for loan losses that represents management's best estimate of the probable incurred loan losses and risks inherent in the loan portfolio. In determining the allowance for loan losses, we estimate losses on specific loans, or groups of loans, where the probable incurred loss can be identified and reasonably determined. The balance of the allowance for loan losses is based on internally assigned risk classifications of loans, historical loan loss rates, changes in the nature of the loan portfolio, overall portfolio quality, industry concentrations, delinquency trends, current economic factors and the estimated impact of current economic conditions on certain historical loan loss rates, among other things. The allowance for loan losses consists of specific and general components, as well as an unallocated component. The unallocated component is maintained to cover uncertainties that could affect management's estimate of probable losses. The unallocated component reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating specific and general losses in the portfolio. In 2016, we had an unallocated portion totaling \$54 thousand. The allowance for loan losses is increased by our loan loss provision, which was discussed above, and reduced by net loan charge-offs. Loans are charged-off when we determine that collection has become unlikely. Recoveries are recorded only when cash payments are received. We held no other real estate owned at any of the reported periods.

We consider a loan to be impaired when, based on current information and events, it is probable that we will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status and the probability of collecting scheduled principal and interest payments when due. Loans for which the terms have been modified as a concession to the borrower due to the borrower experiencing financial difficulties are considered troubled debt restructurings and are classified as impaired. Loans considered to be troubled debt restructurings can be categorized as nonaccrual or performing. The impairment of a loan is measured at the value of expected future cash flows using the loan's effective interest rate, or at the loan's observable market price or the fair value of the collateral less costs to sell if the loan is collateral dependent. Generally, we measure impairment of such loans by reference to the fair value of the collateral less costs to sell. Loans that experience minor payment delays and payment shortfall generally are not classified as impaired.

The following table sets forth changes in the allowance for loan losses:

	Year ended December 31,	
	2016	2015
	(dollars in thousands)	
Beginning balance	\$ 5,268	\$ 4,453
Charge-offs:		
Commercial real estate mortgages	-	(98)
Commercial and industrial	(111)	-
Lease financing	-	(32)
Total	(111)	(130)
Recoveries:		
Commercial real estate mortgages	10	5
Commercial and industrial	-	58
Lease financing	-	15
Total	10	78
Net charge-offs	(101)	(52)
Provision for loan losses charged to operations	632	867
Ending balance	<u>\$ 5,799</u>	<u>\$ 5,268</u>
Ratio of net charge-offs during period to average loans outstanding	<u>0.02%</u>	<u>0.03%</u>

The following table sets forth the allocation of the total allowance for loan losses by loan type and sets forth the percentage of loans in each category to gross loans. The allocation of the allowance for loan losses as shown in the table should neither be interpreted as an indication of future charge-offs, nor as an indication that charge-offs in future periods will necessarily occur in these amounts or in the indicated proportions.

	2016		2015	
	Amount	Percentage of Loans to Total	Amount	Percentage of Loans to Total
	(dollars in thousands)			
Commercial real estate - multi-family	\$ 1,705	38.9 %	\$ 1,852	40.7 %
Commercial real estate mortgages	1,373	27.0	1,289	26.3
Commercial and industrial	2,110	17.7	1,446	15.3
One-to-four family	417	12.1	379	11.8
Real estate - construction	109	2.7	150	4.3
Home equity lines of credit	10	1.0	10	0.9
Lease financing	20	0.5	23	0.5
Installment/consumer	1	0.1	2	0.2
Unallocated	54	-	117	-
Total	<u>\$ 5,799</u>	<u>100.0 %</u>	<u>\$ 5,268</u>	<u>100.0 %</u>

Although we believe that our allowance for loan losses was adequate to provide for probable incurred losses in our loan portfolio as of December 31, 2016, future provisions will be subject to ongoing evaluations of the risks in our loan portfolio.

Securities

Our securities portfolio is used to make various term investments, to provide a source of liquidity, and to serve as collateral for certain types of deposits and borrowings and to provide interest income. We manage our investment portfolio according to a written investment policy approved by our Board of Directors. Investment balances in our securities portfolio are subject to change over time based on our funding needs and interest rate risk management

objectives. Our liquidity levels take into account anticipated future cash flows and all available sources of credits and are maintained at levels management believes are appropriate to assure future flexibility in meeting our anticipated funding needs.

As of December 31, 2016, our securities portfolio consisted primarily of U.S. government agency obligations and mortgage-backed securities with varying contractual maturities. However, these maturities do not necessarily represent the expected life of the securities as the securities may be called or paid down without penalty. No investment in any of those instruments exceeds any applicable limitation imposed by law or regulation. The Investment Committee reviews the investment portfolio on an ongoing basis in order to ensure that the investments conform to our investment policy as approved by the Board of Directors. As of December 31, 2016, our investment portfolio consisted almost entirely of available for sale securities. During 2016, we added a corporate debt obligation to the portfolio. The carrying values of our available for sale investment securities are adjusted for unrealized gain or loss as a valuation allowance, and any gain or loss is reported on an after-tax basis as a component of stockholders' equity.

The following table presents a summary of the amortized cost and estimated fair value of our investment portfolio as of the dates presented:

	December 31, 2016		December 31, 2015	
	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
	(in thousands)			
Available for sale:				
Mortgage backed securities – residential	\$ 143,496	\$ 139,385	\$ 81,239	\$ 80,418
U.S. government agency securities	129,191	125,349	71,252	70,625
Total	<u>\$ 272,687</u>	<u>\$ 264,734</u>	<u>\$ 152,491</u>	<u>\$ 151,043</u>
Held to maturity:				
Corporate bonds	\$ 3,000	\$ 3,032	\$ -	\$ -
Total	<u>\$ 3,000</u>	<u>\$ 3,032</u>	<u>\$ -</u>	<u>\$ -</u>

All of our mortgage-backed securities are agency securities. We do not hold any Fannie Mae or Freddie Mac preferred stock, collateralized debt obligations, collateralized loan obligations, structured investment vehicles, private label collateralized mortgage obligations, sub-prime, Alt-A, or second lien elements in our investment portfolio. At December 31, 2016, our investment portfolio did not contain any securities that are directly backed by subprime or Alt-A mortgages.

The following table sets forth the fair value, amortized cost, maturities and approximated weighted average yield based on estimated annual income divided by the average amortized cost of our securities portfolio at December 31, 2016. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

Available for sale	Amortized Cost	Fair Value	Yield
	(dollars in thousands)		
Due in one year or less	\$ -	\$ -	- %
Due from one to five years	18,650	18,472	1.41
Due from five to ten years	110,541	106,876	2.11
Due after ten years	-	-	-
Mortgage backed securities – residential	143,496	139,386	2.68
	<u>\$ 272,687</u>	<u>\$ 264,734</u>	<u>2.36 %</u>
Held to maturity:	Amortized Cost	Fair Value	Yield
	(dollars in thousands)		
Due from five to ten years	\$ 3,000	\$ 3,032	5.11 %
	<u>\$ 3,000</u>	<u>\$ 3,032</u>	<u>5.11 %</u>

Deposits

Deposits are our primary source of funds to support our earning assets. Total deposits were \$670.7 million as of December 31, 2016 compared to \$518.0 million as of December 31, 2015. To expand and diversify our deposit base, we deployed the following strategies:

- Expansion of our suite of products and services targeting professional practices;
- Strategic initiative to increase municipal deposit relationships in our market area;
- Growth of our retail branch network to provide deposit-taking services from four banking locations;
- Focus on developing and maintaining long-term relationships between our relationship bankers and customers through high quality service; and
- Commitment to the implementation of technology to enhance customer access to banking products and services.

In addition to our deposit growth, the composition of our deposit base has changed substantially since our inception in 2008. In our initial years of operation, we relied significantly on certificates of deposit, including brokered deposits, due to our limited branch network, deposit pricing and the timing of our funding needs. Since that time, we have expanded our geographic footprint with two additional branch locations attracting professional practice relationship deposits, and executed on a strategic initiative to attract public fund deposits. The transition has resulted in a lower overall cost of funds as the composition of the deposit portfolio shifted. We experienced significant growth in savings, N.O.W. and money market deposits during 2016 and 2015 as a result of our strategic initiatives focused on municipal deposit growth.

The following table shows the average balances and weighted average interest rates for each type of deposit since December 31, 2015:

	For the year ended December 31,					
	2016			2015		
	Average Balance	Percent	Weighted Average Rate	Average Balance	Percent	Weighted Average Rate
	(dollars in thousands)					
Savings, N.O.W. and money market deposits	\$ 394,230	63.2 %	0.44 %	\$ 207,410	45.7 %	0.48 %
Demand deposits	192,121	30.8	-	191,265	42.1	-
Certificates of deposit of \$100,000 or more	27,741	4.4	1.05	40,471	8.9	0.93
Other time deposits	10,079	1.6	1.17	15,121	3.3	1.34
Total deposits	<u>\$ 624,171</u>	<u>100.0 %</u>	<u>0.34 %</u>	<u>\$ 454,267</u>	<u>100.0 %</u>	<u>0.35 %</u>

The following table presents a summary of the Corporation's time deposits in amounts of \$100,000 or more by remaining term to maturity at December 31, 2016:

Time Deposits of \$100,000 or More Maturing Within				
0-3 Months	Over 3 to 6 Months	Over 6 to 12 Months	Over 12 Months	Total
(in thousands)				
\$ 4,609	\$ 4,459	\$ 6,054	\$ 2,946	\$ 18,068

Capital resources

Stockholders' equity totaled \$63.0 million at December 31, 2016, a decrease of \$1.2 million from \$64.2 million at December 31, 2015. The decrease was primarily attributable to a decrease of \$4.3 million in accumulated other comprehensive income, partially offset by operating earnings of \$2.8 million. Accumulated other comprehensive income decreased due to a decrease in the after tax amount of unrealized gains on available for sale securities. During 2016, 775 thousand shares of common stock were exchanged for an equivalent number of shares of non-voting common stock. In addition, we issued 60,732 shares of restricted stock under our 2015 Omnibus Stock and Incentive Plan, and 5,800 shares of our common stock were issued upon the exercise of stock options. In September 2015, the shares of Series A preferred stock that we issued in our December 2014 private placement were exchanged on a one-for-one basis for shares of our non-voting common stock. The Series A preferred stock had been issued as a non-voting common stock equivalent and was exchanged following the approval of an amendment to our certificate of incorporation authorizing a class of non-voting common stock at our 2015 annual meeting of stockholders. As of December 31, 2016, our equity structure consisted entirely of shares of common stock. Historically, we have not paid cash dividends on our common stock, but instead have retained our earnings to support the continued growth of our organization. We expect to continue this practice for the foreseeable future.

We are subject to various regulatory capital requirements administered by the federal banking agencies. At this time, these regulatory capital requirements apply only at the bank level. As of December 31, 2016, we were in compliance with all applicable regulatory capital requirements, and the Bank was classified as "well capitalized" for purposes of the OCC's prompt corrective action regulations with leverage, common equity tier 1 risk-based, tier 1 risk-based and total risk-based capital ratios of 10.22%, 16.26%, 16.26% and 17.46%, respectively. "Well capitalized" is the highest capital classification for FDIC-insured financial institutions in the United States. As we employ our capital and continue to grow our operations, our capital levels may decrease depending on our level of earnings. However, we expect to monitor and control our growth in order to remain a "well capitalized" under the applicable regulatory guidelines and in compliance with all regulatory capital standards applicable to us.

CONSOLIDATED STATEMENTS OF CONDITION

	At December 31,	
	2016	2015
	(dollars in thousands, except share and per share data)	
ASSETS		
Cash and due from banks	\$ 4,386	\$ 4,797
Interest earning deposits with banks	1,962	817
Federal funds sold	6	7
Total cash and cash equivalents	6,354	5,621
Securities available for sale, at fair value	264,734	151,043
Securities, held to maturity (fair value of \$3,032)	3,000	-
Securities, restricted	4,131	3,712
Loans	494,274	461,780
Less: Allowance for loan losses	(5,799)	(5,268)
Loans, net	488,475	456,512
Premises and equipment, net	6,052	6,687
Accrued interest receivable	2,610	1,895
Deferred tax asset, net	5,602	2,971
Other assets	477	692
Total Assets	\$ 781,435	\$ 629,133
LIABILITIES AND STOCKHOLDERS' EQUITY		
Demand deposits	\$ 177,299	\$ 189,200
Savings, N.O.W. and money market deposits	465,890	286,635
Certificates of deposit of \$100,000 or more	18,068	31,759
Other time deposits	9,426	10,439
Total deposits	670,683	518,033
Short-term borrowings	26,477	26,064
Subordinated debentures, net	14,735	14,697
Total borrowings	41,212	40,761
Accrued interest payable	110	131
Other liabilities	6,438	6,054
Total Liabilities	718,443	564,979
Stockholders' Equity:		
Common stock, par value \$0.01 per share; 100,000,000 authorized shares; 5,015,252 issued and outstanding at December 31, 2016 and 5,723,720 issued and outstanding at December 31, 2015	50	57
Non-voting common stock, par value \$0.01 per share; 20,000,000 authorized shares; 1,931,250 issued and outstanding at December 31, 2016 and 1,156,250 issued and outstanding at December 31, 2015	19	12
Surplus	64,131	63,791
Retained earnings	4,041	1,251
	68,241	65,111
Accumulated other comprehensive loss	(5,249)	(957)
Total Stockholders' Equity	62,992	64,154
Total Liabilities and Stockholders' Equity	\$ 781,435	\$ 629,133

See accompanying notes to the Consolidated Financial Statements.

CONSOLIDATED STATEMENTS OF INCOME

	<u>Year Ended December 31,</u>	
	<u>2016</u>	<u>2015</u>
	(dollars in thousands, except per share data)	
Interest income:		
Loans (including fee income)	\$ 20,275	\$ 19,012
Securities, taxable	4,545	2,468
Deposits with banks	48	24
Total interest income	24,868	21,504
Interest expense:		
Savings, N.O.W. and money market deposits	1,740	992
Certificates of deposit of \$100,000 or more	290	375
Other time deposits	118	203
Short-term borrowings	61	73
Subordinated debentures	1,092	46
Total interest expense	3,301	1,689
Net interest income	21,567	19,815
Provision for loan losses	632	867
Net interest income after provision for loan losses	20,935	18,948
Other income:		
Other service charges and fees	452	410
Service charges on deposit accounts	379	389
Net securities gains (losses)	346	(71)
Professional practice revenue	300	277
Total other income	1,477	1,005
Other expense:		
Salaries and employee benefits	9,643	8,130
Occupancy and equipment, net	2,822	2,577
Software services	1,430	1,473
Advertising and business development	985	794
Professional fees	664	656
FDIC insurance	352	301
Other operating expenses	2,172	2,067
Total other expenses	18,068	15,998
Income before income taxes	4,344	3,955
Income tax expense	1,554	1,421
Net income	\$ 2,790	\$ 2,534
Basic earnings per share	\$ 0.40	\$ 0.42
Diluted earnings per share	\$ 0.40	\$ 0.37

See accompanying notes to the Consolidated Financial Statements.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE (LOSS) INCOME

	Year Ended December 31,	
	2016	2015
	(in thousands)	
Net income	\$ 2,790	\$ 2,534
Other comprehensive (loss) income:		
Unrealized holding (losses) arising during the period	(6,159)	(1,333)
Reclassification adjustment for (gains) losses included in net securities gains (losses) on the consolidated statements of operations	(346)	71
Change in unrealized net (losses) before income taxes	(6,505)	(1,262)
Tax effect	2,213	417
Other comprehensive (loss)	(4,292)	(845)
Total comprehensive (loss) income	\$ (1,502)	\$ 1,689

See accompanying notes to the Consolidated Financial Statements.

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

	Non-Cumulative Series A Preferred Stock		Common Stock		Non-Voting Common Stock		Surplus	Retained Earnings (Accumulated Deficit)	Accumulated Other Comprehensive Loss	Total
	Shares Outstanding	Amount	Shares Outstanding	Amount	Shares Outstanding	Amount				
	(dollars in thousands, except shares)									
Balance at January 1, 2015	1,156,250	\$ 8,950	5,723,720	\$ 57	-	\$ -	\$ 54,809	\$ (1,283)	\$ (112)	\$ 62,421
Exchange of preferred stock to non-voting common stock	(1,156,250)	(8,950)	-	-	1,156,250	12	8,938	-	-	-
Share based compensation expense	-	-	-	-	-	-	44	-	-	44
Net Income	-	-	-	-	-	-	-	2,534	-	2,534
Other comprehensive loss, net of deferred income taxes	-	-	-	-	-	-	-	-	(845)	(845)
Balance at December 31, 2015	-	-	5,723,720	57	1,156,250	12	63,791	1,251	(957)	64,154
Exchange of voting common stock to non-voting common stock	-	-	(775,000)	(7)	775,000	7	-	-	-	-
Exercise of Stock Options	-	-	5,800	-	-	-	58	-	-	58
Issuance of voting common restricted stock	-	-	60,732	-	-	-	-	-	-	-
Share based compensation expense	-	-	-	-	-	-	282	-	-	282
Net Income	-	-	-	-	-	-	-	2,790	-	2,790
Other comprehensive loss, net of deferred income taxes	-	-	-	-	-	-	-	-	(4,292)	(4,292)
Balance at December 31, 2016	-	\$ -	5,015,252	\$ 50	1,931,250	\$ 19	\$ 64,131	\$ 4,041	\$ (5,249)	\$ 62,992

See accompanying notes to the Consolidated Financial Statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Year Ended December 31,	
	2016	2015
	(in thousands)	
Cash flows from operating activities:		
Net income	\$ 2,790	\$ 2,534
Adjustments to reconcile net income to net cash from operating activities		
Provision for loan losses	632	867
Depreciation and amortization	1,062	1,021
Amortization of premium and accretion of discount on investment securities, net	744	762
Amortization of debt issuance costs	38	-
Share based compensation expense	282	44
Net securities (gains) losses	(346)	71
Increase in accrued interest receivable	(715)	(401)
Decrease (increase) in other assets	215	(178)
Increase in accrued and other liabilities	363	1,767
Increase in deferred income tax	(418)	(245)
Net cash provided by operating activities	4,647	6,242
Cash flows from investing activities:		
Purchases of securities available for sale	(367,937)	(85,748)
Sales of securities available for sale	71,910	18,920
Calls/redemptions of securities available for sale	175,433	14,307
Purchase of securities held to maturity	(3,000)	-
Purchase of securities, restricted	(11,694)	(11,526)
Sales of securities, restricted	11,275	11,776
Net increase in loans	(32,595)	(82,180)
Purchase of banking premises and equipment, net of disposals	(427)	(1,719)
Net cash used by investing activities	(157,035)	(136,170)
Cash flows from financing activities:		
Net increase in deposits	152,650	122,908
Increase (decrease) in short-term borrowings	413	(20,041)
Proceeds from exercise of stock options	58	-
Net proceeds from issuance of subordinated debentures	-	14,697
Net cash provided by financing activities	153,121	117,564
Increase (decrease) in cash and cash equivalents	733	(12,364)
Cash and cash equivalents beginning of period	5,621	17,985
Cash and cash equivalents end of period	\$ 6,354	\$ 5,621
Supplemental information-cash flows:		
Cash paid for:		
Interest	\$ 3,322	\$ 1,664
Income taxes	\$ 2,121	\$ 1,845

See accompanying notes to the Consolidated Financial Statements.

EMPIRE BANCORP, INC
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements include the accounts of Empire Bancorp, Inc. and its wholly-owned subsidiary Empire National Bank. Throughout these notes, “Corporation” refers to Empire Bancorp, Inc. and its consolidated subsidiary, except as the context otherwise requires, and “Bank” refers only to Empire National Bank.

Because the Bank is the sole material asset of the Corporation, other than cash, the Corporation’s financial condition and operating results principally reflects those of the Bank. The Bank is a national banking association domiciled in Islandia, New York, which commenced operations on February 25, 2008. The principal business office of the Corporation and the Bank is located at 1707 Veterans Highway, Islandia, New York.

The financial statements have been prepared in accordance with accounting principles generally accepted in the United States (“GAAP”) and to general practices within the financial institution industry. Certain reclassifications have been made to prior year amounts to conform to the current year presentation. The following is a description of the significant accounting policies that the Corporation follows in preparing its financial statements.

a) Use of Estimates

In preparing the financial statements, management has made estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expense during the reported periods. Such estimates are subject to change in the future as additional information becomes available or previously existing circumstances are modified. Actual future results could differ significantly from those estimates.

b) Cash Flows

Cash and cash equivalents include cash, deposits with other financial institutions with maturities fewer than 90 days, and federal funds sold. Net cash flows are reported for customer loan and deposit transactions, interest bearing deposits in other financial institutions, and federal funds purchased and repurchase agreements.

c) Securities

Current accounting standards require that investment securities be classified as held to maturity, trading or available for sale. The trading category is not applicable to any securities in the Corporation’s portfolio because the Corporation does not buy or hold debt or equity securities principally for the purpose of selling in the near term. Debt securities are classified as held to maturity and carried at amortized cost when management has the positive intent and ability to hold them to maturity. Debt securities are classified as available for sale when they might be sold before maturity. Available for sale securities, or debt and equity securities which are neither held to maturity securities nor trading securities, are reported at fair value, with unrealized gains and losses, net of the related income tax effect, included in other comprehensive income, a separate component of stockholders’ equity. Restricted securities, as disclosed on the balance sheet consisting of Atlantic Community Bankers Bank stock, Federal Home Loan Bank stock, and Federal Reserve Bank stock, are carried at cost.

Interest income includes amortization of purchase premium or accretion of discount. Premiums and discounts on securities are amortized or accreted on the level-yield method. Prepayments are anticipated for mortgage-backed securities. Realized gains and losses on the sale of securities are determined using the specific identification method.

Investment securities are evaluated for other-than-temporary (“OTTI”) no less often than quarterly. In determining OTTI, management considers many factors, including: (1) the length of time and the extent to which the fair value has been less than cost; (2) the financial condition and near-term prospects of the issuer; (3) whether the market

decline was affected by macroeconomic conditions; and (4) whether management has the intent to sell the debt security or more likely than not will be required to sell the debt security before its anticipated recovery. The assessment of whether an other-than-temporary decline exists involves a high degree of subjectivity and judgment and is based on information available to management at a point in time.

The assessment of whether an other-than-temporary decline exists involves a high degree of subjectivity and judgment and is based on the information available to management at a point in time.

When other-than-temporary loss occurs, management considers whether it intends to sell, or, more likely than not, will be required to sell a security in an unrealized loss position before recovery of its amortized cost basis. If either of these criteria is met, the entire difference between amortized cost and fair value is recognized in earnings. For securities that do not meet the aforementioned criteria, the amount of impairment recognized in earnings is limited to the amount related to credit losses, while impairment related to other factors is recognized in other comprehensive income.

d) Federal Home Loan Bank and Federal Reserve Bank Stock

The Bank is a member of and owns stock in the Federal Home Loan Bank of New York (“FHLB”) and the Federal Reserve Bank of New York. The FHLB requires member banks to own a certain amount of stock based on the level of borrowings and other factors, and additional amounts may be invested. The stock of both entities is carried at cost, classified as restricted securities and periodically evaluated for impairment based on the prospects for the ultimate recovery of par value. Both cash and stock dividends, if any, are reported as income.

e) Loans and Allowance for Loan Losses

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are stated at the principal amount outstanding less any charge-offs, net of deferred origination fees and costs, and an allowance for loan losses. Interest on loans is credited to income based on the principal amount outstanding. Loan origination and commitment fees and certain direct and indirect costs incurred in connection with loan originations are deferred and amortized to income over the life of the related loans without anticipating prepayments and as an adjustment to yield. When a loan prepays, the remaining unamortized net deferred origination fees and costs are recognized immediately upon payoff.

Past due status is based on the contractual terms of the loan. Loans that are deemed uncollectable according to the terms of the loan agreement, or are 90 days past due, are placed on nonaccrual and previously accrued interest is reversed and charged against interest income. An exception is made for 90-day past due loans that are well secured and in the process of collection. In all cases, loans are placed on nonaccrual or charged-off at an earlier date if collection of principal or interest is considered doubtful. Interest received on nonaccrual loans is accounted for on the cash basis or cost-recovery method until the loans qualify for return to an accrual status. However, if the Corporation believes that the loan will be fully collectible based upon the individual loan evaluation assessing factors such as collateral and collectability, accrued interest will be recognized upon attainment of certain events. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current for a period of time, and future payments are reasonably assured. When the accrual of interest income is discontinued on a loan, any accrued but unpaid interest is reversed against current period income. Unless otherwise noted, the above policy is applied consistently to all loan classes.

The allowance for loan losses is a valuation allowance for probable incurred credit losses. Loan losses are charged against the allowance when management believes the uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance. Management estimates the allowance balance required using past loss experience, the nature and volume of the portfolio, information about specific borrower situations and estimated collateral values, economic conditions, and other factors. Allocations of the allowance may be made for specific loans, but the entire allowance is available for any loan that, in management’s judgment, should be charged off. The process for estimating credit losses and determining the allowance for loan losses as of any balance sheet date is subjective in nature and requires material estimates. Actual results could differ significantly from those estimates.

The allowance for loan losses is established through provisions for loan losses charged against income. When available information confirms that specific loans or portions thereof, are uncollectible, these amounts are charged against the allowance for loan losses, and subsequent recoveries, if any, are credited to the allowance. The allowance consists of specific and general components. The specific component relates to loans that are individually classified as impaired when, based on current information and events, it is probably that the Corporation will be unable to collect all amounts due according to the contractual terms of the loan agreement. Loans for which the terms have been modified resulting in a concession, and for which the borrower is experiencing financial difficulties, are considered troubled debt restructurings (“TDRs”) and classified as impaired.

Management currently estimates the general component of the allowance based upon factors including, but not limited to, an evaluation of inherent risks in the loan portfolio, industry experience, credit risk grades assigned to loans, adverse situations that may affect the borrowers’ ability to repay, the estimated value of any underlying collateral, and current economic conditions. Future additions to the allowance may be necessary based on changes in economic conditions or other factors used in management’s determination as well as probable incurred losses. In addition, as part of their examination process, regulatory agencies may require additions to the allowance based on their judgments about information available to them. An unallocated component is maintained to cover uncertainties that could affect management’s estimate of probable incurred losses. The unallocated component of the allowance reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating specific and general losses in the portfolio.

Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the borrower’s prior payment record, and the amount of the shortfall in relation to the principal and interest owed.

If a loan is impaired, a portion of the allowance is allocated so that the loan is reported, net, at the present value of estimated future cash flows using the loan’s existing rate or at the fair value of collateral if repayment is expected solely from the collateral.

Troubled debt restructurings are individually evaluated for impairment and included in the separately identified impairment disclosures. TDRs are measured at the present value of estimated future cash flows using the loan’s effective rate at inception. If a TDR is considered to be a collateral dependent loan, the loan is reported, net, at the fair value of the collateral. For TDRs that subsequently default, the Company determines the amount of the allowance on that loan in accordance with the accounting policy for the allowance for loan losses on loans individually identified as impaired.

f) Concentration of Credit Risk

The Corporation’s portfolio segments are comprised of commercial real estate - multi-family loans, commercial real estate mortgages, commercial and industrial loans, one-to-four family loans, real estate – construction loans, home equity lines of credit, lease financing, and installment/consumer loans. Risk characteristics of the Corporation’s commercial real estate and real estate construction loans tend to be subjective due to vacancy rates, cash flows and the underlying real estate values located in the Corporation’s market and primary service area of the counties of Suffolk, Nassau, Kings, Queens, and New York. Commercial and industrial and lease financing risk characteristics are driven by economic conditions and the management and capital strength of the borrower.

g) Premises and Equipment

Buildings, furniture and fixtures and equipment are stated at cost less accumulated depreciation. Equipment, computer hardware and software, and furniture and fixtures are depreciated using the straight-line method with a range for useful lives of two to ten years. Leasehold improvements are amortized over the lives of the respective leases, including any option extensions when expected to exercise or the service lives of the improvements whichever is shorter.

Improvements and major repairs are capitalized, while the cost of ordinary maintenance, repairs and minor improvements is charged to operations.

h) Loan Commitments and Related Financial Instruments

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

i) Income Taxes

Income tax expense is the total of the current year income tax due or refundable and the change in deferred tax assets and liabilities. Deferred tax assets and liabilities are the expected future tax amounts for the temporary differences between carrying amounts and tax bases of assets and liabilities, computed using tax rates. Temporary differences are differences between the tax basis of assets and liabilities and their reported amounts in the financial statements that will result in taxable or deductible amounts in future years. The effect on deferred taxes of a change in tax rates is recognized in income in the period that includes the enactment date. A valuation allowance is recorded for deferred tax assets if the Corporation cannot determine that the benefits will more likely than not be realized.

A tax position is recognized as a benefit only if it is “more likely than not” that the tax position would be sustained in a tax examination, with a tax examination being presumed to occur. The amount recognized is the largest amount of tax benefit that is greater than fifty percent likely of being realized on examination. For tax positions not meeting the “more likely than not” test, no tax benefit is recorded.

j) Earnings per Share

Basic earnings per common share is computed by dividing net income by the weighted-average number of common shares outstanding for the period. Diluted earnings per share, which reflect the potential dilution of mandatory convertible preferred stock formerly outstanding as well as the dilution that could occur if outstanding options and warrants were exercised and resulted in the issuance of common stock that then shared in the earnings of the Corporation, is computed by dividing net income by the weighted average number of common shares and common stock equivalents. All outstanding unvested, share-based payment awards that contain rights to non-forfeitable dividends are considered participating securities for this calculation.

k) Stock Based Compensation Plans

Stock based compensation awards are recorded in accordance with FASB ASC No. 718 and 505, “*Accounting for Stock-Based Compensation*” which requires companies to record compensation cost for stock options, restricted stock awards and stock awards granted to employees in return for employee service. The cost is measured at the fair value of the options and awards when granted, and this cost is expensed over the employee service period, which is normally the vesting period of the options and awards.

l) Comprehensive Income

Comprehensive income includes net income and other comprehensive income. Other comprehensive income includes revenues, expenses, gains and losses that under generally accepted accounting principles are included in comprehensive income but excluded from net income. Comprehensive income and accumulated other comprehensive income are reported net of related income taxes. Accumulated other comprehensive income for the Corporation includes unrealized holding gains or losses on available for sale securities. Such gains or losses are net of reclassification adjustments for realized gains (losses) on sales of available for sale securities.

m) Fair Value of Financial Instruments

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

n) New Accounting Standards

ASU 2015-03, Interest – Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs

In April 2015, the FASB amended existing guidance related to the presentation of debt issuance costs. It requires entities to present debt issuance costs related to a recognized debt liability as a direct deduction from the carrying amount of that debt liability. The guidance does not address presentation or subsequent measurement of debt issuance costs related to the line-of-credit arrangements. The Corporation early adopted ASU 2015-03 at December 31, 2015. The adoption of this standard did not have a material effect on the Corporation's operating results.

ASU 2014-12, Compensation – Stock Compensation (718) - Accounting for Share-Based Payments When the Terms of an Award Provide that a Performance Target Could Be Achieved After the Requisite Service Period.

In June 2014, the FASB amended existing guidance related to the accounting for share-based payments when the terms of an award provide that a performance target could be achieved after the requisite service period. These amendments require that a performance target that affects vesting and that could be achieved after the requisite service period be treated as a performance condition. A reporting entity should apply existing guidance in Topic 718, Compensation – Stock Compensation, as it relates to awards with performance conditions that affect vesting to account for such awards. The total amount of compensation cost recognized during and after the requisite service period should reflect the number of awards that are expected to vest and should be adjusted to reflect those awards that ultimately vest. The requisite service period ends when the employee can cease rendering service and still be eligible to vest in the award if the performance target is achieved. The adoption of this standard did not have upon adoption and is not expected to have going forward a material effect on the Corporation's operating results; Empire Bancorp, Inc. 2015 Omnibus Stock and Incentive Plan and the Empire National Bank 2008 Stock Incentive Plan do not have a performance target that has to be achieved.

o) Impact of Issued but Not Yet Effective Accounting Standards

ASU 2014-09, Revenue from Contracts with Customers (Topic 606)

In May 2014, the FASB amended existing guidance related to revenue from contracts with customers. This amendment supersedes and replaces nearly all existing revenue recognition guidance, including industry-specific guidance, establishes a new control-based revenue recognition model, changes the basis for deciding when revenue is recognized over time or at a point in time, provides new and more detailed guidance on specific topics and expands and improves disclosures about revenue. In addition, this amendment specifies the accounting for some costs to obtain or fulfill a contract with a customer. The amendments in ASU 2014-09 for public entities such as the Corporation, is effective for interim and annual reporting periods beginning after December 15, 2017. The amendment is being evaluated for the impact that ASU 2014-09 will have on the Corporation's financial position, results of operations and disclosures, but we do not believe that such impact will be material.

ASU 2016-01, Financial Instruments – Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities

In January 2016, the FASB amended existing guidance that requires equity investments (except those accounted for under the equity method of accounting, or those that result in consolidation of the investee) to be measured at fair value with changes in fair value recognized in net income. It requires public business entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes. It requires separate presentation of financial assets and financial liabilities by measurement category and form of financial asset. It

eliminates the requirement for public business entities to disclose the method(s) and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost. The amendments in ASU 2016-01 for public entities such as the Corporation is effective for interim and annual reporting beginning after December 15, 2017. The amendment is being evaluated for the impact that ASU 2016-01 will have on the Corporation's financial position, results of operations and disclosures, but we do not believe that such impact will be material.

ASU 2016-02, Leases (Topic 842)

In February 2016, the FASB amended existing guidance that requires lessees recognize the following for all leases (with the exception of short-term leases) at the commencement date (1) A lease liability, which is a lessee's obligation to make lease payments arising from a lease, measured on a discounted basis; and (2) A right-of-use asset, which is an asset that represents the lessee's right to use, or control the use of, a specified asset for the lease term. Under the new guidance, lessor accounting is largely unchanged. Certain targeted improvements were made to align, where necessary, lessor accounting with the lessee accounting model and Topic 606, Revenue from Contracts with Customers. The amendments in ASU 2016-02 for public entities such as the Corporation is effective for interim and annual reporting periods beginning after December 15, 2018. The amendment is being evaluated for the impact that ASU 2016-02 will have on the Corporation's financial position, results of operations and disclosures. Upon adoption of the ASU, the Corporation's assets and liabilities will increase due to the recognition of a lease asset and a lease obligation.

ASU 2016-09, Compensation- Stock Compensation (Topic 718)

In March 2016, the FASB amended existing guidance to simplify several aspects of the accounting for employee share-based payment transactions for both public and nonpublic entities, including the accounting for income taxes, forfeitures, and statutory tax withholding requirements as well as classification in the statement of cash flows. ASU 2016-09 is effective for annual periods, and interim periods within those annual periods, beginning after December 15, 2016, with early adoption permitted. The Company adopted ASU 2016-09 in the first quarter of 2016. The adoption of ASU 2016-09 did not have a material impact on the Company's consolidated financial statements.

ASU 2016-13, Financial Instruments – Credit Losses (Topic 326)

In June 2016, FASB issued guidance to replace the incurred loss model with an expected loss model, which is referred to as the current expected credit loss (CECL) model. The CECL model is applicable to the measurement of credit losses on financial assets measured at amortized cost, including loan receivables, held to maturity debt securities, and reinsurance receivables. It also applies to off-balance sheet credit exposures not accounted for as insurance (loan commitments, standby letters of credit, financial guarantees, and other similar instruments) and net investments in leases recognized by a lessor. For debt securities with other-than temporary impairment (OTTI), the guidance will be applied prospectively. Existing purchased credit impaired (PCI) assets will be grandfathered and classified as purchased credit deteriorated (PCD) assets at the date of adoption. The asset will be grossed up for the allowance for expected credit losses for all PCD assets at the date of adoption and will continue to recognize the noncredit discount in interest income based on the yield of such assets as of the adoption date. Subsequent changes in expected credit losses will be recorded through the allowance. For all other assets within the scope of CECL, a cumulative-effect adjustment will be recognized in retained earnings as of the beginning of the first reporting period in which the guidance is effective. The amendments in ASU 2016-13 for public entities such as the Corporation is effective for interim and annual reporting periods beginning after December 15, 2020. The amendment is being evaluated for the impact that ASU 2016-13 will have on the Corporation's financial position, results of operations and disclosures. The overall impact of the amendment will be affected by the portfolio composition and quality at the adoption date as well as economic conditions and forecast at that time.

p) Subsequent Events

The Corporation has evaluated subsequent events for recognition and disclosure through March 30, 2017, which is the date the financial statements were available to be issued.

2. SECURITIES

The following tables summarize the amortized cost and fair value of securities available-for-sale and securities held-to-maturity at December 31, 2016 and 2015:

	December 31, 2016			
	Gross		Gross	
	Amortized Cost	Unrealized Gains	Unrealized Losses	Estimated Fair Value
	(in thousands)			
Available for sale:				
Mortgage-backed securities-residential	\$ 143,496	\$ 95	\$ (4,206)	\$ 139,385
U.S. government agency securities	129,191	-	(3,842)	125,349
Total available for sale securities	<u>\$ 272,687</u>	<u>\$ 95</u>	<u>\$ (8,048)</u>	<u>\$ 264,734</u>

	Gross		Gross		Estimated Fair Value
	Amortized Cost	Unrecognized Gains	Unrecognized Losses		
	(in thousands)				
Held to maturity:					
Corporate bonds	\$ 3,000	\$ 32	\$ -	\$ 3,032	
Total held to maturity	<u>\$ 3,000</u>	<u>\$ 32</u>	<u>\$ -</u>	<u>\$ 3,032</u>	

	December 31, 2015			
	Gross		Gross	
	Amortized Cost	Unrealized Gains	Unrealized Losses	Estimated Fair Value
	(in thousands)			
Available for sale:				
Mortgage-backed securities-residential	\$ 81,239	\$ 377	\$ (1,198)	\$ 80,418
U.S. government agency securities	71,252	77	(704)	70,625
Total available for sale securities	<u>\$ 152,491</u>	<u>\$ 454</u>	<u>\$ (1,902)</u>	<u>\$ 151,043</u>

	Gross		Gross		Estimated Fair Value
	Amortized Cost	Unrecognized Gains	Unrecognized Losses		
	(in thousands)				
Held to maturity:					
Corporate bonds	\$ -	\$ -	\$ -	\$ -	
Total held to maturity	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	

Securities with unrealized losses at December 31, 2016 and 2015 aggregated by category and length of time that individual securities have been in a continuous unrealized loss position are as follows:

	December 31, 2016					
	Less than 12 months		Greater than 12 months		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
	(in thousands)					
Available for sale:						
Mortgage-backed securities-residential	\$ 117,762	\$ (3,661)	\$ 10,774	\$ (545)	\$ 128,536	\$ (4,206)
U.S. government agency securities	125,349	(3,842)	-	-	125,349	(3,842)
Total available for sale securities	<u>\$ 243,111</u>	<u>\$ (7,503)</u>	<u>\$ 10,774</u>	<u>\$ (545)</u>	<u>\$ 253,885</u>	<u>\$ (8,048)</u>

	December 31, 2015					
	Less than 12 months		Greater than 12 months		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
	(in thousands)					
Available for sale:						
Mortgage-backed securities-residential	\$ 21,867	\$ (305)	\$ 19,886	\$ (893)	\$ 41,753	\$ (1,198)
U.S. government agency securities	64,957	(704)	-	-	64,957	(704)
Total available for sale securities	<u>\$ 86,824</u>	<u>\$ (1,009)</u>	<u>\$ 19,886</u>	<u>\$ (893)</u>	<u>\$ 106,710</u>	<u>\$ (1,902)</u>

At December 31, 2016, all of the mortgage-backed securities and U.S. government agency securities held by the Corporation were issued by U.S. government-sponsored entities and agencies, primarily Ginnie Mae and Fannie Mae, institutions which the government has affirmed its commitment to support. Because the decline in fair value is

attributable to changes in interest rates and illiquidity, and not credit quality, and because the Corporation does not have the intent to sell these mortgage-backed securities and U.S. government agency securities, and it is likely that it will not be required to sell the securities before their anticipated recovery, the Corporation does not consider these securities to be other-than-temporarily impaired at December 31, 2016.

The fair value of debt securities and carrying amount, if different, at December 31, 2016 by contractual maturity were as follows. Securities not due at a single maturity date, solely mortgage-backed securities, are shown separately.

December 31, 2016	
Available for Sale	
Amortized Cost	Fair Value
(in thousands)	
Due in one year or less	\$ - \$ -
Due from one to five years	18,650 18,472
Due from five to ten years	110,541 106,876
Due after ten years	- -
Mortgage-backed securities-residential	143,496 139,386
Total	<u>\$ 272,687 \$ 264,734</u>

Held to Maturity	
Amortized Cost	Fair Value
(in thousands)	
Due from five to ten years	\$ 3,000 \$ 3,032
Total	<u>\$ 3,000 \$ 3,032</u>

Proceeds from sales and calls of securities available for sale were \$247.3 million and \$33.2 million for the years ended December 31, 2016 and 2015, respectively. There were gross gains of \$406 thousand realized on the sale and call of securities during 2016 as compared to no gross gains in 2015. There were gross losses on the sale and call of securities in 2016 and 2015 of \$60 thousand and \$71 thousand, respectively.

At December 31, 2016, investment securities with a carrying value of \$221.4 million were pledged as collateral to secure public and bankruptcy deposits.

3. LOANS

The following table sets forth the major classifications of loans:

	December 31,	
	2016	2015⁽¹⁾
(in thousands)		
Commercial real estate-multi family	\$ 192,168	\$ 187,885
Commercial real estate mortgages	133,432	121,330
Commercial and industrial loans	87,649	70,630
One-to-four family loans	59,801	54,277
Real estate - construction loans	13,540	19,970
Home equity lines of credit	5,068	4,217
Lease financing	2,319	2,505
Installment/consumer loans	297	966
Total	<u>\$ 494,274</u>	<u>\$ 461,780</u>
Allowance	<u>(5,799)</u>	<u>(5,268)</u>
Net loans	<u>\$ 488,475</u>	<u>\$ 456,512</u>

(1) Prior year loan amounts are shown net of deferred costs to conform to the current year presentation.

Allowance for Loan Losses

An evaluation of the allowance for loan losses is performed on a quarterly basis. To adequately assess the allowance for loan losses the following quantitative and qualitative factors are considered:

Quantitative factors:

- Delinquency trends of the Corporation;
- Historical loss experience of the Corporation; and
- Results of internal and external loan reviews.

Qualitative factors:

- Allowance levels and trends for peer banks;
- Changes in lending policies, procedures, underwriting criteria, as well as collection, charge-off and recovery practices;
- Changes in international, national, regional, and local economic and business conditions;
- Changes in portfolio nature and volume;
- Changes in the experience, ability, and depth of lending management and related staff;
- Changes in the volume and severity of past due loans, nonaccrual loans, criticized and classified loans;
- Changes in the quality of the Corporation's loan review system;
- Changes in the value of underlying collateral for collateral-dependent loans;
- Existence and effect of any concentrations of credit and changes in the level of each such concentration;
- Effect of other external factors such as competition and legal and regulatory requirements;
- Comparison of the Corporation's performance versus that of its peer group; and
- Delinquency trends for peer banks.

The following tables present the balance in the allowance for loan losses and the recorded investment in loans by portfolio segment and based on impairment methods as of December 31, 2016 and 2015:

2016	Commercial real estate- multi family	Commercial real estate mortgages	Commercial and industrial loans	One-to- four family	Real estate- construction loans (in thousands)	Home equity lines of credit	Lease financing	Installment/ consumer loans	Unallocated	Total
Beginning balance	\$ 1,852	\$ 1,289	\$ 1,446	\$ 379	\$ 150	\$ 10	\$ 23	\$ 2	\$ 117	\$ 5,268
Provision for loan losses	(147)	74	775	38	(41)	-	(3)	(1)	(63)	632
Charge-offs	-	-	(111)	-	-	-	-	-	-	(111)
Recoveries	-	10	-	-	-	-	-	-	-	10
Net charge-offs/recoveries	-	10	(111)	-	-	-	-	-	-	(101)
Ending balance	\$ 1,705	\$ 1,373	\$ 2,110	\$ 417	\$ 109	\$ 10	\$ 20	\$ 1	\$ 54	\$ 5,799
Ending balance: individually evaluated for impairment	-	-	538	-	-	-	-	-	-	538
Ending balance: collectively evaluated for impairment	\$ 1,705	\$ 1,373	\$ 1,572	\$ 417	\$ 109	\$ 10	\$ 20	\$ 1	\$ 54	\$ 5,261
Loans	\$ 192,168	\$ 133,432	\$ 87,649	\$ 59,801	\$ 13,540	\$ 5,068	\$ 2,319	\$ 297	\$ -	\$ 494,274
Ending balance: individually evaluated for impairment	2,198	854	1,496	-	-	-	-	-	-	4,548
Ending balance: collectively evaluated for impairment	\$ 189,970	\$ 132,578	\$ 86,153	\$ 59,801	\$ 13,540	\$ 5,068	\$ 2,319	\$ 297	\$ -	\$ 489,726

2015	Commercial real estate- multi family	Commercial real estate mortgages	Commercial and industrial loans	One-to- four family	Real estate- construction loans (in thousands)	Home equity lines of credit	Lease financing	Installment/ consumer loans	Unallocated	Total
Beginning balance	\$ 1,471	\$ 1,513	\$ 1,156	\$ 186	\$ 106	\$ 8	\$ 12	\$ 1	\$ -	\$ 4,453
Provision for loan losses	381	(131)	232	193	44	2	28	1	117	867
Charge-offs	-	(98)	-	-	-	-	(32)	-	-	(130)
Recoveries	-	5	58	-	-	-	15	-	-	78
Net charge-offs/recoveries	-	(93)	58	-	-	-	(17)	-	-	(52)
Ending balance	\$ 1,852	\$ 1,289	\$ 1,446	\$ 379	\$ 150	\$ 10	\$ 23	\$ 2	\$ 117	\$ 5,268
Ending balance: individually evaluated for impairment	-	-	127	-	-	-	-	-	-	127
Ending balance: collectively evaluated for impairment	\$ 1,852	\$ 1,289	\$ 1,319	\$ 379	\$ 150	\$ 10	\$ 23	\$ 2	\$ 117	\$ 5,141
Loans	\$ 187,885	\$ 121,330	\$ 70,630	\$ 54,277	\$ 19,970	\$ 4,217	\$ 2,505	\$ 966	\$ -	\$ 461,780
Ending balance: individually evaluated for impairment	2,215	878	1,810	-	-	-	-	-	-	4,903
Ending balance: collectively evaluated for impairment	\$ 185,670	\$ 120,452	\$ 68,820	\$ 54,277	\$ 19,970	\$ 4,217	\$ 2,505	\$ 966	\$ -	\$ 456,877

Troubled Debt Restructurings

A restructuring constitutes a troubled debt restructuring when the restructuring includes a concession by the Bank and the borrower is experiencing financial difficulty. In order to determine whether a borrower is experiencing financial difficulty, an evaluation is performed of the probability that the borrower will be in payment default on any of its debt in the foreseeable future without modification. The Bank performs the evaluation under its internal underwriting policy.

As of December 31, 2016 and 2015, the Corporation had a recorded investment in three troubled debt restructurings totaling \$2.5 million and \$2.8 million, respectively. The Corporation had allocated \$38 thousand and \$127 thousand of specific allowances for those loans at December 31, 2016 and 2015, respectively, and has not committed to lend additional amounts.

Based upon continued performance, one of the three troubled debt restructured loans, totaling \$2.2 million at December 31, 2016, is on accrual status.

During 2016 there was one new troubled debt restructuring, which consisted of a modification to a \$29 thousand commercial and industrial loan. There were no troubled debt restructurings for which there was a payment default during 2016 and 2015 that were modified during the twelve-month period prior to default. A loan is typically declared to be in payment default once it is contractually past due and reaches 90 days or it is deemed uncollectable under the modified terms.

To determine whether a borrower is experiencing financial difficulty, an evaluation is performed of the probability that the borrower will be in payment default on any of its debt in the foreseeable future without the modification. This evaluation is performed under the Bank's internal underwriting policy.

Past Due and Nonaccrual Loans

The following table presents the recorded investment in nonaccrual and loans past due over 90 days still on accrual by class of loans as of December 31, 2016 and 2015:

	2016		2015	
	Loan Past Due Over 90 Days still		Loan Past Due Over 90 Days still	
	Nonaccrual	Accruing	Nonaccrual	Accruing
	(in thousands)			
Commercial real estate- multi-family	\$ -	\$ -	\$ -	\$ -
Commercial real estate mortgages	854	-	-	-
Commercial and industrial loans	1,496	-	548	100
One-to-four family	-	-	-	-
Real estate - construction loans	-	-	-	-
Home equity lines of credit	-	-	-	-
Lease financing	-	-	-	-
Installment/consumer loans	-	-	-	-
Total	<u>\$ 2,350</u>	<u>\$ -</u>	<u>\$ 548</u>	<u>\$ 100</u>

The following table presents information related to impaired loans by class of loans as of and for the year ended December 31, 2016 and 2015:

	December 31, 2016				
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
	(in thousands)				
With no related allowance recorded:					
Commercial real estate-multi family	\$ 2,198	\$ 2,258	\$ -	\$ 2,278	\$ 160
Commercial real estate mortgages	854	854	-	866	53
Commercial and industrial loan	-	-	-	-	-
Subtotal	<u>3,052</u>	<u>3,112</u>	<u>-</u>	<u>3,144</u>	<u>213</u>
With an allowance recorded:					
Commercial and industrial loan	1,496	1,732	538	1,873	60
Subtotal	<u>1,496</u>	<u>1,732</u>	<u>538</u>	<u>1,873</u>	<u>60</u>
Total	<u>\$ 4,548</u>	<u>\$ 4,844</u>	<u>\$ 538</u>	<u>\$ 5,017</u>	<u>\$ 273</u>
	December 31, 2015				
	(in thousands)				
With no related allowance recorded:					
Commercial real estate-multi family	\$ 2,215	\$ 2,430	\$ -	\$ 2,302	\$ 201
Commercial real estate mortgages	878	878	-	877	50
Commercial and industrial loan	1,259	1,259	-	1,200	60
Subtotal	<u>4,352</u>	<u>4,567</u>	<u>-</u>	<u>4,379</u>	<u>311</u>
With an allowance recorded:					
Commercial and industrial loan	551	746	127	849	1
Subtotal	<u>551</u>	<u>746</u>	<u>127</u>	<u>849</u>	<u>1</u>
Total	<u>\$ 4,903</u>	<u>\$ 5,313</u>	<u>\$ 127</u>	<u>\$ 5,228</u>	<u>\$ 312</u>

The Corporation categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt such as current financial information, historical payment experience, credit documentation,

public information, and current economic trends, among other factors. The Corporation analyzes loans individually by rating the loans based on credit risk. A loan is assigned a risk rating as part of the underwriting process. A risk rating for a loan is reviewed periodically in conjunction with annual credit reviews, external loan review or when one or more events occur such as an event requiring credit approval, changes to an existing credit facility or whenever material favorable or unfavorable information regarding the credit is obtained. The Corporation uses the following definitions for risk ratings:

Pass - Non-criticized and non-classified asset.

Special Mention - A special mention asset has potential weaknesses that deserve management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the asset, or, in the institutions credit position at some future date. Special mention assets are not adversely classified and do not expose an institution to sufficient risk to warrant adverse classification. A special mention loan is not a "classified" asset.

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

Doubtful - An asset classified as doubtful has all the weaknesses inherent in one classified substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable.

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

The following tables present risk grades and classified loans by class of loans as of December 31, 2016 and 2015. Classified loans included loans in risk categories of Pass, Special Mention, Substandard, Doubtful and Loss.

	December 31, 2016				
	Pass	Special Mention	Sub- standard	Doubtful	Loss
	(in thousands)				
Commercial real estate - multi-family	\$ 189,970	\$ 2,198	\$ -	\$ -	\$ -
Commercial real estate mortgages	128,334	2,403	2,695	-	-
Commercial and industrial loans	82,523	1,926	3,200	-	-
One-to-four family	59,801	-	-	-	-
Real estate - construction loans	13,540	-	-	-	-
Home equity lines of credit	5,068	-	-	-	-
Lease financing	2,319	-	-	-	-
Installment/consumer loans	297	-	-	-	-
	\$ 481,852	\$ 6,527	\$ 5,895	\$ -	\$ -

	December 31, 2015 ⁽¹⁾				
	Pass	Special Mention	Sub- standard	Doubtful	Loss
	(in thousands)				
Commercial real estate - multi-family	\$ 187,885	\$ -	\$ -	\$ -	\$ -
Commercial real estate mortgages	118,072	469	2,789	-	-
Commercial and industrial loans	67,695	686	2,249	-	-
One-to-four family	54,277	-	-	-	-
Real estate - construction loans	19,970	-	-	-	-
Home equity lines of credit	4,217	-	-	-	-
Lease financing	2,505	-	-	-	-
Installment/consumer loans	966	-	-	-	-
	\$ 455,587	\$ 1,155	\$ 5,038	\$ -	\$ -

(1) Prior year loan amounts are shown net of deferred costs to conform to the current year presentation.

Two substandard commercial and industrial loans totaling \$1.3 million were modified subsequent to year end and were deemed impaired and to be troubled debt restructurings. Three substandard commercial and industrial loans totaling \$1.2 million were paid off subsequent to year end.

Related Party Loans

Certain directors and their related parties, including their immediate families and companies in which they are principal owners, were loan customers of the Corporation during 2016. The balance of related party loans for the years ended December 31, 2016 and December 31, 2015 were \$7.6 million and \$5.9 million, respectively. There were no loans to directors or executive officers that were nonaccrual at December 31, 2016.

Loans to principal officers, directors, and their affiliates during 2016 were as follows:

	<u>2016</u>
	(in thousands)
Beginning Balance:	\$ 5,922
New loans	121
Advances on existing lines	2,429
Paydowns	(845)
Ending Balance	<u>\$ 7,627</u>

4. PREMISES AND EQUIPMENT

Premises and equipment consisted of:

	<u>December 31,</u>	
	<u>2016</u>	<u>2015</u>
	(in thousands)	
Furniture and fixtures	\$ 6,516	\$ 6,154
Leasehold improvements	<u>7,060</u>	<u>7,045</u>
	13,576	13,199
Less: accumulated depreciation and amortization	<u>(7,524)</u>	<u>(6,512)</u>
	<u>\$ 6,052</u>	<u>\$ 6,687</u>

Depreciation and amortization expense was \$1.1 million and \$1.0 million for 2016 and 2015, respectively.

Leases

The Corporation is obligated to make minimum annual rental payments under non-cancelable operating leases on its premises. Projected minimum rentals under existing leases are as follows:

	<u>December 31, 2016</u>
	(in thousands)
2017	\$ 1,210
2018	1,265
2019	1,294
2020	1,299
2021	1,329
Thereafter	12,066

Certain leases contain renewal options and rent escalation clauses. In addition, certain leases provide for additional payments based upon real estate taxes, interest and other charges. Rental expenses under these leases for the years ended December 31, 2016 and 2015 approximated \$1.1 million and \$1.0 million, respectively. The above chart includes the minimum annual rental payments through lease renewal periods based upon management's intentions to execute the renewal options.

5. DEPOSITS

Time Deposits

The following table sets forth the remaining maturities of the Corporation's time deposits at December 31, 2016:

	<u>Less than</u> <u>\$100,000</u>	<u>\$100,000 or</u> <u>Greater</u>	<u>Total</u>
	(in thousands)		
2017	\$ 5,449	\$ 15,122	\$ 20,571
2018	3,038	1,555	4,593
2019	384	251	635
2020	400	487	887
2021	155	258	413
Thereafter	-	395	395
	<u>\$ 9,426</u>	<u>\$ 18,068</u>	<u>\$ 27,494</u>

The total amounts of time deposits that meet or exceed the FDIC insurance limit of \$250,000 at December 31, 2016 and 2015 were \$6.2 million and \$6.7 million, respectively. The total amounts of brokered deposits at December 31, 2016 and 2015 were \$108.5 million and \$93.1 million, respectively. Deposits from principal officers, directors, and their affiliates at year-end 2016 and 2015 were \$17.3 million and \$17.5 million, respectively.

6. SHORT-TERM BORROWINGS

At December 31, 2016, the Corporation had \$26.5 million of short-term borrowings outstanding with the Federal Home Loan Bank ("FHLB") at a rate of 0.74% with a maturity date of January 3, 2016. FHLB advances were collateralized by a blanket lien on commercial mortgages with a lendable value of \$232.8 million at December 31, 2016 and \$234.1 million at December 31, 2015.

During 2016, the Bank maintained an overnight line of credit with the FHLB. The Bank has the ability to borrow against its unencumbered mortgages and investment securities owned by the Bank.

As a member of the Federal Reserve Bank, the Bank may borrow on a collateralized basis at the discount window. There were no borrowings from the discount window at December 31, 2016.

At December 31, 2016, the Bank had aggregate lines of credit of \$23.0 million with unaffiliated correspondent banks to provide short-term credit for liquidity requirements. Of these aggregate lines of credit, \$19.0 million were available on an unsecured basis. As of December 31, 2016, the Bank had no such borrowings outstanding.

7. SUBORDINATED DEBENTURES

In December 2015, the Corporation issued \$15.3 million in aggregate principal amount of fixed and fixed-to-floating rate subordinated debentures ("Notes"). \$7.5 million of the Notes have a stated maturity of December 17, 2025 and bear interest at a fixed annual rate of 7.375% per year, from and including December 17, 2015 up to but excluding December 17, 2025. The fixed rate Notes are subject to redemption beginning on December 17, 2020 at an amount equal to 103% of the principal amount outstanding, plus accrued and unpaid interest, with the redemption premium decreasing by 50 basis points on each subsequent anniversary. The remaining \$7.75 million of the Notes have a stated maturity of December 17, 2025 and bear interest at a rate of 6.50% per year, from and including December 17, 2015 up to but excluding December 20, 2020. From and including December 20, 2020 to the maturity date or early redemption date, the interest rate will reset quarterly to an annual interest rate equal to the then-current three-month LIBOR plus 488 basis points. The fixed-to-floating Notes are subject to redemption beginning on December 17, 2020 at par. The fixed and fixed-to-floating Notes are subject to redemption under certain limited circumstances at par prior to December 17, 2020. The Notes were structured to qualify as Tier 2 capital under Federal Reserve regulations.

The Notes are recorded net of unamortized issuance costs of \$515 thousand and \$553 thousand at December 31, 2016 and December 31, 2015, respectively.

8. INCOME TAXES

Income tax expense (benefit) was as follows:

	For the years ended December 31,	
	2016	2015
	(in thousands)	
Current:		
Federal	\$ 1,973	\$ 1,666
State and local		-
	<u>1,973</u>	<u>1,666</u>
Deferred:		
Federal	(419)	(245)
State and local	(920)	(264)
	<u>(1,339)</u>	<u>(509)</u>
Change in valuation allowance	920	264
Total	<u>\$ 1,554</u>	<u>\$ 1,421</u>

The reconciliation of the expected federal income tax expense at the statutory tax rate to the actual provision follows:

	For the years ended December 31,			
	2016		2015	
	Amount	Percentage of Pre-tax Earnings	Amount	Percentage of Pre-tax Earnings
	(dollars in thousands)			
Federal income tax benefit computed by applying the statutory rate to income before income taxes	\$ 1,477	34 %	\$ 1,344	34 %
State and local tax, net of federal	(920)	(21)	(264)	(5)
Incentive stock options	13	-	15	-
Other	64	2	62	2
Valuation allowance	920	21	264	5
Provision for income taxes	<u>\$ 1,554</u>	<u>36 %</u>	<u>\$ 1,421</u>	<u>36 %</u>

Deferred tax assets and liabilities are comprised of the following:

	<u>For the year ended December 31,</u>	
	<u>2016</u>	<u>2015</u>
	(in thousands)	
Deferred tax assets:		
Allowance for loan losses	\$ 2,298	\$ 2,075
NYS and NYC net operating loss	927	57
Organizational and start-up costs	430	506
Nonqualified stock options	240	243
Deferred rent expense	769	726
Nonaccrual loan interest income	104	83
Stock compensation	83	-
Other	237	223
Net unrealized loss on available for sale securities	<u>2,704</u>	<u>491</u>
	7,792	4,404
Deferred tax liabilities:		
Net deferred loan costs	(499)	(504)
Depreciation	(33)	(210)
Other	<u>(88)</u>	<u>(69)</u>
	(620)	(783)
Valuation allowance	(1,570)	(650)
Net deferred tax asset	<u>\$ 5,602</u>	<u>\$ 2,971</u>

At year-end 2016, the Company had no federal net operating loss carryforwards. The Company also had New York State and New York City net operating loss carryforwards of \$10.7 million and \$5.8 million, respectively, which expire at various dates from 2035 to 2036. Deferred tax assets are not recognized for New York State and New York City net operating losses as the benefit of such losses is not more likely than not to be realized.

Due to legislation enacted in 2014 and 2015, the Corporation will not be in a taxable income position for the foreseeable future in New York State and New York City. As a result, we determined that it was not more likely than not that we would be able to utilize state and city deferred tax assets. Accordingly, the Corporation maintains a valuation allowance against all state and city deferred tax assets. We believe that the revisions to the New York State and New York City corporate income tax laws will continue to decrease our future state and local income tax liability.

At December 31, 2016 and December 31, 2015, the Corporation had no unrecognized tax benefits. The Corporation does not expect the amount of unrecognized tax benefits to significantly change within the next twelve months. The Corporation is not currently under Federal or New York State audit.

The Corporation is subject to U.S. federal and New York state income tax. The tax years 2012 through 2016 remain open to examination by the Internal Revenue Service and 2013 through 2016 by New York State.

9. STOCKHOLDERS' EQUITY

On December 19, 2014, the Corporation completed a private placement of its capital stock, generating \$18.7 million in net proceeds from the sale of 1,343,750 shares of common stock and 1,156,250 shares of Series A preferred stock at a price of \$8.00 per share. In September 2015, following the effectiveness of an amendment to the Corporation's certificate of incorporation authorizing a class of non-voting common stock, all shares of Series A preferred stock were converted on a one-for-one basis to shares of non-voting common stock.

The non-voting common stock is mandatorily convertible into voting common stock of the Corporation on a one-for-one basis upon (i) the consummation of the transfer by a holder of non-voting common stock to third parties in a

widely dispersed offering or (ii) in the case of an investor whose ownership of the common stock issuable upon a proposed conversion is conditioned upon the execution of passivity commitments in a form acceptable to the Board of Governors of the Federal Reserve System (acting itself or on delegated authority), upon the execution of such passivity commitments. Holders of non-voting common stock have no voting rights, except as required by law.

During 2016, 775 thousand shares of common stock were converted to non-voting common stock.

10. EMPLOYEE BENEFITS

401(K) Plan

The Corporation participates in a contributory retirement and savings plan, which meets the requirements of Section 401(k) of the Internal Revenue Code and covers substantially all current employees. Newly hired employees can elect to participate in the savings plan after completing one year and 1,000 hours of service. Under the provisions of the savings plan, employee contributions are partially matched by the Corporation with cash contributions. Participants can invest their account balances into several investment alternatives. As of December 31, 2016, the savings plan did not allow for investment in the common stock of the Corporation. During the years ended December 31, 2016 and 2015, the Corporation recorded compensation expense related to the plan of approximately \$158 thousand and \$237 thousand, respectively.

Stock Based Compensation

The Corporation maintains the Empire National Bank 2008 Stock Incentive Plan (“2008 Plan”), which authorizes the issuance of an aggregate of 600,000 stock options to such individuals and in such amounts as may be designated by the Board of Directors or its Compensation Committee. This plan provides for the issuance of “incentive stock options” and “nonqualified stock options” to certain qualified individuals. All stock options issued by the Bank prior to the holding company reorganization transaction were assumed by the Corporation as of the effective date of the reorganization. All stock options that have been issued under the plan have a ten-year term and vest at a rate of twenty percent on each of the first five annual anniversary dates from the date of grant. Each option entitles the holder to purchase one share of the Corporation’s common stock at an exercise price not less than fair market value at the time of issuance. Upon the effectiveness of the 2015 Plan discussed below, no further awards have been issued under this plan.

In 2015, the Empire Bancorp, Inc. 2015 Omnibus Stock and Incentive Plan (“2015 Plan”) was adopted, effective May 21, 2015. The plan provides for the issuance of stock options, restricted stock, restricted stock units, stock appreciation rights and other cash and equity-based awards to qualified persons. During 2016, 60,732 restricted stock awards were granted to non-employee directors and employees under the plan.

Stock Options

A summary of the status of the Corporation’s stock options as of December 31, 2016 follows:

	Number of Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life	Aggregate Intrinsic Value
Outstanding, beginning of year	444,000	\$ 10.00		
Granted	-	-		
Exercised	5,800	-		
Forfeited	1,700	\$ 10.00		
Outstanding, end of year	<u>436,500</u>	\$ 10.00	1.70 years	\$ 1,196,010
Exercisable, end of year	426,200	\$ 10.00	1.61 years	\$ 1,167,788
Vested or expected to vest	436,500	\$ 10.00	1.70 years	\$ 1,196,010
	<u>Number of Shares</u>	<u>Price</u>		
Range of exercise prices	436,500	\$ 10.00		

All options shown on the table above vest ratably over five years beginning one year from the date of grant and have a ten-year duration. Compensation expense attributable to these options was \$37 thousand and \$44 thousand for the years ended December 31, 2016 and 2015, respectively. As of December 31, 2016, there were \$20 thousand of total unrecognized compensation costs related to nonvested stock options granted under the Plan. The cost is expected to be recognized in full during 2017.

A summary of activity related to the stock options follows:

	<u>December 31,</u>	
	<u>2016</u>	<u>2015</u>
	(in thousands)	
Intrinsic value of options exercised	\$ 16	\$ -
Cash received from options exercised	58	-
Tax benefit realized from option exercised	-	-
Weighted average fair value of options granted	-	-

Restricted Stock Awards

The 2015 Omnibus Plan provides for the issuance of shares to directors and officers. Compensation expense is recognized over the vesting period of the awards based on the fair value of the stock at issue date. The fair value of the stock was determined using the fair value on the date of the grant. Of the shares granted in 2016, 37,990 shares vest ratably over five years. The balance of shares totaling 22,742 shares vest over one year. Total shares issuable under the plan are 241,268 at year-end 2016 and 60,732 shares were issued in 2016. Such shares are subject to restrictions based on continued service as employees of the Corporation or its subsidiaries.

A summary of the status of the Corporation's shares of unvested restricted stock for the year ended December 31, 2016 follows:

	<u>Shares</u>	<u>Weighted</u>
		<u>Average</u>
		<u>Grant-Date</u>
		<u>Fair Value</u>
Unvested, January 1, 2016	-	-
Granted	60,732	\$ 9.21
Vested	-	-
Forfeited	-	-
Unvested, December 31, 2016	<u>60,732</u>	\$ 9.21

Compensation expense attributable to these awards was approximately \$245 thousand for the year ended December 31, 2016. The total fair value of shares nonvested during the years ended December 31, 2016 was \$559 thousand. As of December 31, 2016, there was \$314 thousand of total unrecognized compensation costs related to non-vested restricted stock awards granted under the Plan. This cost is expected to be recognized over a weighted-average period of 2.60 years.

11. WARRANTS

At December 31, 2016, the Corporation had 594,376 warrants issued and outstanding. Of this amount, 307,500 warrants were issued by the Bank at inception to the members of its organizational group in exchange for amounts advanced during the organizational stage. Additionally, 57,500 warrants were issued by the Bank at inception to two vendors in exchange for services rendered in connection with the Bank's organization. Each of the warrants originally issued by the Bank was assumed by the Corporation at the time of the holding company reorganization, has an exercise price of \$10.00 per share and is exercisable through February 24, 2018. These warrants may be subject to exercise or forfeiture in the event that the Corporation's capital levels have fallen below regulatory minimums (or higher levels as the regulatory agencies may determine). On December 19, 2014, the Corporation issued a total of 229,376 warrants to certain institutional investors as a part of their respective equity investments in

the Corporation made on the same date. These warrants have an exercise price of \$9.00 per share and a term of five years from the grant date. At December 31, 2016 the issued and outstanding warrants have an aggregate intrinsic value of \$1.9 million.

12. EARNINGS PER SHARE

The restricted stock awards and certain restricted stock units granted by the Company contain non-forfeitable rights to dividends and therefore are considered participating securities. The two-class method for calculating basic EPS excludes dividends paid to participating securities and any undistributed earnings attributable to participating securities.

The following is a reconciliation of earnings per share for December 31, 2016 and 2015.

	For the years ended December 31,	
	2016	2015
	(in thousands, except per share data)	
Net income	\$ 2,790	\$ 2,534
Earnings allocated to participating securities	(23)	-
Income attributable to common stock	<u>\$ 2,767</u>	<u>\$ 2,534</u>
Weighted average common shares outstanding, including participating securities	6,936,561	6,100,689
Weighted average participating securities	(56,338)	-
Weighted average common shares outstanding	<u>6,880,223</u>	<u>6,100,689</u>
Basic earnings per share	<u>\$ 0.40</u>	<u>\$ 0.42</u>
Income attributable to common stock	<u>\$ 2,767</u>	<u>\$ 2,534</u>
Weighted average common shares outstanding	6,880,223	6,100,689
Incremental shares from conversions of Series A Convertible Preferred Stock	-	779,281
Incremental shares from conversion of stock warrants	19,432	-
Weighted average common shares outstanding	<u>6,899,655</u>	<u>6,879,970</u>
Diluted earnings per share	<u>\$ 0.40</u>	<u>\$ 0.37</u>

There are 436,500 options and 365,000 warrants outstanding at December 31, 2016 that were not included in the computation of diluted earnings per share because the exercise prices were greater than the average market price of common stock and were, therefore, antidilutive.

13. OTHER OPERATING EXPENSES

Expenses included in other operating expenses that exceed one percent of the aggregate of total interest income and noninterest income in the years shown are as follows:

	<u>2016</u>	<u>2015</u>
	(in thousands)	
Directors Compensation	\$ 531	\$ 356

14. COMMITMENTS, CONTINGENCIES AND OTHER MATTERS

In the normal course of business, the Corporation has various outstanding commitments and contingent liabilities, such as claims and legal actions, minimum annual rental payments under non-cancelable operating leases, guarantees and commitments to extend credit, which are not reflected in Corporation's financial statements. No material losses are anticipated as a result of these actions or claims.

Loan Commitments

Some financial instruments, such as loan commitments, credit lines, letters of credit, and overdraft protection, are issued to meet customer financing needs. These are agreements to provide credit or to support the credit of others, as long as conditions established in the contract are met, and usually have expiration dates. Commitments may expire without being used. Off-balance-sheet risk to credit loss exists up to the face amount of these instruments, although material losses are not anticipated. The same credit policies are used to make such commitments as are used for loans, often including obtaining collateral at exercise of the commitment.

The following represents commitments outstanding:

	December 31,			
	2016		2015	
	Fixed Rate	Variable Rate	Fixed Rate	Variable Rate
	(in thousands)			
Standby letters of credit	\$ 1,544	\$ 1,755	\$ 1,303	\$ 172
Commercial letters of credit	-	-	-	-
Unused loan commitments	-	63,424	150	61,390
Commitments to make loans	796	17,200	-	8,749
Total commitments outstanding	<u>\$ 2,340</u>	<u>\$ 82,379</u>	<u>\$ 1,453</u>	<u>\$ 70,311</u>

15. ESTIMATED FAIR VALUE MEASUREMENTS

FAS ASC, “*Fair Value Measurements and Disclosures*,” establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair value:

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

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

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

The fair values of securities available for sale are determined by obtaining quoted prices on nationally recognized securities exchanges (Level 1 inputs) or matrix pricing, which is a mathematical technique widely used within the industry to value debt securities without relying exclusively on quoted prices for the specific securities but rather by relying on the securities’ relationship to other benchmark quoted securities (Level 2 inputs).

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

Fair Value Measurements at December 31, 2016 using:				
Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total	
(in thousands)				
Assets:				
Mortgage-backed securities-residential	\$ -	\$ 139,385	\$ -	\$ 139,385
U.S government agency securities	-	125,349	-	125,349
Total	\$ -	\$ 264,734	\$ -	\$ 264,734
Fair Value Measurements at December 31, 2015 using:				
Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total	
(in thousands)				
Assets:				
Mortgage-backed securities-residential	\$ -	\$ 80,418	\$ -	\$ 80,418
U.S government agency securities	-	70,625	-	70,625
Total	\$ -	\$ 151,043	\$ -	\$ 151,043

At December 31, 2016 and 2015, there were no material impaired loans carried at fair value.

As of December 31, 2016 and 2015, the carrying amounts and estimated fair values of financial instruments, not previously presented, were as follows:

	Level of Fair Value Hierarchy	December 31, 2016	
		Carrying Amount	Fair Value
(in thousands)			
Financial assets:			
Cash and cash equivalents	Level 1	\$ 6,354	\$ 6,354
Securities, restricted	Level 1	4,131	n/a
Loans	Level 3	488,475	482,906
Accrued interest receivable:			
Investment securities	Level 2	1,018	1,018
Loans	Level 3	1,592	1,592
Financial liabilities:			
Demand, savings, N.O.W. and money market deposits	Level 1	\$ 643,189	\$ 643,189
Certificates of deposits of \$100,000 or more and other time deposits	Level 2	27,494	27,453
Short-term borrowings	Level 1	26,477	26,477
Subordinated debentures	Level 3	14,735	15,342
Accrued interest payable:			
Demand, savings, N.O.W. and money market deposits	Level 1	12	12
Certificates of deposits of \$100,000 or more and other time deposits	Level 2	66	66
Subordinated debentures	Level 3	32	32

	Level of Fair Value Hierarchy	December 31, 2015	
		Carrying Amount	Fair Value
(in thousands)			
Financial assets:			
Cash and cash equivalents	Level 1	\$ 5,621	\$ 5,621
Securities, restricted	Level 1	3,712	n/a
Loans	Level 3	456,512	451,619
Accrued interest receivable:			
Investment securities	Level 2	479	479
Loans	Level 3	1,416	1,416
Financial liabilities:			
Demand, savings, N.O.W. and money market deposits	Level 1	\$ 475,835	\$ 475,835
Certificates of deposits of \$100,000 or more and other time deposits	Level 2	42,198	42,052
Short-term borrowings	Level 1	26,064	26,064
Subordinated debentures	Level 3	14,697	14,697
Accrued interest payable:			
Demand, savings, N.O.W. and money market deposits	Level 1	8	8
Certificates of deposits of \$100,000 or more and other time deposits	Level 2	79	79
Subordinated debentures	Level 3	44	44

The carrying amounts of cash and cash equivalents approximate fair values and are classified as Level 1. It is not practical to determine the fair value of restricted securities due to restrictions placed on its transferability. The fair value of loans is computed by calculating the new present value of estimated future cash flows using the current rates at which similar loans would be made to borrowers with similar credit ratings and for the remaining maturities and terms, resulting in a Level 3 classification. The fair values disclosed for demand, savings, N.O.W. and money market deposits are, by definition, equal to the amount payable on demand at the reporting date resulting in Level 1 classification. The fair value for certificates of deposit is computed by calculating the net present value of estimated future cash flows, using the current rates at which similar certificates of deposit would be issued to depositors, resulting in a Level 2 classification. The short term borrowings generally maturing within 90 days approximate their fair values resulting in a Level 2 classification. For accrued interest receivable and payable, the recorded book value is a reasonable estimate of fair value and the fair value level follows the underlying contract.

16. REGULATORY MATTERS

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios (set forth in the following table) of total and tier 1 capital to risk weighted assets, common equity tier 1 risk-based capital ratio, and of tier 1 capital to average assets, as those terms are defined in applicable OCC regulations.

Banks and bank holding companies are subject to regulatory capital requirements administered by federal banking agencies. Capital adequacy guidelines and, additionally for banks, prompt corrective action regulations, involve quantitative measures of assets, liabilities, and certain off-balance-sheet items calculated under regulatory accounting practices. Capital amounts and classifications are also subject to qualitative judgments by regulators. Failure to meet capital requirements can initiate regulatory action. The final rules implementing Basel Committee on Banking Supervision's capital guidelines for U.S. banks (Basel III rules) became effective for the Bank on January 1, 2015 with full compliance with all of the requirements being phased in over a multi-year schedule, and fully phased in by January 1, 2019. Under the Basel III rules, the Company must hold a capital conservation buffer above the adequately capitalized risk-based capital ratios. The capital conservation buffer is being phased in from 0.0% for 2015 to 2.50% by 2019. The capital conservation buffer for 2016 is 0.625%. The net unrealized gain or loss on available for sale securities is not included in computing regulatory capital. Management believes as of December 31, 2016, the Bank met all capital adequacy requirements to which they are subject.

As of December 31, 2016 and December 31, 2015, the Bank was classified as “well capitalized,” for purposes of the OCC’s prompt corrective action regulations. “Well capitalized” is the highest capital classification for FDIC-insured financial institutions in the United States. To be categorized as “well capitalized,” the Bank must maintain minimum total risk-based, tier 1 risk-based, tier 1 common equity risk-based and tier 1 leverage capital ratios as set forth in the table below.

The Bank’s actual capital amounts and ratios are presented in the following table:

As of December 31,	2016					
	Actual		To be Adequately Capitalized Under Prompt Corrective Action Provisions		To be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
	(dollars in thousands)					
Tier 1 leverage capital ratio	\$ 78,532	10.22 %	\$ 30,745	4.00 %	\$ 38,432	5.00 %
Common equity tier 1 risk-based capital ratio	78,532	16.26	21,733	4.50	31,392	6.50
Tier 1 risk-based capital ratio	78,532	16.26	28,978	6.00	38,637	8.00
Total risk-based capital ratio	84,334	17.46	38,637	8.00	48,296	10.00
	2015					
	(dollars in thousands)					
Tier 1 leverage capital ratio	\$ 74,670	12.22 %	\$ 24,444	4.00 %	\$ 30,556	5.00 %
Common equity tier 1 risk-based capital ratio	74,670	16.83	19,969	4.50	28,845	6.50
Tier 1 risk-based capital ratio	74,670	16.83	26,626	6.00	35,501	8.00
Total risk-based capital ratio	79,938	18.01	35,501	8.00	44,376	10.00

17. PARENT COMPANY ONLY CONDENSED FINANCIAL INFORMATION

Condensed parent company only financial information of Empire Bancorp, Inc. is shown below. The parent company has no significant operating activities.

CONDENSED STATEMENTS OF CONDITION

	At December 31,	
	2016	2015
	(in thousands)	
ASSETS		
Cash	\$ 4,472	\$ 5,222
Investment in the Bank	73,283	73,714
Other assets	43	28
Total Assets	\$ 77,798	\$ 78,964
LIABILITIES AND STOCKHOLDERS' EQUITY		
Subordinated debentures, net	\$ 14,735	\$ 14,697
Accrued interest payable	32	44
Other liabilities	39	69
Total Liabilities	14,806	14,810
Total Stockholders' Equity	62,992	64,154
Total Liabilities and Stockholders' Equity	\$ 77,798	\$ 78,964

CONDENSED STATEMENTS OF INCOME

	Year Ended December 31,	
	2016	2015
	(in thousands)	
Interest expense	\$ 1,092	\$ 46
Other expense	104	99
Loss before income taxes and equity in undistributed earnings of the Bank	(1,196)	(145)
Income tax benefit	407	49
Loss before equity in undistributed earnings of the Bank	(789)	(96)
Equity in undistributed earnings of the Bank	3,579	2,630
Net income	\$ 2,790	\$ 2,534

CONDENSED STATEMENTS OF CASH FLOWS

	Year Ended December 31,	
	2016	2015
	(in thousands)	
Operating activities:		
Net income	\$ 2,790	\$ 2,534
Adjustments to reconcile net cash (used by) provided by operating activities:		
Amortization of debt issuance costs	38	-
Equity in undistributed earnings of the Bank	(3,579)	(2,630)
(Increase) decrease in other assets	(15)	69
(Decrease) increase in accrued interest payable	(12)	44
Decrease in other liabilities	(30)	(82)
Net cash (used by) provided by operating activities	(808)	(65)
Investing activities:		
Investments in the Bank	-	(10,000)
Net cash used by investing activities	-	(10,000)
Financing activities:		
Proceeds from exercise of stock options	58	-
Net proceeds from issuance of subordinated debentures	-	14,697
Net cash provided by financing activities	58	14,697
Increase in cash and cash equivalents	(750)	4,632
Cash and cash equivalents at beginning of year	5,222	590
Cash and cash equivalents at end of year	\$ 4,472	\$ 5,222

INDEPENDENT AUDITOR'S REPORT

Board of Directors and Stockholders
Empire Bancorp, Inc.
Islandia, New York

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of Empire Bancorp, Inc., which comprise the consolidated statements of condition as of December 31, 2016 and 2015, and the related consolidated statements of operations, comprehensive (loss) income, stockholders' equity, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Empire Bancorp, Inc. as of December 31, 2016 and 2015, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Crowe Horwath LLP

Crowe Horwath LLP

New York, New York
March 30, 2017

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INVESTOR RELATIONS

Empire Bancorp, Inc. is a registered bank holding company for Empire National Bank. Empire Bancorp, Inc.'s common stock is listed on the OTCQB marketplace, which is the middle tier of the OTC market, under the symbol "EMPK." Empire National Bank is a Long Island-based independent bank that specializes in serving the financial needs of small and medium-sized businesses, professionals, nonprofit organizations, municipalities, real estate investors, and consumers. The bank has four full-service banking offices located in Islandia, Shirley, Port Jefferson Station and Mineola and a private banking branch office in Manhattan, New York. The bank takes pride in understanding the needs of each and every customer so that it can deliver the highest quality service with a sense of urgency.

Additional copies of Empire Bancorp, Inc.'s Annual Report can be obtained in PDF form from the Bank's website (www.empirenb.com) in the Investor Relations section.

INVESTOR RELATIONS DIRECTOR

William T. Franz, Senior Vice President

Islandia, NY
631-881-5375

LEGAL COUNSEL

Geoffrey Scot Kay

Fenimore, Kay, Harrison & Ford, LLP
Austin, TX

INDEPENDENT REGISTERED PUBLIC ACCOUNTANTS

Crowe Horwath LLP

New York, NY

TRANSFER AGENT

Broadridge Corporate Issuer Solutions, Inc.

Brentwood, NY
877-830-4936

BOARD OF DIRECTORS*



Douglas C. Manditch
Chairman of the Board &
Chief Executive Officer
Empire National Bank



Thomas M. Buonaiuto, CPA
President &
Chief Operating Officer
Empire National Bank



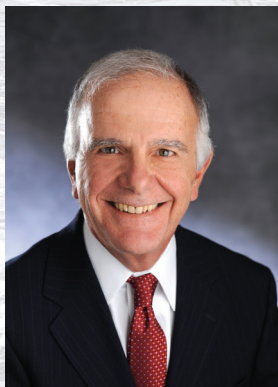
John D. Caffrey, Jr.
Organizer & Vice Chairman
of the Board
*Owner, Castle Financial
Advisors, LLC & Castle Asset
Management, LLC*



John P. Bracken, Esq.
Organizer & Director
*Managing Partner, Bracken
Margolin Besunder, LLP, Retired*



Francis F. Boulton
Organizer & Director
*CEO, Long Island Ducks
Professional Baseball Club, LLC*



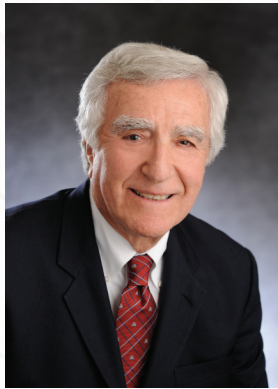
John L. Ciarelli, Esq.
Organizer & Director
*President, Ciarelli &
Dempsey P.C.*



Dr. Alan M. Coren
Organizer & Director
*President, West Hills Animal
Hospital P.C.*



Larry R. Davis, Esq.
Organizer & Director
Principal, Davis & Prager, P.C.



Frank A. DiFazio
Organizer & Director
President, Dekal Services, Inc.



Robert D. Falese, Jr.
Director
*Owner & President
Falese Investments, LLC*



Salvatore Ferro
Organizer & Director
*Owner, President/CEO,
Alure Home Improvements
& Alure Designs*



Mukeshkumar Patel
Organizer & Director
*Managing Member PSA Realty
Corp. DBA La Quinta Hotels &
Priya Hospitality LLC*



Charles C. Russo, Esq.
Organizer & Director
*Senior Partner, Russo Karl
Widmaier & Cordano, PLLC*



Joseph S. Tantillo, Jr.
Organizer & Director
*Founder & CEO, Nassau Suffolk
Electrical & Mechanical*



Paul J. Tonna
Organizer & Director
*Molloy College's Executive
Director for the Energeia
Partnership*



Jeffrey M. Weiner
Organizer & Director
Managing Partner, Marcum, LLP

*Each director serves on the Boards of Empire National Bank and Empire Bancorp, Inc.

EXECUTIVE TEAM

EMPIRE BANCORP, INC. EXECUTIVE OFFICERS

Douglas C. Manditch
Chairman of the Board, Chief Executive Officer & Secretary

John D. Caffrey, Jr.
Vice Chairman of the Board

Thomas M. Buonaiuto, CPA
President, Chief Operating Officer & Assistant Secretary

John Pinna
Vice President

Janet T. Verneuille, CPA
Vice President & Chief Financial Officer

Diane L. Murray, CPA
Assistant Secretary

EMPIRE NATIONAL BANK EXECUTIVE OFFICERS

Douglas C. Manditch
Chairman of the Board & Chief Executive Officer

Thomas M. Buonaiuto, CPA
President & Chief Operating Officer

Michael P. Locorriere
Executive Vice President & Director of Municipal Banking

Susanne Pheffer
Executive Vice President, Chief Technology Officer
& Security Officer

John Pinna
Executive Vice President & Chief Information Officer

Janet T. Verneuille, CPA
Executive Vice President & Chief Financial Officer

William T. Franz
Senior Vice President & Director of Marketing
& Investor Relations

Diane L. Murray, CPA
Senior Vice President & Chief Risk Officer

Raffaella Palazzo
Senior Vice President & Co-Chief Credit Officer

Matthew Ruppert
Senior Vice President & Co-Chief Credit Officer

Robert S. Schepis
Senior Vice President & Chief Lending Officer

SENIOR VICE PRESIDENTS

Craig Goldstein
Commercial Loan Officer

Dorothy Overton
Branch Manager, *Islandia*

VICE PRESIDENTS

Richard Corrado
Senior Credit Analyst

Frank DeRosa
Commercial Loan Officer

Danielle DiGrazia
Operations Officer

Catherine Giamundo, CPA
Controller

Erik Griemsmann
IT Manager

William Guiducci
Branch Manager, *Shirley*

Edy Meyer
Branch Manager, *Port Jefferson Station*

Steven Post
Electronic Banking Manager

Jane Reid
Human Resources

Jeffrey B. Reid
Commercial Loan Officer

Neil Roberts
Senior Credit Analyst

Marguerite Smith
BSA & Compliance Officer





EXECUTIVE OFFICERS Left to Right: Matthew Ruppert, Raffaella Palazzo, Michael P. Locorriere, William T. Franz, Thomas M. Buonaiuto, Douglas C. Manditch, Janet T. Verneuille, Diane L. Murray, Robert S. Schepis, Susanne Pheffer, John Pinna

ASSISTANT VICE PRESIDENTS

Linda Carman

Electronic Banking

Krista M. Classie

Branch Manager, *Mineola*

Tracey Cullen

Senior Credit Analyst

Jeanne M. Dahl

Assistant Branch Manager, *Port Jefferson Station*

Miranda M. D'Angelis

Assistant Controller

Margaret Downing

Assistant Branch Manager, *Shirley*

Gregory Durso

Senior Credit Analyst

Suzanne Fox

Assistant Branch Manager, *Islandia*

Nancy Leonard

Deposit Operations

Yi Lu

Loan Administration

Deborah McCullough

Assistant Branch Manager, *Mineola*

Jessica M. Michalski

Staff Accountant

Janet Weissman

Assistant Branch Manager, *Islandia*

MANAGERS ASSISTANT BRANCH MANAGERS

Dorothy Lamboy

Assistant Branch Manager, *Shirley*

Theresa Naumann

Assistant Branch Manager, *Shirley*

Sueann Rando

Assistant Branch Manager, *Port Jefferson Station*

PRIVATE BANKING

Michael Wilk

Private Banking Officer

FINANCE

Andrew Meltzer

Accounting Officer

BRANCH LOCATIONS



ISLANDIA

Headquarters

1707 Veterans Highway
Islandia, NY 11749
631-348-4444



MINEOLA

170 Old Country Road, Suite 1WA
Mineola, NY 11501
516-741-0444



PORT JEFFERSON STATION

4747 Nesconset Highway, Unit 36
Port Jefferson Station, NY 11776
631-928-4444



SHIRLEY

1044 William Floyd Parkway
Shirley, NY 11967
631-395-9500



MANHATTAN

99 Park Ave, Suite 1510
New York, NY 10016
212-986-4444

SUPPORTING OUR COMMUNITY

We are well aware that a large part of our success is tied to the strength of the local economy. As a community bank, we embrace our position within each community and look to facilitate helping businesses and individuals grow and prosper.

Our commitment to community is in everyone's best interest. We are proud to work with so many important, local organizations.

Association for Children with Down Syndrome
Advancement for Commerce Industry and Technology
ADDAPT
AHRC Suffolk
ALS Ride for Life
Alzheimer's Foundation of America
American Diabetes Association
American Kidney Foundation
American Heart Association
Ancient Order of Hiberians
Angela's House
Arthritis Foundation - LI Chapter
Boy Scouts of America
Bonei Olam
Central Nassau Guidance & Counseling
Chamber of Commerce Shirley & The Mastics
Children's Medical Fund of NY
Child Care Council of Suffolk, Inc.
Christmas Magic, Inc.
Clark Gilles Foundation

Colonial Youth & Family Services
Commack Gridiron Club
Community Library Friends of the Arts
Community Family Literacy Project
Community Mainstreaming Associates
Comsewogue Youth Lacrosse
Cooley's Anemia Foundation, Inc.
Crohn's & Colitis Foundation of America
Doc Fallot Scholarship Fund
East End Arts & Humanities Council, Inc.
Eden II and Genesis Foundation
EMI Network
Enegeia Partnership at Molloy College
Family Service League
Father John Papallo Lodge
Federation of Organizations
Feed The Children
Friends and Family of Chris Barnes
The Fuoco Memorial Golf Festival
Garden City Chamber of Commerce, Inc.

Girl Scouts of Suffolk County
Great River Fire Department
Half Hollow Hills East
Hauppauge Eagles Lacrosse Booster
Hauppauge Industrial Association
Hauppauge Public Schools
Hofstra University
Holocaust Memorial and Tolerance Center
Hope House Ministries
Interfaith Nutrition Network
Island Harvest
James V. Kavanaugh Knights of Columbus
JTM Foundation
The Jewish Academy
Jocelyn's Operation Holiday Spirit
The Kelly Memorial Charitable Fund
Kiwanis Club of the Mastics
Lions Club of Medford - N. Patchogue
Long Island Council on Alcoholism and Drug Dependence
Long Island Against Domestic Violence

Long Island Against Trafficking	Nassau Suffolk Chapter of Autism	Steven Antaki Memorial Golf Outing
Long Island Builders Institute, Inc.	New Ground, Inc.	Stony Brook Foundation
Long Island Childrens Museum	Never Alone Never Afraid	Suffolk County Fire District
Long Island Convention & Visitors Bureau	North Shore Child & Family Guidance	Suffolk Sports Hall of Fame
Long Island Hispanic Chamber of Commerce	NYOSIA Grand Lodge Foundation, Inc.	Telecare
Long Island Imagine Awards	Our Lady Queen of Apostles	The Paul Conroy Foundation
Long Island Museum of American Art, History and Carriages	Outreach	Theodore Roosevelt Association
Long Island Village Clerks & Treasurer Association	Pal-O-Mine Equestrian, Inc.	Three Village Kiwanis / SEPTA
Lustraten Foundation	Port Jefferson Yacht Club	United Veterans Beacon House
Mandy's Mark Memorial Golf Outing	Public Library Directors Association	United Way of Long Island
Marcum Workplace Challenge	The Richard J. O'Brien Foundation	Viscardi Center
Mastic Beach Yacht Club	Rotary Club of the Patchogue	Ward Melville Heritage Organization
Mastic Fire Department	Rotary Club of the Ronkonkomas	William Floyd Alumni Association
Maurer Foundation	Rotary Club of Shirley & The Mastics	William Floyd Community Summit
Mercy Haven, Inc.	Shanti Fund	William Floyd Scholarship Fund & H.S.
Michael McCarthy Foundation	Smithtown Booster Club	YMCA of Long Island, Inc.
Middle Country Library Foundation	Shootout for Soldiers	
Miller Place Athletic Booster Club	St. Baldrick's Foundation	
Miller Place Lacrosse	St. Charles Hospital Foundation	
	St. Jude R.C. Church	
	St. Louis De Monfort Church	



HEADQUARTERS

1707 Veterans Highway

Islandia, NY 11749

631-348-4444

empirenb.com

