BEO Bancorp and Subsidiary

Consolidated Financial Statements

With Independent Auditor's Report

Years Ended December 31, 2018 and 2017

C O N T E N T S

BEO BANCORP
P.O. BOX 39 Heppner, OR 97836 Administrative Office: 279 N. Main Heppner, OR 97836 Phone: (541) 676-0201

Message to our stockholders

Enclosed you will find the consolidated financial statements and operating results of BEO Bancorp and Bank of Eastern Oregon for 2018.

2018 was a good year for your Bank. Consolidated net income was the highest level on record, influenced by a strong net interest margin and the lower corporate tax rate signed into law late in 2017. Consolidated after tax net income for BEO Bancorp was $3,949,000 up 27.6% from 2017. Return on Average Assets (ROAA) for 2018 was 0.95% compared to 0.78% in 2017. Return on Average Equity came in at 11.91% compared to 10.06% in 2017. Net earnings per share were $3.33 in 2018 compared to $2.60 in 2017.

Dividend payout in 2018 was $1,006,148; the first time that we have returned over $1 million (in a single year) to our shareholders. This equates to $0.85 per share.

Stockholders' equity grew 9.0% in 2018 to $34.58 million; Deposits were down modestly (-0.7%) at $368.2 million; while net loans increased slightly (+1.8%) to $324.6 million. Total assets increased 0.5% to $416.6 million.

Your Bank continues to expand its footprint. In 2018 we opened a new loan production office in Dayton, WA and announced during 4th quarter our agreement to purchase 4 branches from Umpqua Bank. The branches will continue our expansion into eastern Washington. The new branches are in Colfax, Dayton, LaCrosse, and Pomeroy. The deal will close in 1st quarter 2019.

As shareholders in BEO Bancorp, thank you for your continued investment. Record profitability and dividends, strong capital position, and expansion into new markets, only come about with the hard work and support of you as shareholders, customers, and a dedicated effort by a fantastic group of employees. These people are our most important asset and I thank them for their continued work to make your Bank successful and be crucial members of the communities we have the privilege to serve.

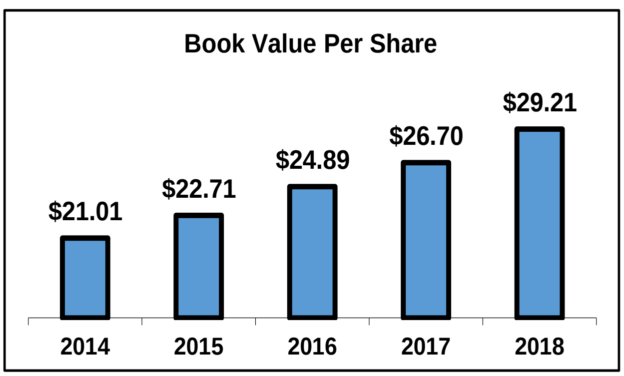
I cordially invite you to attend our annual meeting of shareholders. We will provide a recap of 2018, elect directors, and offer a glimpse at what we expect in 2019. We will meet **Thursday, April 25, 2019 at 7:00 pm** at the St. Patrick's Catholic parish hall at 560 N. Jones Street in Heppner, OR. I hope to see you there.

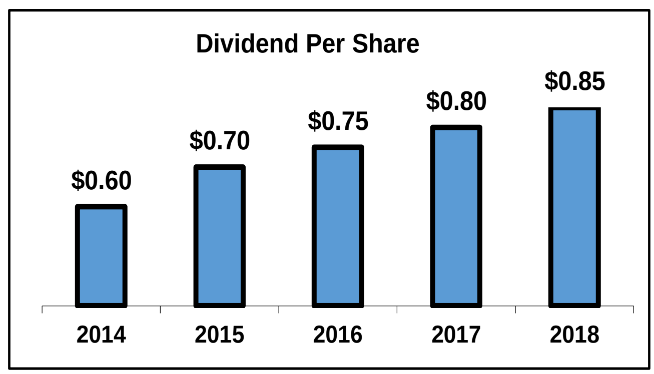
Sincerely,

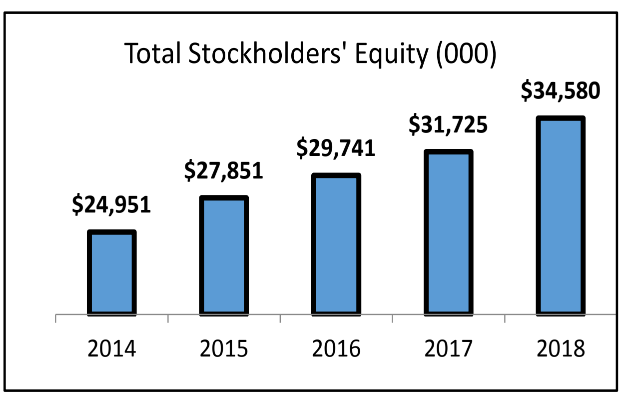
Jeff L. Bailey
President and CEO
BEO Bancorp

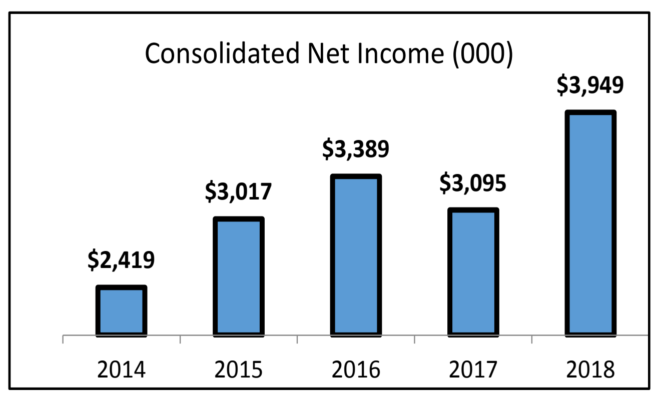
FINANCIAL HIGHLIGHTS
2014-2018

	2014	2015	2016	2017	2018
Net Income (000)	$2,419	$3,017	$3,389	$3,095	$3,949
Total Assets (000)	$325,898	$357,258	$382,187	$414,532	$414,379
Total Equity (000)	$24,951	$27,851	$29,741	$31,725	$34,580
Return on Average Assets	0.77%	0.86%	0.92%	0.78%	0.95%
Return on Average Equity	10.10%	11.43%	11.77%	10.07%	11.91%
Net Income Per Share	$2.09	$2.46	$2.80	$2.60	$3.33
Dividend Per Share	$0.60	$0.70	$0.75	$0.80	$0.85
Book Value Per Share	$21.01	$22.71	$24.89	$26.70	$29.21









Board of Directors:

Joel Peterson, Chairman	Owner, Daily Bread Farms, Inc.
Joe Gonzalez, Vice Chairman	Owner, American Electric, Inc.
Brad Anderson	Partner, Triangle Ranches
Robert M. Armstrong	CPA, Solutions, CPA's
Jeff Bailey	Banker, Bank of Eastern Oregon
E. George Koffler	Retired Banker
Gary Neal	Retired General Manager, Port of Morrow

Bank Officers:

Executive Team

Jeff Bailey, President and CEO
Mark Lemmon, Executive Vice President and CFO
Gary Propheter, Executive Vice President and COO

Senior Vice Presidents:

Becky Kindle, SVP Chief Banking Officer
John Qualls, SVP Chief Lending Officer
Ed Rollins, SVP Chief Credit Officer

Vice Presidents:

John Bailey, Team Lead Loan Officer
Dawna Dougherty, Compliance Officer
Janet Dezellem, Controller
James Gardner, Loan Officer
Pete McCabe, Loan Officer
Jed Myers, Team Lead Loan Officer
Kristy Nelson, Loan Officer
Anita Orem, Operations Support Mgr.
Robert Quinton, Loan Officer
Russell Seewald, Loan Officer
Rhonda Shaffer, Consumer Lending Mgr.
Mike Short, Team Lead Loan Officer
Robert Williams, Team Lead Loan Officer

Assistant Vice Presidents:

Arletta Arnspiger, Mortgage Loan Officer
Jim Bleth, IT Manager
Nial Bradshaw, Loan Officer
Christy Correa, Finance Coordinator
Karen Cossitt, Branch Manager
Jolene Cox, Team Lead Branch Manager
Jill Martin, Human Resource Manager
Janice Provencher, Branch Manager
Tricia Rollins, Branch Manager
Lucy Sifuentez, Branch Manager

Lenders and Managers

Jessica Barnett, Branch Manager
Laura Georges, Loan Officer
Susan Jones, Branch Manager
Shane Lazinka, Loan Officer
Amy McNamee, Loan Officer
Sherrie Modey, Branch Manager
Andrea Moles, Branch Manager
Lori Moss, Branch Manager
Debi Munck, Branch Manager
Sharon Rietmann, Branch Manager
Todd Roseborough, Loan Officer
Amber Schlaich, Loan Officer
Shayne Wagner, Loan Officer
Todd Wood, Loan Officer
Fred Zack, Loan Officer

ISLER CPA
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Independent Auditors' Report

To the Board of Directors
BEO Bancorp:

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of BEO Bancorp and Subsidiary ("BEO") which comprise the consolidated balance sheets as of December 31, 2018 and 2017 and the related consolidated statements of income, profit and other comprehensive income, changes in stockholders' equity, and cash flows for the years then ended, and the related notes to the consolidated financial statements, collectively the 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 of 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 BEO as of December 31, 2018 and 2017, 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.

Isler CPA, LLC

March 7, 2019

BEO Bancorp and Subsidiary
Consolidated Balance Sheets

	December 31	
	2018	2017
ASSETS		
Cash and cash equivalents:		
Cash and due from banks	**$ 9,231,823**	$ 6,478,699
Interest bearing deposits at other financial institutions	**21,765,499**	41,220,930
Total cash and cash equivalents	**30,997,322**	47,699,629
Investment securities available-for-sale	**31,404,133**	23,085,201
Investment securities held-to-maturity	**2,346,612**	2,850,866
Loans, less allowance for loan losses	**324,638,967**	318,869,463
Interest receivable	**3,649,866**	3,320,016
Federal Home Loan Bank stock	**497,300**	458,600
Property, less accumulated depreciation	**9,403,867**	9,529,905
Deferred taxes, net	**825,308**	768,772
Foreclosed assets	**1,844,453**	1,872,203
Cash surrender value of bank owned life insurance	**7,505,287**	4,898,194
Other assets	**1,265,471**	1,179,738
	383,381,264	366,832,958
Total assets	**$ 414,378,586**	$ 414,532,587
LIABILITIES and STOCKHOLDERS' EQUITY		
Liabilities:		
Deposits:		
Noninterest-bearing demand	**$ 93,245,316**	$ 94,380,069
Savings and interest-bearing demand	**234,957,073**	233,357,414
Time, $100,000 and over	**11,701,994**	13,223,496
Other time	**28,327,046**	29,727,641
	368,231,429	**370,688,620**
Subordinated debentures	**8,767,000**	8,817,000
Interest payable	**87,904**	80,600
Other liabilities	**2,712,537**	3,221,800
Total liabilities	**379,798,870**	382,808,020
Stockholders' equity:		
Common stock, $2.50 par value, 2,975,592 shares authorized 1,183,704 outstanding December 31, 2018, 1,189,392 outstanding December 31, 2017	**3,066,170**	3,066,170
Additional paid-in capital	**4,209,474**	4,209,474
Retained earnings	**28,529,720**	25,586,727
Treasury stock at cost, 42,764 shares outstanding	**(1,096,412)**	(924,267)
Accumulated other comprehensive income (loss)	**(129,236)**	(213,537)
Total stockholders' equity	**34,579,716**	31,724,567
Total liabilities and stockholders' equity	**$ 414,378,586**	$ 414,532,587

The accompanying notes are an integral part of these consolidated financial statements.

BEO Bancorp and Subsidiary
Consolidated Statements of Income

	Year Ended December 31	
	2018	2017
Interest income:		
Interest and fees on loans:		
Taxable	**$18,736,872**	$18,015,506
Nontaxable	**532,728**	373,510
Interest on investment securities:		
Taxable	**552,890**	269,657
Nontaxable	**110,241**	138,235
Interest on federal funds sold and short-term time deposits	**273,891**	226,720
	20,206,622	19,023,628
Interest expense	**1,276,276**	1,119,642
Net interest income	**18,930,346**	17,903,986
Provision for loan losses	**1,300,000**	600,000
Net interest income after provision for loan losses	**17,630,346**	17,303,986
Noninterest income:		
Service charges	**2,187,072**	2,053,578
Mortgage banking income	**223,814**	227,497
Other	**426,081**	202,518
	2,836,967	2,483,593
Noninterest expense:		
Salaries and employee benefits	**9,152,195**	8,945,531
Occupancy expense	**980,943**	932,770
Equipment expense	**1,538,288**	1,377,181
Foreclosed asset expenses	**85,857**	43,544
Other	**3,767,227**	3,395,314
	15,524,510	14,694,340
Income before income taxes	**4,942,803**	5,093,239
Provision for income taxes	**994,000**	1,999,000
Net income	**$ 3,948,803**	$ 3,094,239
Basic earnings per share	**$ 3.33**	$ 2.60

The accompanying notes are an integral part of these consolidated financial statements.

BEO Bancorp and Subsidiary
Consolidated Statements of Profit and Other Comprehensive Income

	Year Ended December 31	
	2018	**2017**
Net Income	**$ 3,948,803**	$ 3,094,239
Other comprehensive income (loss), net of tax:		
Unrealized gains (losses) on investment securities	**(67,165)**	1,465
Unrealized gain (loss) on cash flow hedge instrument	**151,467**	(2,265)
Other comprehensive income (loss)	**84,301**	(800)
Comprehensive Income	**$ 4,033,104**	$ 3,093,439

The accompanying notes are an integral part of these consolidated financial statements.

BEO Bancorp and Subsidiary
Consolidated Statements of Changes in Stockholders' Equity
For the Years Ended December 31, 2018 and 2017

	Common Stock	Additional Paid-in Capital	Retained Earnings	AOC Income (Loss)	Treasury Stock	Total
Balance, January 1, 2017	$3,066,170	$4,209,474	$23,444,201	$ (212,737)	(765,988)	$ 29,741,120
Net income			3,094,239			3,094,239
Other comprehensive income (loss):				(800)		(800)
Purchase of 5,401 shares of treasury stock					(158,279)	(158,279)
Cash dividends ($.80 per share)			(951,713)			(951,713)
Balance, December 31, 2017	3,066,170	4,209,474	25,586,727	(213,537)	(924,267)	31,724,567
Net income			**3,948,803**			**3,948,803**
Other comprehensive income (loss):				**84,301**		**84,301**
Purchase of 5,688 shares of treasury stock					**(172,145)**	**(172,145)**
Cash dividends ($.85 per share)			**(1,005,810)**			**(1,005,810)**
Balance, December 31, 2018	**$3,066,170**	**$4,209,474**	**$28,529,720**	**$ (129,236)**	**$(1,096,412)**	**$ 34,579,716**

The accompanying notes are an integral part of these consolidated financial statements.

BEO Bancorp and Subsidiary
Consolidated Statements of Cash Flows

	Year Ended December 31	
	2018	**2017**
Cash flows from operating activities:		
Net income	**$ 3,948,803**	$ 3,094,239
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	**742,673**	627,771
Net gains or losses on property dispositions	**(675)**	2,886
Amortization of investment premiums, net	**186,565**	146,335
Provision for loan losses	**1,300,000**	600,000
Write down of foreclosed assets	**27,750**	-
Increase in cash value of life insurance	**(107,093)**	(106,669)
Deferred income taxes	**(87,000)**	396,000
Change in:		
Interest receivable and other assets	**(415,583)**	(35,627)
Deferred loan fees	**3,334**	(163,223)
Accrued interest and other liabilities	**(295,797)**	(23,581)
Net cash provided by operating activities	**5,302,977**	4,538,131
Cash flows from investing activities:		
Proceeds from maturities of investment securities	**10,397,568**	9,602,174
Purchase of investment securities	**(18,490,208)**	(13,413,760)
Proceeds from sale of loans	**2,963,743**	-
Purchase of bank owned life insurance	**(2,500,000)**	-
Proceeds from sale of foreclosed assets	**-**	67,458
Purchase of FHLB stock	**(38,700)**	(29,700)
Loans originated, net of principal collected	**(10,036,581)**	(17,958,237)
Purchases of property	**(615,960)**	(984,203)
Net cash provided (used) in investing activities	**(18,320,138)**	(22,716,268)
Cash flows from financing activities:		
Net increase in deposits	**(2,457,191)**	30,635,763
Increase (Decrease) in subordinated debt	**(50,000)**	(250,000)
Repurchase of common stock	**(172,145)**	(158,279)
Dividends paid	**(1,005,810)**	(951,713)
Net cash provided by financing activities	**(3,685,146)**	29,275,771
Net increase (decrease) in cash and cash equivalents	**(16,702,307)**	11,097,634
Cash and cash equivalents, beginning of year	**47,699,629**	36,601,995
Cash and cash equivalents, end of year	**$ 30,997,322**	$ 47,699,629

The accompanying notes are an integral part of these consolidated financial statements.

BEO Bancorp and Subsidiary
Consolidated Statements of Cash Flows, Continued

	Year Ended December 31	
	2018	**2017**
Supplemental information:		
Cash paid during the year for:		
Income taxes	**$ 800,140**	$ 784,745
Interest	**1,268,972**	1,130,179
Transfer of loans to foreclosed assets	**-**	906,211

The accompanying notes are an integral part of these consolidated financial statements.

1. Summary of Significant Accounting Policies:

Basis of Presentation – The consolidated financial statements include the accounts of BEO Bancorp ("Bancorp"), a bank holding company, and its wholly-owned subsidiary, Bank of Eastern Oregon (the "Bank"). All significant intercompany accounts and transactions have been eliminated in consolidation. Bancorp has also established subsidiary grantor trusts in connection with the issuance of trust preferred securities (see Note 10). In accordance with the requirements of ASC 810 the accounts and transactions of these trusts are not consolidated in the accompanying consolidated financial statements.

Description of Business - The Bank provides commercial and consumer financing, banking and mortgage lending and other services in Northeastern Oregon and Southeastern Washington. Its activities include the usual lending and deposit functions of a commercial bank: commercial, agricultural, real estate, installment, credit card and mortgage loans; checking, money market, time deposit and savings accounts; internet banking and bill payment; automated teller machines and safe deposit facilities. Additionally, the Bank originates and sells mortgage loans into the secondary market.

Financial Statement Presentation – The preparation of the financial statements in conformity with U.S. generally accepted accounting principles (GAAP) requires management to make estimates and assumptions that affect reported amounts and related disclosures, and actual results could differ from those estimates. The most significant estimates are the allowance for loan losses and fair value estimates. The Company has evaluated subsequent events through February 26, 2018, the date the financial statements are available for distribution. Certain prior year amounts may have been reclassified to conform to the current year presentation. Such reclassifications have no effect on previously reported net income.

Cash and Cash Equivalents – For purposes of presentation in the consolidated statements of cash flows, cash and cash equivalents are defined as those amounts included in the balance sheet caption "cash and due from banks". Such amounts include interest bearing deposits and federal funds sold on a short-term basis and may exceed amounts insured by FDIC.

Investment Securities – Securities for which management has the positive intent and ability to hold to maturity are classified as held-to-maturity and are reported at cost adjusted for remaining balances of premiums or discounts.

Securities purchased with the intent to sell in the near term are classified as trading securities and are reported at estimated fair market value with unrealized gains or losses reported in non-interest income. The Bank had no trading securities at December 31, 2018 or 2017.

1. Summary of Significant Accounting Policies, Continued:

Securities not classified as held-to-maturity or as trading securities are classified as available-for-sale. Securities available-for-sale are held for indefinite periods of time and may be sold in response to changes in market interest rates, shifts in the maturity mix or concentration of bank assets or liabilities or to alleviate liquidity demands. Securities designated as available-for-sale are carried at estimated fair value. Unrealized gains and losses are excluded from earnings and are credited or charged to other comprehensive income in stockholders' equity, net of applicable deferred taxes. Interest income on debt securities is included in income using the effective interest method. Gains and losses realized on sales of securities are recognized on the specific identification method.

The Bank recognizes other-than-temporary impairments for debt securities classified as available for sale in accordance with ASC 320. Accordingly, the Bank assesses whether it intends to sell, or it is more likely than not that it will be required to sell a security before recovery of its amortized cost basis less any current-period credit losses. For debt securities that are considered other-than-temporarily impaired and that the Bank does not intend to sell and will not be required to sell prior to recovery of the amortized cost basis, the Bank separates the amount of the impairment into the amount that is credit related (credit loss component) and the amount due to all other factors. The credit loss component is recognized in earnings and is the difference between the security's amortized cost basis and the present value of its expected future cash flows discounted at the security's effective yield. The remaining difference between the security's fair value and the present value of future expected cash flows is due to factors that are not credit related and, therefore, is not required to be recognized as losses in the income statement but is recognized in other comprehensive income. The Bank has not recognized an other-than-temporary impairment of its debt securities as management believes all unrealized losses on investment securities at December 31, 2018 are temporary (see note 3).

Loans and Income Recognition – Loans are stated at the amount of unpaid principal, net of deferred loan origination fees, premiums or discounts on purchased loans, and an allowance for loan losses. Interest on loans is calculated using the simple-interest method on daily balances of the principal amount outstanding. Accrual of interest is discontinued on a loan when management believes, after considering economic and business conditions and collection efforts that the borrower's financial condition is such that collection of the interest is doubtful. Cash receipts on non-accrual loans are first recorded as principal collections. Loan origination fees, net of associated direct costs, if significant, are amortized by the interest method over the contractual life of the loan. Premiums and discounts on loans purchased are amortized using the straight-line method over a period management believes best matches the cash flow and risks associated with the loan.

1. Summary of Significant Accounting Policies, Continued:

Allowance for Loan Losses – The allowance for loan losses is established through a provision for loan losses charged to expense. Loans are charged against the allowance for loan losses when management believes that the collectability of the principal is unlikely. The allowance is an amount that management considers adequate to absorb possible losses on existing loans that may become uncollectible based on evaluations of the collectability of loans and prior loss experience. The evaluations take into consideration such factors as changes in the nature and value of the loan portfolio, overall portfolio quality, review of specific problem loans, and current economic conditions that may affect the borrower's ability to pay.

A loan is considered impaired when management believes that it is probable that all amounts will not be collected according to the contractual terms. An impaired loan is valued using the present value of expected cash flows discounted at the loan's effective interest rate, the observable market price of the loan or the estimated fair value of the loan's collateral or related guaranty. Loans deemed impaired have a specifically allocated reserve within the allowance for loan losses.

The allowance and provision are estimates that are necessarily subjective and may be adjusted as more current information becomes available. Any adjustment could be significant.

The Bank classifies reserves for potential losses on commitments to loan in other liabilities.

Federal and state bank regulatory agencies, as an integral part of their examination process, periodically review the Bank's reserve for loan losses. Such agencies may require the Bank to recognize additions to the reserve in the future based on their judgment of the information available to them at the time of their examinations.

Federal Home Loan Bank Stock – The investment in Federal Home Loan Bank ("FHLB") stock is a restricted investment carried at cost, which is based on the ultimate recoverability at par value. As a member of the FHLB system, the Bank is required to maintain a minimum level of investment in FHLB stock based on borrowings. At December 31, 2018, the minimum required investment was $497,300. The Bank may request redemption at par value of any stock in excess of the amount it is required to hold. Stock redemptions are at the discretion of the FHLB.

Property and Equipment – Property is stated at cost, net of accumulated depreciation. Additions, betterments and replacements of major units are capitalized. Expenditures for normal maintenance, repairs and replacements of minor units are charged to expense as incurred. Gains or losses realized from sales or retirements are reflected in operations currently. Depreciation is computed by the straight-line method over the estimated useful lives of the assets.

1. Summary of Significant Accounting Policies, Continued:

Core Deposit Intangible – Core deposit intangible is stated at cost, net of accumulated amortization. Amortization is recorded on a straight-line basis with periodic evaluation for impairment.

Foreclosed Assets – Assets acquired through, or in lieu of, loan foreclosure are held-for-sale and are initially recorded at fair value at the date of foreclosure based on current appraisals, establishing a new cost basis. Subsequent to foreclosure, valuations are periodically performed by management and the assets are carried at the lower of carrying amount or fair value less cost to sell. Revenue and expenses from operations and changes in the valuation allowance are included in other noninterest expense.

Advertising – Advertising costs are generally charged to expense during the year in which they are incurred.

Income Taxes – Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are calculated on differences between financial statement and tax bases of assets and liabilities using tax rates in effect for the year in which the differences are expected to reverse. Valuation allowances are established to reduce the net carrying amount of deferred tax assets if it is determined to be more likely than not, that all or some of the potential deferred tax asset will not be recognized.

Uncertain tax positions are accounted for in accordance with ASC 740 which prescribes recognition and measurement standards for uncertain income tax positions. The Standard provides guidance on recognition, de-recognition, interest, penalties and disclosure. There is no material impact of potential tax uncertainties on Bancorp's financial condition or results of operations at December 31, 2018.

Fair Value – Bancorp applies the hierarchy and framework for measuring fair value, disclosure about fair value measurements and the reliability of valuation inputs as provided in ASC 820. When determining the fair value, Bancorp considers the transaction to sell an asset or transfer a liability occurs in the most advantageous market for that asset or liability. Within the hierarchy, Level 1 instruments use observable market prices for the identical item in active markets and have the most reliable valuations. Level 2 instruments are valued through broker/dealer quotation or through market-observable inputs for similar items in active markets, including forward and spot prices, interest rates and volatilities. Level 3 instruments are valued using inputs not observable in an active market such as company-developed future cash flow estimates and are considered the least reliable. Valuations for all of Bancorp's and the Bank's financial instruments fall within Levels 2 and 3 (see note 16).

1. **Summary of Significant Accounting Policies,** Continued:

Derivative Instruments – Bancorp and the Bank use a derivative financial instrument (interest rate swaps) to limit exposure to changes in interest rates related to a subordinated debenture. The derivatives entered into by Bancorp and the Bank are designated as cash flow hedge with perfect effectiveness between changes in the value of the interest rate swap and the hedged instrument (subordinated debenture liability). The derivative and related hedged debenture are recognized in the balance sheet at their fair value. Bancorp and the Bank formally documents all relationships between hedging instruments and formally assesses, both at the hedge's inception and on an ongoing basis, whether the derivative that is used in the hedging transaction is highly effective in offsetting changes in fair values of hedged items.

Bancorp and the Bank would discontinue hedge accounting when: (a) it is determined that a derivative is no longer effective in offsetting changes in the fair value of the associated hedged item; (b) the derivative expires or is sold, terminated, or exercised; or (c) management determines that designation of the derivative as a hedge instrument is no longer appropriate. The hedged liability would no longer be adjusted for changes in fair value and the derivative would be carried at its fair value in the balance sheet, with changes in its fair value recognized in current-period earnings.

Recently Issued Accounting Pronouncements Effective in 2017 and subsequent years:

FASB Accounting Standards Update 2015-17, Income Taxes (Topic 740): The amendment simplifies the presentation of deferred income taxes, the amendments in this Update require that deferred tax liabilities and assets be classified as noncurrent in a classified statement of financial position. This update is effective for the Bank for the year ended December 31, 2018.

FASB Accounting Standards Update (ASU) No. 2014-09, Revenue from Contracts with Customers (ASU 2014-09): ASU 2014-09 implements a common revenue standard that clarifies the principles for recognizing revenue. The core principle of ASU 2014-09 is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. To achieve that core principle, an entity should apply the following steps: (1) identify the contract(s) with a customer, (2) identify the performance obligations in the contract, (3) determine the transaction price, (4) allocate the transaction price to the performance obligations in the contract, and (5) recognize revenue when (or as) the entity satisfies a performance obligation. ASU 2014-09 is effective for annual periods, and interim reporting periods within those annual periods. This update is effective for the Bank for the year ended December 31, 2019.

1. Summary of Significant Accounting Policies, Continued:

FASB Accounting Standards Update 2016-02 Leases: This is intended to increase transparency and comparability among organizations by requiring the recognition of lease assets and lease liabilities on the balance sheet and disclosure of key information about leasing arrangements. The principal change required by ASU 2016-02 relates to lessee accounting, and is that for operating leases, a lessee is required to (1) recognize a right-of-use asset and a lease liability, initially measured at the present value of the lease payments, in the statement of financial position, (2) recognize a single lease cost, calculated so that the cost of the lease is allocated over the lease term on a generally straight-line basis, and (3) classify all cash payments within operating activities in the statement of cash flows. For leases with a term of 12 months or less, a lessee is permitted to make an accounting policy election by class of underlying asset not to recognize lease assets and lease liabilities. If a lessee makes this election, it should recognize lease expense for such leases generally on a straight-line basis over the lease term. ASU 2016-02 also changes disclosure requirements related to leasing activities and requires certain qualitative disclosures along with specific quantitative disclosures. This update is effective for the Bank for the year ended December 31, 2020,

FASB Accounting Standards Update 2016-13, Financial Instruments—Credit Losses (Topic 326): The main objective of this Update is to provide financial statement users with more decision-useful information about the expected credit losses on financial instruments and other Commitments to extend credit held by a reporting entity at each reporting date. The amendments in this Update replace the incurred loss impairment methodology in current GAAP with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to inform credit loss estimates. This update is effective for the Bank for the year ended December 31, 2021.

FASB Accounting Standards Update 2017- 08 Receivables—Nonrefundable Fees and Other Costs (Subtopic 310-20): Premium Amortization on Purchased Callable Debt. This amendment requires the premium for certain callable securities be amortized to the earliest call date. This update is effective for the Bank for the year ended December 31, 2020.

FASB Accounting Standards Update 2017-12 Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities: This update was issued to improve the financial reporting of hedging relationships to better portray the economic results of the hedge. This update is effective for the Bank for the year ended December 31, 2021.

2. Cash and Due From Banks:

The Bank is required to maintain an average reserve balance with the Federal Reserve Bank or maintain such reserve balance in the form of cash. The required reserve balances at December 31, 2018 and 2017 were approximately $5,751,000 and $3,221,000, respectively, and were met by holding cash and maintaining an average balance with the Federal Reserve Bank.

3. Investment Securities:

The amortized cost and estimated fair values of investment securities at December 31, 2018 and 2017 are as follows:

2018

Available-for-sale:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Obligations of U.S. Government agencies	**$ 18,237,007**	**$ 52,396**	**$ (42,882)**	**$ 18,246,521**
Government guaranteed loan pools	**7,051,409**	**18,914**	**(86,088)**	**6,984,235**
Mortgage-backed securities	**5,304,447**	**11,190**	**(44,593)**	**5,271,044**
Obligations of municipal entities	**893,039**	**10,210**	**(916)**	**902,333**
	$ 31,485,902	**$ 92,710**	**$ (174,479)**	**$ 31,404,133**

Held-to-maturity:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Obligations of municipal entities	**$ 2,346,612**	**$ -**	**$ -**	**$ 2,346,612**
	$ 2,346,612	**$ -**	**$ -**	**$ 2,346,612**

2017

Available-for-sale:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Obligations of U.S. Government agencies	$ 13,260,859	$ 16,413	$ (42,776)	$ 13,234,496
Government guaranteed loan pools	6,090,446	70,821	(27,958)	6,133,309
Mortgage-backed securities	2,834,545	409	(30,095)	2,804,859
Obligations of municipal entities	889,723	22,814	-	912,537
	$ 23,075,573	$ 110,457	$ (100,829)	$ 23,085,201

Held-to-maturity:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Obligations of municipal entities	$ 2,850,866	$ -	$ -	$ 2,850,866
	$ 2,850,866	$ -	$ -	$ 2,850,866

3. Investment Securities, Continued:

Investment securities that were in unrealized loss positions as of December 31, 2018 and 2017 are presented in the following tables, based on the length of time that individual securities were in unrealized loss positions.

Securities in Unrealized Loss Positions as of December 31, 2018

	Less than 12 Months		12 Months or Longer		Total	
	Fair Value	**Unrealized Losses**	**Fair Value**	**Unrealized Losses**	**Fair Value**	**Unrealized Losses**
Obligations of U.S. Government agencies	**$ 3,740,514**	**$ 9,013**	**$ 5,481,131**	**$ 33,869**	**$ 9,221,645**	**$ 42,882**
Mortgage-backed securities	**1,705,991**	**7,994**	**2,036,761**	**36,599**	**3,742,752**	**44,593**
Government guaranteed loan pools	**2,655,326**	**33,229**	**1,855,218**	**52,859**	**4,510,544**	**86,088**
Total	**$ 8,101,831**	**$ 50,236**	**$ 9,373,110**	**$ 123,327**	**$ 17,474,941**	**$ 173,563**

Securities in Unrealized Loss Positions as of December 31, 2017

	Less than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Obligations of U.S. Government agencies	$ 498,983	$ (1,016)	$ 9,945,776	$ (41,760)	$ 10,444,759	$ (42,776)
Mortgage-backed securities	381,419	(1,052)	2,390,977	(29,043)	2,772,396	(30,095)
Government guaranteed loan pools	1,160,687	(3,875)	1,429,601	(24,083)	2,590,288	(27,958)
Total	$ 2,041,089	$ (5,943)	$ 13,766,354	$ (94,886)	$ 15,807,443	$ (100,829)

The unrealized losses on investment securities were caused by interest rate increases subsequent to the purchase of the securities and are considered temporarily impaired. It is expected that the securities will not be settled at a price less than the amortized cost of the investment. Because the decline in fair value is attributable to changes in interest rates and not credit quality, and because the Bank has the ability and intent to hold these investments until a market price recovery or to maturity, the unrealized losses on these investments are not considered other-than-temporarily impaired.

3. Investment Securities, Continued:

The amortized cost and estimated fair value of investment securities at December 31, 2018 by contractual maturity are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Available-for-Sale		Held-to-Maturity	
	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
Due in one year or less	$ 6,364,252	$ 6,365,587	$ -	$ -
Due after one year through five years	16,462,490	16,422,005	2,346,612	2,346,612
Due after five years	3,354,714	3,345,497	-	-
Mortgage-backed securities	5,304,446	5,271,044	-	-
	$ 31,485,902	$ 31,404,133	$ 2,346,612	$ 2,346,612

There were no sales of securities in 2018 or 2017.

At December 31, 2018, investment securities with amortized costs of $14,276,953 and estimated fair values of $14,263,529 were pledged for public deposits ($11,191,497 and $11,216,567 at December 31, 2017, respectively).

4. Loans:

Major classifications of loans by type of collateral at December 31 are as follows:

	2018	2017
Farmland Loans	**$ 93,481,476**	$ 97,731,273
Commercial real estate loans	**63,872,261**	65,890,677
Agriculture loans	**66,119,694**	61,044,614
Government guaranteed loans	**15,341,476**	15,296,878
Commercial loans	**35,100,489**	35,706,703
Real estate loans	**40,195,714**	33,169,453
Municipal loans	**11,494,643**	10,528,138
Consumer loans	**3,272,796**	3,567,279
	328,878,549	322,935,015
Deferred loan origination fees	**(559,453)**	(556,119)
Purchased loans discount	**(124,363)**	(191,513)
	328,194,733	322,187,383
Allowance for loan losses	**(3,555,766)**	(3,317,920)
	$ 324,638,967	$ 318,869,463

The loan portfolio at December 31, 2018 and 2017 includes $260,330,420 and $255,388,424, respectively, of loans which have a variable rate of interest. The December 31, 2018 amount includes $128,063,339 of loans with interest rates at their contractual floors.

Loans serviced for others are not included in the accompanying consolidated balance sheets. There were no loans being serviced for others at December 31, 2018 or 2017.

The total loans outstanding on December 31 which were on a nonaccrual basis, contractually past due 90 days or more as to interest or principal payments are as follows:

	Recorded Investment Nonaccrual Loans	**Unpaid Principal Nonaccrual Loans**	**Loans Past Due 90 Days or More and Still Accruing**
2018			
Agriculture	**2,771,453**	**3,036,881**	
Commercial real estate	**2,028,105**	**2,128,606**	
Commercial	**245,451**	**245,451**	
Farmland	**$ 15,381**	**$ 15,381**	
Consumer	**4,485**	**4,485**	
	$ 5,064,875	**$ 5,430,804**	**$ -**
2017			
Farmland	$ 3,277,453	$ 3,334,386	$ -
Commercial real estate	2,459,335	2,909,174	-
Agriculture	2,611,740	4,675,702	-
Commercial	265,630	265,630	-
Real estate	28,505	28,505	-
Consumer	-	-	9,991
	$ 8,642,663	$ 11,213,397	$ 9,991

4. Loans, Continued:

The following is an analysis of impaired loans as of December 31:

2018	**Impaired Loans**				
	With a Related Allowance	**Without a Related Allowance**	**Total Recorded Investment**	**Unpaid Principal Balance**	**Related Allowance**
Farmland	**$ -**	**$1,462,377**	**$ 1,462,377**	**$ 1,667,261**	**$ -**
Commercial real estate	**-**	**2,072,018**	**2,072,018**	**2,172,519**	**-**
Agriculture	**-**	**3,415,918**	**3,415,918**	**3,681,346**	**-**
Commercial	**-**	**414,088**	**414,088**	**716,094**	**-**
Real estate		**174,822**	**174,822**	**177,397**	**-**
Consumer	**-**	**4,484**	**4,484**	**4,484**	**-**
	$ -	**$7,543,707**	**$ 7,543,707**	**$ 8,419,101**	**$ -**

2017	Impaired Loans				
	With a Related Allowance	Without a Related Allowance	Total Recorded Investment	Unpaid Principal Balance	Related Allowance
Farmland	$ -	$3,277,453	$ 3,277,453	$ 3,539,269	$ -
Commercial real estate	-	2,217,419	2,217,419	2,365,252	-
Agriculture	225,743	2,385,997	2,611,740	4,675,702	36,831
Commercial	-	557,287	557,287	859,293	-
Real estate		186,051	186,051	188,627	-
	$ 225,743	$8,624,207	$ 8,849,950	$11,628,143	$ 36,831

The average recorded investment in impaired loans was approximately $8,279,802 and $10,555,858 in 2018 and 2017, respectively. Interest income recognized on impaired loans totaled $273,026 and $124,407 in 2018 and 2017, respectively. Interest income which would have been realized on non-accrual loans if they had remained current and still accruing was $810,620 and $871,799 in 2018 and 2017, respectively.

4. Loans, Continued:

There were no loans accounted for as Trouble Debt Restructurings (TDR) that occurred during the years ended December 31, 2018 and 2017.

None of the loans accounted for as TDR from previous years were in default as of December 31, 2018. At December 31, 2018 the Bank had no unfunded commitments on TDR loans. There were no unfunded commitments on TDR loans at December 31, 2017. Loans are accounted for as TDR when significant concessions have been granted that would not have otherwise been considered except for the borrower's financial difficulties. Concessions may include extended repayment terms such as interest only payments or lengthened maturities, or interest rate modifications and are granted to improve the likelihood that the borrower will be able to repay the obligation. TDR loans are included in impaired loans and the methodology for evaluating credit losses and accrual status is the same as for other impaired loans.

5. Allowance for Loan Losses:

The Bank maintains an allowance for loan losses ("ALLL") to absorb losses resulting from the inherent risks of lending. The balance of the ALLL is reviewed at least quarterly to assess the adequacy relative to probable estimated losses within the loan portfolio. The methodology is consistent with the Contingencies and Receivables topics of the FASB ASC and did not significantly change during 2018 or 2017
. The ALLL includes a general allowance based on quantitative and qualitative factors on non-impaired loans plus specific reserves on impaired loans established to account for credit attributes of the individual relationships. Credit risk is managed through established policies and procedures including lending limits, diversification, approval requirements, and an ongoing comprehensive review process. The review process includes assigning a numerical risk rating to a loan when originated, and then modifying that risk rating as circumstances dictate.

These Loan risk ratings are assigned as follows:

A rating of 1-2 indicates low apparent credit risk.
A rating of 3-4 indicates average to above average potential credit risk.
A rating of 5-6 indicates weaknesses and factors displaying potential credit risk that requires a higher level of management attention.
A rating of 7 indicates a probable loss but the amount is not specifically determined.
A rating of 8 indicates specific loss has been identified and charge-off is imminent.

5. Allowance for Loan Losses, Continued:

A detailed analysis of the ALLL by major portfolio segment as of December 31:

2018

			Allowance for Loan Losses					
	Weighted Average Risk Rating	**Recorded Investment in Loans**	**Beginning Balance**	**Net (Charge-off) Recovery**	**Provision**	**Ending Balance**	**Specific Reserve**	**General Allocation**
Farmland	**3.10**	**$ 93,257,535**	**$ 887,853**	**$ (313,710)**	**$ 290,000**	**$ 864,143**	**$ -**	**$ 864,143**
Commercial real estate	**2.73**	**63,611,246**	**1,306,500**	**(5,556)**	**20,000**	**1,320,944**	**-**	**1,320,944**
Agriculture	**3.23**	**66,105,774**	**467,381**	**(671,355)**	**815,000**	**611,026**	**-**	**611,026**
Government guaranteed	**2.62**	**15,341,476**	**27,287**	**(21,232)**	**60,000**	**66,055**	**-**	**66,055**
Commercial	**2.90**	**35,071,336**	**271,528**	**3,402**	**30,000**	**304,930**	**-**	**304,930**
Real estate	**2.99**	**40,102,845**	**205,779**	**-**	**60,000**	**265,779**	**-**	**265,779**
Municipal	**2.57**	**11,431,849**	**45,810**	**-**	**10,000**	**55,810**	**-**	**55,810**
Consumer	**3.20**	**3,272,672**	**68,952**	**(16,873)**	**15,000**	**67,079**	**-**	**67,079**
Total	**3.11**	**$ 328,194,733**	**$3,281,090**	**$(1,025,324)**	**$1,300,000**	**$3,555,766**	**$ -**	**$3,555,766**

2017

			Allowance for Loan Losses					
	Weighted Average Risk Rating	Recorded Investment in Loans	Beginning Balance	Net (Charge-off) Recovery	Provision	Ending Balance	Specific Reserve	General Allocation
Farmland	3.12	$ 97,471,675	$ 786,985	$ (449,133)	$ 550,000	$ 887,852	$ -	$ 887,852
Commercial real estate	2.74	65,581,761	1,628,956	1,067,544	(1,390,000)	1,306,500	-	1,306,500
Agriculture	3.16	61,034,298	466,101	(661,889)	700,000	504,212	36,831	467,381
Government guaranteed	2.33	15,296,878	(6,894)	(40,819)	75,000	27,287	-	27,287
Commercial	2.99	35,672,163	269,579	(715,751)	717,700	271,528	-	271,528
Real estate	3.06	33,121,660	205,578	53,201	(53,000)	205,779	-	205,779
Municipal	2.58	10,443,160	45,810	-	-	45,810	-	45,810
Consumer	3.33	3,565,788	68,944	(292)	300	68,952	-	68,952
Total	3.11	$ 322,187,383	$3,465,059	$ (747,139)	$ 600,000	$3,317,920	$ 36,831	$3,281,089

6. Property and Equipment:

Property and Equipment at December 31 consists of the following:

	2018	2017
Land	**$ 865,464**	$ 865,464
Buildings and improvements	**10,807,302**	10,749,864
Furniture and equipment	**5,544,731**	5,192,845
	17,217,497	16,808,173
Accumulated depreciation	**(7,813,630)**	(7,278,268)
	$ 9,403,867	$ 9,529,905

Depreciation expense of $742,673 and $627,771 was recognized in the years ending December 31, 2018 and 2017, respectively.

7. Other Assets:

	2018	2017
Prepaid expenses	**$ 619,513**	$ 529,367
Investment in unconsolidated subsidiaries (Trusts) (Note 11)	**217,000**	217,000
Other equity securities	**190,425**	190,425
Other items, net	**238,533**	242,946
	$ 1,265,471	$ 1,179,738

8. Deposits:

The scheduled maturities of time deposits at December 31 are as follows:

	2018	2017
Less than one year	**$ 30,919,194**	$ 31,976,537
One to three years	**6,941,557**	7,884,102
Over three years	**2,168,289**	3,090,498
	$ 40,029,040	$ 42,951,137

9. Borrowings:

At December 31, 2018, the Bank has unused credit available totaling approximately $50,000,000 from the Federal Home Loan Bank of Des Moines, $29,000,000 of federal funds lines with correspondent banks and $5,000,000 with the Federal Reserve Bank of San Francisco. There were no balances outstanding on these credit lines at December 31, 2018 or December 31, 2017.

The Federal Home Loan Bank line of credit, when borrowed against, is secured by certain investment securities and real estate loans. The Federal Reserve Bank line of credit is secured by pledged real estate and agricultural loans.

10. Subordinated Debentures:

As of December 31, 2018, Bancorp had two wholly-owned trusts ("Trusts") that were formed to issue trust preferred securities and related common securities. The Trusts issued Capital Securities ("Trust Preferred Securities") and invested the proceeds in a like amount of Junior Subordinated Debentures ("Debentures") of BEO Bancorp. Interest distributions on the Trust Preferred Securities are payable quarterly and are deferrable, at Bancorp's option, for up to five years. The Debentures bear the same terms and interest rates as the related Trust Preferred Securities. The Debentures are the sole assets of the Trusts. Bancorp has unconditionally guaranteed all of the obligations of the Trusts.

The Trust Preferred Securities are mandatorily redeemable, in whole or in part, upon repayment of the underlying Debentures at their stated maturities or their earlier redemption. The Debentures are redeemable prior to maturity at Bancorp's option.

In accordance with provisions of ASC 810 the Trusts have not been consolidated in these financial statements. The $7,217,000 of Debentures issued to the Trusts as of December 31, 2018 is reflected as subordinated debentures in the consolidated balance sheets. The common stock issued by the Trusts is recorded in other assets (Note 7).

In February 2015 Bancorp issued a total of $1,850,000 in 4% 5-year Callable Subordinated Notes ("Notes") in a private offering to fund a portion of the cash consideration of the purchase of Bank Reale. Interest is payable quarterly. Prepayment of the Notes, in whole or in part, may be made at the election of Bancorp at any time after the first anniversary date. Bancorp prepaid $50,000 and $250,000 of the Notes during 2018 and 2017 respectively.

A summary of the terms of all outstanding subordinated debentures at December 31, 2018 is as follows:

	BEO Trust I	BEO Trust II	Callable Subordinated Notes
Amount outstanding	$4,124,000	$3,093,000	$1,550,000
Date of original issue	December 17, 2003	March 17, 2005	February 20, 2015
Stated maturity	December 17, 2033	March 17, 2035	January 31, 2020
Interest rate	LIBOR plus 2.85% (5.64% at 12/31/2018)	LIBOR plus 1.90% (4.69% at 12/31/2018)	4%

11. Interest Expense:

Interest expense for the years ended December 31 is comprised of the following:

	2018	2017
Savings and interest-bearing demand	**$ 427,957**	$ 351,996
Time deposits in excess of $100,000	**136,316**	121,941
Other time deposits	**283,873**	205,774
Interest expense on deposits	**848,146**	679,711
Subordinated debentures (Note 11)	**419,549**	437,169
Short-term borrowings	**8,581**	2,762
Total interest expense	**$ 1,276,276**	$ 1,119,642

12. Benefit Plans:

The Bank has a defined contribution 401(k) plan and employee stock ownership plan (ESOP) that covers substantially all employees. Employer contributions are determined annually by the Board of Directors. The ESOP may use employer contributions to purchase Bancorp stock. Shares of Bancorp stock are then credited to plan participants based on annual compensation. All investments of the ESOP are held in trust for the exclusive benefit of participating employees.

Compensation for plan participants is the total eligible wages paid to participants by the Bank for each calendar year, excluding fringe benefits. Dividends on allocated ESOP shares are recorded as a reduction of retained earnings.

Employer contributions charged to expense were $485,590 and $481,520 in 2018 and 2017, respectively. During 2018 and 2017 the plan purchased 8,207 and 5,685 shares of BEO Bancorp stock at a cumulative purchase price of $248,570 and $170,169, respectively. At December 31, 2018 the plan held 115,577 Bancorp shares, all of which were allocated to participants.

The Bank is beneficiary of bank-owned life insurance (BOLI) to support life insurance and salary continuation benefits for certain key employees. At December 31, 2018 and 2017, the Bank recorded a salary continuation benefit obligation included in other liabilities of $1,405,213 and $1,282,294, respectively. During 2018 and 2017, $72,471 and $72,471 was paid in benefits and the amount of expense charged to income was $195,391 and $190,251, respectively.

13. Income Taxes:

The provision for income taxes for the years ended December 31 consists of the following:

	2018	2017
Current tax expense:		
Federal	**$ 858,000**	$ 1,327,000
State	**223,000**	276,000
	1,081,000	1,603,000
Deferred tax expense (benefit):		
Federal	**(64,000)**	288,000
State	**(23,000)**	108,000
	(87,000)	396,000
	$ 994,000	$ 1,999,000

The provision for income taxes results in effective tax rates less than the federal income tax statutory rate. The reasons for the differences are as follows:

	2018	2017
Tax on income at federal statutory rate (34%)	**$ 1,680,552**	$ 1,731,700
State income tax, net of federal benefit	**146,628**	180,248
Effect of change in deferred tax rate	**-**	(364,000)
Nontaxable interest income, net of allocable interest expense	**(214,966)**	(171,360)
Other, net	**(618,214)**	622,412
	$ 994,000	$ 1,999,000

13. Income Taxes, Continued:

The provision for deferred income taxes results from timing differences in the recognition of transactions for financial statement and tax purposes. The nature and tax effects of these differences for the years ended December 31 are as follows:

	2018	2017
Deferred compensation not deducted for tax purposes	**$ (34,903)**	$ (33,963)
Loan origination costs	**(3,459)**	(484)
Loan loss deduction for tax purposes more (less) than provision for financial reporting purposes	**(132,220)**	(82,902)
Depreciation and amortization	**72,532**	91,613
Other, net	**11,050**	421,736
	$ (87,000)	$ 396,000

The components of deferred tax assets and liabilities at December 31 are as follows:

	2018	2017
Assets:		
Allowance for loan losses	**$ 763,747**	$ 641,310
Deferred compensation	**399,603**	341,303
Purchased NOL carryforward	**325,298**	344,434
Purchased Oregon BETC	**6,864**	11,439
Foreclosed assets basis difference	**18,107**	10,386
Unrealized loss on investment securities available-for-sale	**22,210**	-
Unrealized loss on cash flow hedge instrument	**27,097**	81,792
Total deferred tax assets	**1,562,926**	1,430,664
Liabilities:		
Unrealized gain on investment securities available-for-sale	**-**	2,022
Loan origination costs	**92,905**	97,376
Excess tax over book depreciation, amortization and impairment charges	**511,504**	440,729
Prepaid expenses	**110,512**	98,716
Federal Home Loan Bank stock dividends	**22,697**	23,049
Total deferred tax liabilities	**737,618**	661,892
Net deferred tax assets	**$ 825,308**	$ 768,772

14. Financial Instruments with Off-Balance-Sheet Risk:

In order to meet the financing needs of its customers, the Bank commits to extensions of credit and issues standby letters of credit. The Bank's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit and standby letters of credit is represented by the contractual notional amount of those instruments. The Bank uses the same credit policies in making commitments and conditional obligations as it does for on-balance-sheet instruments.

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any conditions established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since some of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements.

Standby letters of credit written are conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers.

Financial instruments with off-balance-sheet risk at December 31 are as follows:

	2018	**2017**
Commitments to extend credit	**$ 73,509,465**	$ 63,116,676
Standby letters of credit and financial guarantees written	**2,219,782**	1,929,626

15. Loans to Related Parties:

The Bank has granted loans to officers and directors. Such loans are made on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with unrelated parties. Activity with respect to these loans during the year ended December 31 was as follows:

	2018	2017
Balance, January 1	**$ 1,418,232**	$ 1,515,995
Net additions or renewals	**672,585**	579,878
Amounts collected or renewed	**(866,383)**	(677,641)
Balance, December 31	**$ 1,224,434**	$ 1,418,232

In addition, there were $814,285 and $814,120 in commitments to extend credit to directors and officers at December 31, 2018 and 2017, respectively, which are included as part of commitments in Note 14.

16. Fair Value Disclosures of Financial Instruments:

The following disclosures are made in accordance with provisions of ASC 825. The use of different assumptions and estimation methods could have a significant effect on fair value amounts. Accordingly, the estimates of fair value herein are not necessarily indicative of the amounts that might be realized in a current market exchange.

The estimated fair values of the financial instruments at December 31 are as follows:

	2018		2017	
	Carrying Amount	**Fair Value**	**Carrying Amount**	**Fair Value**
Financial assets:				
Cash and cash equivalents	**$30,997,322**	**$30,997,322**	$47,699,629	$ 47,699,629
Investment securities	**33,750,745**	**33,750,745**	25,936,067	25,936,067
Loans, net of allowance for loan losses	**324,638,967**	**324,789,929**	318,869,463	330,708,634
Interest receivable	**3,649,866**	**3,649,866**	3,320,016	3,320,016
Federal Home Loan Bank stock	**497,300**	**497,300**	458,600	428,900
Financial liabilities:				
Deposits	**368,231,429**	**368,406,755**	370,688,620	370,951,412
Cash flow hedge	**96,773**	**96,773**	302,935	302,935
Trust Preferred Securities	**7,217,000**	**6,795,665**	7,217,000	6,665,114
Other subordinated debentures	**1,550,000**	**1,550,000**	1,600,000	1,600,000
Accrued interest payable	**87,904**	**87,904**	806,000	80,600

Cash and Cash Equivalents – The fair value approximates carrying amount.

Investment securities – Fair value is based on quoted market prices. If a quoted market price is not available, fair value is estimated using quoted market prices from similar securities.

Loans – Fair value of fixed-rate loans is estimated by discounting the future cash flows using the current rates at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturities. Variable rate loans not at contractual floors have carrying amounts that are a reasonable estimate of fair value. Impaired loans' fair values are estimated primarily at collateral values and consider credit risk.

Deposits – Fair value of demand, interest-bearing demand and savings deposits is the amount payable on demand at the reporting date. Fair value of time deposits is estimated using the interest rates currently offered for the deposits of similar remaining maturities. The estimated fair values of deposits do not take into account the benefit that results from low-cost funding such deposits provide.

16. Fair Value Disclosures of Financial Instruments, Continued:

Subordinated debentures – The fair value is estimated by discounting future cash flow at rates currently available for debt with similar terms and maturities.

Off-Balance-Sheet Financial Instruments – The carrying amount and fair value are based on fees charged for similar commitments and are not material.

The following table presents the Company's fair value hierarchy for those assets and liabilities measured at fair value:

		Fair Value Measurements Using			
	Total	Quoted Prices in Active Markets for Identical Assets (Level I)	Significant Other Observable Inputs (Level II)	Significant Unobservable Inputs (Level III)	Total Period Losses Included in Earnings
December 31, 2018					
Recurring items, assets (liabilities):					
Cash flow hedge instrument	**$ (96,773)**	**$ -**	**$ (96,773)**	**$ -**	
Investment securities available for sale	**31,404,133**	**-**	**31,404,133**	**-**	
Total items measured at fair value on a recurring basis	**$ 31,307,360**	**$ -**	**$ 31,307,360**	**$ -**	
Non-recurring items:					
Impaired loans net of reserves	**$ 7,543,707**	**$ -**	**$ -**	**$ 7,543,707**	
Foreclosed assets	**1,844,453**	**-**	**-**	**1,844,453**	**$ 27,750**
Total items measured at fair value on a non-recurring basis	**$ 9,388,160**	**$ -**	**$ -**	**$ 9,388,160**	
December 31, 2017					
Recurring items, assets (liabilities):					
Cash flow hedge instrument	$ (302,935)	$ -	$ (302,935)	$ -	
Investment securities available for sale	23,085,201	-	23,085,201	-	
Total items measured at fair value on a recurring basis	$ 22,782,266	$ -	$ 22,782,266	$ -	
Non-recurring items:					
Impaired loans net of reserves	$ 8,849,950	$ -	$ -	$ 8,849,950	$ 600,000
Foreclosed assets	1,872,203	-	-	1,872,203	-
Total assets measured at fair value on a non-recurring basis	$ 10,722,153	$ -	$ -	$ 10,722,153	

16. Fair Value Disclosures of Financial Instruments, Continued

The fair value represents management's best estimates based on a range of methodologies and assumptions. For loans with doubt as to collectability and foreclosed assets expected cash flows are discounted using an appropriate rate considering the time of collection, credit risk, and the discount for the uncertainty of the flows. The value of collateral is also considered.

A roll-forward of the assets measured at Fair Value Using Unobservable Inputs (Level III) is as follows:

Fair Value Measurement Using Unobservable Inputs (Level III)

	Impaired loans net of reserves	Foreclosed assets	Total
Beginning balance 12/31/17	$ 8,849,950	$ 1,872,203	$ 10,722,153
Net unrealized losses	-	(27,750)	(27,750)
Additions, collections and deletions, net	(1,306,243)	-	(1,306,243)
Ending balance 12/31/18	$ 7,543,707	$ 1,844,453	$ 9,388,160

17. Regulatory Matters:

Bancorp and the Bank are subject to the regulations of certain federal and state agencies and receive periodic examinations by those regulatory authorities. In addition, the Bank is subject to various regulatory capital requirements administered by the Federal Deposit Insurance Corporation ("FDIC"). Failure to meet minimum capital requirements can initiate certain mandatory – and possibly additional discretionary – actions by regulators that, if undertaken, could have a direct material effect on the financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, banks must meet specific capital guidelines that involve quantitative measures of assets, liabilities, and certain off-balance-sheet items as calculated under regulatory accounting practices. The Bank's capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings and other factors. As a Small Bank Holding Company, Bancorp's capital adequacy is measured through the Bank.

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 Common Equity, Tier I and Total capital to risk-weighted assets, and of Tier I capital to leverage assets, all as defined in the regulations. Management believes, as of December 31, 2018, the Bank met all capital adequacy requirements to which it is subject.

As of December 31, 2018, the most recent notification from the FDIC categorized the Bank as well capitalized. There are no conditions or events subsequent to that notification that management believes have changed the institution's category.

17. Regulatory Matters, Continued:

The Bank's actual capital amounts (in thousands) and ratios are presented in the following tables.

	Actual		**For Capital Adequacy Purposes**		**To be Well Capitalized Under Prompt Corrective Action Provisions**	
	Amount	**Ratio**	**Amount**	**Ratio**	**Amount**	**Ratio**
As of December 31, 2018:						
Common tier 1 to risk-weighted assets						
Bank of Eastern Oregon	**42,214**	**11.34%**	**16,748**	**4.5%**	**24,191**	**6.5%**
Tier1 capital to risk-weighted assets						
Bank of Eastern Oregon	**42,214**	**11.34%**	**22,330**	**6.0%**	**29,774**	**8.0%**
Total capital to risk-weighted assets						
Bank of Eastern Oregon	**45,795**	**12.30%**	**29,774**	**8.0%**	**37,217**	**10.0%**
Tier I leverage ratio						
Bank of Eastern Oregon	**42,214**	**10.36%**	**16,297**	**4.0%**	**20,372**	**5.0%**

	Actual		For Capital Adequacy Purposes		To be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2017:						
Common tier 1 to risk-weighted assets						
Bank of Eastern Oregon	39,932	11.19%	16,054	4.5%	23,189	6.5%
Tier1 capital to risk-weighted assets						
Bank of Eastern Oregon	39,932	11.19%	21,405	6.0%	28,540	8.0%
Total capital to risk-weighted assets						
Bank of Eastern Oregon	43,275	12.13%	28,540	8.0%	35,675	10.0%
Tier I leverage ratio						
Bank of Eastern Oregon	39,932	9.90%	16,138	4.0%	20,173	5.0%

18. Parent Company Financial Information:

Financial information for BEO Bancorp is presented below:

BALANCE SHEETS

	December 31	
	2018	**2017**
Assets:		
Cash, deposited with the Bank	**$ 216,724**	$ 135,784
Investments in:		
Bank subsidiary	**42,998,169**	40,464,588
Nonbank subsidiaries (Trusts)	**217,000**	217,000
Other assets, net of amortization	**27,096**	81,792
	$ 43,458,989	$ 40,899,164
Liabilities and stockholders' equity:		
Liabilities:		
Accrued interest payable	**$ 15,500**	$ 25,201
Other Accrued Liabilities	**-**	29,461
Unrealized loss on cash flow hedge instrument	**96,773**	302,935
Subordinated debt	**8,767,000**	8,817,000
Total liabilities	**8,879,273**	9,174,597
Stockholders' equity:		
Common stock	**3,066,170**	3,066,170
Surplus	**4,209,474**	4,209,474
Retained earnings and accumulated other comprehensive income	**28,400,484**	25,373,190
Treasury stock at cost (31,675 shares)	**(1,096,412)**	(924,267)
Total stockholders' equity	**34,579,716**	31,724,567
Total liabilities and stockholders' equity	**$ 43,458,989**	$ 40,899,164

18. Parent Company Financial Information, Continued:

STATEMENTS OF INCOME

	Year Ended December 31	
	2018	**2017**
Cash dividends from Bank	**$ 1,716,148**	$ 1,336,714
Less:		
Interest expense	**(419,499)**	(437,119)
Professional fees and administrative expenses	**(142,553)**	(110,394)
Amortization of capital issuance costs	**-**	-
Income (loss) before equity in undistributed earnings of the Bank	**1,154,096**	789,201
Equity in undistributed earnings of Bank	**2,594,707**	2,065,038
Credit for income taxes	**200,000**	240,000
Net income	**$ 3,948,803**	$ 3,094,239

STATEMENTS OF CASH FLOWS

	Year Ended December 31	
	2018	**2017**
Operating activities:		
Net income	**$ 3,948,803**	$ 3,094,239
Adjustments to reconcile net income to net cash provided by operating activities:		
Undistributed earnings of the Bank	**(2,594,707)**	(2,065,038)
Amortization of capital issuance costs	**-**	-
Change in other assets and liabilities	**(45,201)**	28,753
Net cash provided by operating activities	**1,308,895**	1,057,954
Investing activities:		
Investment in Subsidiaries	**-**	250,000
Financing activities:		
Issuance (Retirement) of subordinated debt	**(50,000)**	-
Ajustment to acquisition value	**-**	-
Repurchase of common stock	**(172,145)**	(158,279)
Dividends paid	**(1,005,810)**	(951,713)
Net cash provided (used) by financing activities	**(1,227,955)**	(1,109,992)
Net increase (decrease) in cash	**80,940**	(52,038)
Cash, beginning of year	**135,784**	187,822
Cash, end of year	**$ 216,724**	$ 135,784

17. Subsequent Events:

Effective February 2, 2019 Bank of Eastern Oregon acquired four branches in Washington from Umpqua Bank. The branches are located in Colfax, Dayton, Lacrosse and Pomeroy. The acquisition will add approximately $40 million in deposits, $3 million in loans and $200 thousand in premises and equipment. The premium paid for deposits will be approximately 3.3% for the total balances transferred. All consideration for the acquisition will be in cash. After the transaction Bank of Eastern Oregon will have five branches in Washington, all doing business as Bank of Eastern Washington.