FNCB Bancorp, Inc.
Form 10-Q
August 03, 2018

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2018

OR

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

For the transition period from to

Commission File No. 000-53869

FNCB BANCORP, INC.

(Exact Name of Registrant as Specified in Its Charter)

Pennsylvania	**23-2900790**
(State or Other Jurisdiction	(I.R.S. Employer
of Incorporation or Organization)	Identification No.)
102 E. Drinker St., Dunmore, PA	**18512**
(Address of Principal Executive Offices)	(Zip Code)

Registrant's telephone number, including area code **(570) 346-7667**

(Former Name, Former Address and Former Fiscal Year, if Changed Since Last Report)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). YES NO

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

Large Accelerated Filer	Accelerated Filer
	Smaller reporting company
Non-Accelerated Filer	
	Emerging Growth Company

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes
No

Indicate the number of shares outstanding of each of the issuer's classes of common stock as of the latest practicable date:

Common Stock, $1.25 par value	**16,819,258 shares**
(Title of Class)	(Outstanding at August 3, 2018)

Contents

Part I - Financial Information

Item 1 - Financial Statements

FNCB BANCORP, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION
(unaudited)

(in thousands, except share data)	**June 30, 2018**	**December 31, 2017**
Assets		
Cash and cash equivalents:		
Cash and due from banks	$*16,500*	$*22,755*
Interest-bearing deposits in other banks	*4,624*	*14,991*
Total cash and cash equivalents	*21,124*	*37,746*
Debt securities available for sale, at fair value	*290,863*	*289,459*
Equity securities	*892*	*918*
Restricted stock, at cost	*7,964*	*2,763*
Loans held for sale	*629*	*1,095*
Loans, net of allowance for loan and lease losses of $9,459 and $9,034	*845,932*	*761,609*
Bank premises and equipment, net	*13,900*	*10,388*
Accrued interest receivable	*3,654*	*3,234*
Bank-owned life insurance	*30,732*	*30,460*
Other real estate owned	*787*	*1,023*
Net deferred tax assets	*16,282*	*15,785*
Other assets	*6,528*	*7,825*
Total assets	$*1,239,287*	$*1,162,305*
Liabilities		
Deposits:		
Demand (non-interest-bearing)	$*177,388*	$*176,325*
Interest-bearing	*777,855*	*826,123*
Total deposits	*955,243*	*1,002,448*
Borrowed funds:		
Federal Home Loan Bank of Pittsburgh advances	*174,251*	*44,968*
Subordinated debentures	*5,000*	*5,000*
Junior subordinated debentures	*10,310*	*10,310*
Total borrowed funds	*189,561*	*60,278*
Accrued interest payable	*331*	*241*
Other liabilities	*7,027*	*10,147*
Total liabilities	*1,152,162*	*1,073,114*
Shareholders' equity		
Preferred stock ($1.25 par)		
Authorized: 20,000,000 shares at June 30, 2018 and December 31, 2017		

Issued and outstanding: 0 shares at June 30, 2018 and December 31, 2017	-	-
Common stock ($1.25 par)		
Authorized: 50,000,000 shares at June 30, 2018 and December 31, 2017		
Issued and outstanding: 16,817,097 shares at June 30, 2018 and 16,757,963 shares at December 31, 2017	*21,021*	*20,947*
Additional paid-in capital	*63,374*	*63,210*
Retained earnings	*9,792*	*6,779*
Accumulated other comprehensive loss	*(7,062*)	*(1,745*)
Total shareholders' equity	*87,125*	*89,191*
Total liabilities and shareholders’ equity	$*1,239,287*	$*1,162,305*

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

FNCB BANCORP, INC. AND SUBSIDIARIES CONSOLIDATED STATEMENTS OF INCOME (unaudited)

(in thousands, except share data)	Three Months Ended June 30, 2018	2017	Six Months Ended June 30, 2018	2017
Interest income				
Interest and fees on loans	$9,031	$7,191	$17,319	$14,172
Interest and dividends on securities:				
U.S. government agencies	886	850	1,776	1,750
State and political subdivisions, tax-free	38	12	58	35
State and political subdivisions, taxable	1,027	978	2,051	1,800
Other securities	240	120	435	243
Total interest and dividends on securities	2,191	1,960	4,320	3,828
Interest on interest-bearing deposits in other banks	12	32	35	122
Total interest income	11,234	9,183	21,674	18,122
Interest expense				
Interest on deposits	1,134	826	2,201	1,570
Interest on borrowed funds:				
Interest on Federal Home Loan Bank of Pittsburgh advances	707	130	1,059	261
Interest on subordinated debentures	57	114	113	226
Interest on junior subordinated debentures	99	73	186	142
Total interest on borrowed funds	863	317	1,358	629
Total interest expense	1,997	1,143	3,559	2,199
Net interest income before provision (credit) for loan and lease losses	9,237	8,040	18,115	15,923
Provision (credit) for loan and lease losses	880	421	1,600	(57)
Net interest income after provision (credit) for loan and lease losses	8,357	7,619	16,515	15,980
Non-interest income				
Deposit service charges	747	728	1,449	1,419
Net (loss) gain on the sale of available-for-sale securities	(4)	693	(4)	971
Net loss on equity securities	(7)	-	(26)	-
Net gain on the sale of mortgage loans held for sale	51	110	100	135
Net gain on the sale of SBA guaranteed loans	71	56	322	56
Net (loss) gain on the sale of other repossessed assets	-	(10)	-	47
Net (loss) gain on the sale of other real estate owned	(7)	6	31	57
Loan-related fees	76	65	160	156
Income from bank-owned life insurance	138	135	272	270

Other	*464*	*240*	*744*	*482*
Total non-interest income	*1,529*	*2,023*	*3,048*	*3,593*
Non-interest expense				
Salaries and employee benefits	*3,485*	*3,298*	*7,151*	*6,822*
Occupancy expense	*526*	*586*	*1,129*	*1,173*
Equipment expense	*323*	*446*	*637*	*906*
Advertising expense	*213*	*191*	*326*	*305*
Data processing expense	*647*	*509*	*1,295*	*996*
Regulatory assessments	*196*	*164*	*397*	*337*
Bank shares tax	*222*	*252*	*489*	*510*
Expense of other real estate owned	*55*	*288*	*100*	*328*
Professional fees	*196*	*180*	*492*	*456*
Insurance expense	*133*	*128*	*268*	*253*
Other losses	*86*	*147*	*127*	*285*
Other operating expenses	*884*	*751*	*1,787*	*1,497*
Total non-interest expense	*6,966*	*6,940*	*14,198*	*13,868*
Income before income tax expense	*2,920*	*2,702*	*5,365*	*5,705*
Income tax expense	*508*	*910*	*934*	*1,716*
Net income	$*2,412*	$*1,792*	$*4,431*	$*3,989*
Earnings per share				
Basic	$*0.14*	$*0.11*	$*0.26*	$*0.24*
Diluted	$*0.14*	$*0.11*	$*0.26*	$*0.24*
Cash dividends declared per common share	$*0.04*	$*0.03*	$*0.08*	$*0.06*
WEIGHTED AVERAGE NUMBER OF SHARES OUTSTANDING:				
Basic	*16,792,812*	*16,716,899*	*16,778,188*	*16,687,389*
Diluted	*16,819,286*	*16,736,995*	*16,801,426*	*16,704,056*

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

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FNCB BANCORP, INC. AND SUBSIDIARIES CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS) (unaudited)

(in thousands)	Three Months Ended June 30, 2018	Three Months Ended June 30, 2017	Six Months Ended June 30, 2018	Six Months Ended June 30, 2017
Net income	$2,412	$1,792	$4,431	$3,989
Other comprehensive (loss) income:				
Unrealized (losses) gains on securities available for sale	(1,840)	3,323	(6,816)	5,159
Taxes	387	(1,129)	1,431	(1,754)
Net of tax amount	(1,453)	2,194	(5,385)	3,405
Reclassification adjustment for losses (gains) included in net income	4	(693)	4	(971)
Taxes	(1)	235	(1)	330
Net of tax amount	3	(458)	3	(641)
Total other comprehensive (loss) income	(1,450)	1,736	(5,382)	2,764
Comprehensive income (loss)	$962	$3,528	$(951)	$6,753

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

FNCB BANCORP, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
Six Months Ended June 30, 2018 and 2017
(unaudited)

(in thousands, except share data)	Number of Common Shares	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive (Loss) Income	Total Shareholders' Equity
Balances, December 31, 2016	16,645,845	$ 20,807	$ 62,593	$ 8,531	$ (1,560)	$ 90,371
Net income for the period	-	-	-	3,989	-	3,989
Cash dividends paid, $0.06 per share	-	-	-	(1,003)	-	(1,003)
Restricted stock awards	-	-	167	-	-	167
Common shares issued under long-term incentive compensation plan	46,878	58	(58)	-	-	-
Common shares issued through dividend reinvestment / optional cash purchase plan	65,240	82	374	-	-	456
Other comprehensive income, net of tax of $1,424	-	-	-	-	2,764	2,764
Balances, June 30, 2017	16,757,963	$ 20,947	$ 63,076	$ 11,517	$ 1,204	$ 96,744
Balances, December 31, 2017	16,757,963	$ 20,947	$ 63,210	$ 6,779	$ (1,745)	$ 89,191
Net income for the period	-	-	-	4,431	-	4,431
Cash dividends paid, $0.08 per share	-	-	-	(1,343)	-	(1,343)
Reclassification of unrealized loss on equity securities, net of tax	-	-	-	(65)	65	-
Restricted stock awards	-	-	137	-	-	137
Common shares issued under long-term incentive compensation plan	46,358	58	(58)	-	-	-
Common shares issued through dividend reinvestment / optional cash purchase plan	12,776	16	85	(10)	-	91
Other comprehensive loss, net of tax of $1,430	-	-	-	-	(5,382)	(5,382)
Balances, June 30, 2018	16,817,097	$ 21,021	$ 63,374	$ 9,792	$ (7,062)	$ 87,125

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

FNCB BANCORP, INC. AND SUBSIDIARIES CONSOLIDATED STATEMENTS OF CASH FLOWS (unaudited)

(in thousands)	Six Months Ended June 30, 2018	2017
Cash flows from operating activities:		
Net income	$4,431	$3,989
Adjustments to reconcile net income to net cash provided by operating activities:		
Investment securities amortization, net	398	568
Equity in trust	(6)	(4)
Depreciation and amortization	1,341	1,317
Valuation adjustment for loan servicing rights	-	(4)
Stock-based compensation expense	137	167
Provision (credit) for loan and lease losses	1,600	(57)
Valuation adjustment for off-balance sheet commitments	(55)	18
Net loss (gain) on the sale of available-for-sale securities	4	(971)
Net loss on equity securities	26	-
Net gain on the sale of mortgage loans held for sale	(100)	(135)
Net gain on the sale of SBA guaranteed loans	(322)	(56)
Net gain on the sale of other real estate owned	(31)	(57)
Valuation adjustment of other real estate owned	17	240
Net gain on the sale of other repossessed assets	-	(47)
Loss on the disposition of bank premises and equipment	30	63
Income from bank-owned life insurance	(272)	(270)
Proceeds from the sale of mortgage loans held for sale	5,032	6,402
Funds used to originate mortgage loans held for sale	(4,466)	(6,288)
Decrease in net deferred tax assets	934	1,716
Increase in accrued interest receivable	(420)	(27)
Decrease in prepaid expenses and other assets	1,271	355
Increase (decrease) in accrued interest payable	90	(7)
Decrease in director indemnification liability	(2,553)	-
Decrease in accrued expenses and other liabilities	(512)	(1,401)
Total adjustments	2,143	1,522
Net cash provided by operating activities	6,574	5,511
Cash flows from investing activities:		
Maturities, calls and principal payments of debt securities available for sale	3,160	4,250
Proceeds from the sale of debt securities available for sale	4,559	76,486

Purchases of debt securities available for sale	(16,337)	(78,037)
(Purchase) redemption of the stock in Federal Home Loan Bank of Pittsburgh	(5,201)	1,029
Net (increase) decrease in loans to customers	(92,242)	45
Proceeds from the sale of SBA guaranteed loans	6,032	634
Proceeds from the sale of other real estate owned	470	808
Proceeds from the sale of other repossessed assets	-	280
Purchases of bank premises and equipment	(4,463)	(721)
Net cash (used in) provided by investing activities	(104,022)	4,774
Cash flows from financing activities:		
Net decrease in deposits	(47,205)	(82,389)
Net proceeds from Federal Home Loan Bank of Pittsburgh advances - overnight	72,590	2,070
Proceeds from Federal Home Loan Bank of Pittsburgh advances - term	73,929	22,890
Repayment of Federal Home Loan Bank of Pittsburgh advances - term	(17,236)	(38,594)
Proceeds from issuance of common shares, net of discount	91	456
Cash dividends paid	(1,343)	(1,003)
Net cash provided by (used in) financing activities	80,826	(96,570)
Net decrease in cash and cash equivalents	(16,622)	(86,285)
Cash and cash equivalents at beginning of period	37,746	112,445
Cash and cash equivalents at end of period	$21,124	$26,160
Supplemental cash flow information:		
Cash paid during the period for:		
Interest	$3,469	$2,206
Income taxes	18	122
Other transactions:		
Transfer of bank premises and equipment to other real estate owned	220	-
Loans transferred to other real estate owned and repossessed assets	-	80
Investor loans tranferred to other real estate owned or other assets	-	45
Available-for-sale securities purchased, not settled	-	3,134
Change in deferred gain on sale of other real estate owned	-	1

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

FNCB BANCORP, INC. and subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

Note *1.* Basis of Presentation

The consolidated financial statements of FNCB are comprised of the accounts of FNCB Bancorp, Inc., and its wholly-owned subsidiary, FNCB Bank (the "Bank"), as well as the Bank's wholly-owned subsidiaries (collectively, "FNCB"). The accounting and reporting policies of FNCB conform to accounting principles generally accepted in the United States of America ("GAAP") for interim financial information and with the instructions to Form *10*-Q and Article *10-01* of Regulation S-*X.* Accordingly, they do *not* include all the information and accompanying notes required by GAAP for complete financial statements. In the opinion of management, all adjustments necessary for a fair presentation of the financial position and the results of operations for the periods presented have been included in the consolidated financial statements. All intercompany balances and transactions have been eliminated in consolidation. Prior period amounts have been reclassified when necessary to conform to the current period's presentation. Such reclassifications did *not* have an impact on the operating results or financial position of FNCB. The operating results and financial position of FNCB for the *three* and *six* months ended *June 30, 2018, may not* be indicative of future results of operations and financial position.

The preparation of financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ significantly from those estimates. Material estimates that are particularly susceptible to change in the near term are the allowance for loan and lease losses ("ALLL"), securities' valuation and impairment evaluation, the valuation of other real estate owned ("OREO"), and income taxes.

These financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in FNCB's audited financial statements, included in the Annual Report filed on Form *10*-K as of and for the year ended *December 31, 2017.*

Note *2.* New Authoritative Accounting Guidance

Accounting Guidance to be Adopted in Future Periods

ASU 2016-02, Leases (Topic 842): “Leases” will require organizations that lease assets to recognize on the balance sheet the assets and liabilities for the rights and obligations created by those leases with lease terms of more than 12 months. Consistent with current GAAP, the recognition, measurement and presentation of expenses and cash flows arising from a lease by the lessee will primarily depend on its classification as a finance or operating lease. However, unlike current GAAP, which requires only capital leases to be recognized on the balance sheet, the new ASU will require both finance and operating leases to be recognized on the balance sheet. ASU 2016-02 will also require disclosures to help investors and other financial statement users better understand the amount, timing and uncertainty of cash flows arising from leases. The new disclosures will include both qualitative and quantitative requirements that provide additional information about the amounts recorded in the financial statements. ASU 2016-02 is effective with fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018 for public entities. Accordingly, FNCB will adopt this guidance on January 1, 2019. Management is currently evaluating the effect this guidance may have on its operating results or financial position, including working with various business units within the organization and reviewing contractual arrangements for embedded leases in an effort to identify FNCB’s full lease population. Upon adoption, FNCB will recognize right-of-use assets and lease liabilities for the majority of its operating lease commitments. The amounts of right-to-use assets and corresponding lease liabilities recorded upon adoption will be based primarily on the present value of unpaid future minimum lease payments as of January 1, 2019. The amounts will also be impacted by assumptions around renewals and/or extensions, and the interest rate used to discount those future lease obligations. As of December 31, 2017, FNCB reported approximately $825 thousand in minimum lease payments due under such agreements for the period January 1, 2019 and forward. While these leases represent a majority of the leases within the scope of the standard, the lease portfolio is subject to change as a result of the execution of new leases and the termination of existing leases prior to the effective date, as well as the identification of potential embedded and other leases through the date of adoption.

ASU *2016-13,* Financial Instruments – Credit Losses (Topic *326*): "Measurement of Credit Losses on Financial Instruments," replaces the current loss impairment methodology under GAAP with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to form credit loss estimates in an effort to provide financial statement users with more decision-useful information about the expected credit losses on financial instruments and other commitments to extend credit. Specifically, the amendments in this ASU will require a financial asset (or a group of financial assets) measured at amortized cost basis to be presented at the net amount expected to be collected. The amendments in this update affect entities holding financial assets and net investment in leases that are *not* accounted for at fair value through net income, including such financial assets as loans, debt securities, trade receivables, net investments in leases, off-balance-sheet credit exposures, reinsurance receivables, and any other financial assets *not* excluded from the scope that have the contractual right to receive cash. On *June 17, 2016,* the four, federal financial institution regulatory agencies (the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the National Credit Union Administration and the Office of the Comptroller of the Currency), issued a joint statement to provide information about ASU *2016-13* and the initial supervisory views regarding the implementation of the new standard. The joint statement applies to all banks, savings associations, credit unions and financial institution holding companies, regardless of asset size. The statement details the key elements of, and the steps necessary for, the successful transition to the new accounting standard. In addition, the statement notifies financial institutions that because the appropriate allowance levels are institution-specific amounts, the agencies will *not* establish benchmark targets or ranges for the change in institutions' allowance levels upon adoption of the ASU, or for allowance levels going forward. Due to the importance of ASU *2016-13,* the agencies encourage financial institutions to begin planning and preparing for the transition and state that senior management, under the oversight of the board of directors, should work closely with staff in their accounting, lending, credit risk management, internal audit, and information technology functions during the transition period leading up to, and well after, adoption. ASU *2016-13* is effective for public business entities that are U.S. Securities and Exchange Commission ("SEC") filers for fiscal years beginning after *December 15, 2019,* including interim periods within those fiscal years. All entities *may* adopt the amendments in this ASU earlier as of the fiscal years beginning after *December 15, 2018,* including interim periods within those fiscal years. Accordingly, FNCB will adopt this guidance on *January 1, 2020.* FNCB has created a Current Expected Credit Loss ("CECL") task group comprised of members of its finance, credit administration, lending, internal audit, loan operations and information systems units. The CECL task group has become familiar with the provisions of ASU *2016-13* and is in the process of planning and preparing for the transition to the new guidance, which includes, but is *not* limited to: (*1*) developing an appropriate course of action for FNCB taking into consideration the nature, scope, and risk of its lending and investing activities; (*2*) identifying segments and sub-segments within the loan portfolio that have similar risk characteristics; (*3*) reviewing the existing allowance and credit risk management practices to identify processes that *may* be leveraged when applying the new guidance; (*4*) identifying data needs and implementing changes that are necessary to its core operating system and interfaces to be able to capture data requirements; and (*5*) evaluating the effect this guidance *may* have on FNCB's operating results and/or financial position, including assessing any potential impact on its capital.

Refer to Note *2* to FNCB's consolidated financial statements included in the *2017* Annual Report on Form *10*-K and the Quarterly Report on Form 10-Q for the period ended March 31, 2018 for a discussion of additional accounting guidance applicable to FNCB that will be adopted in future periods and accounting guidance previously adopted by FNCB during the three months ended March 31, 2018.

Note *3.* Securities

During the *third* quarter of *2017,* management identified *two* subordinated notes issued by other financial institutions in the amount of *$1.0* million each and *$1.0* million in mandatory-redeemable preferred stock of a subsidiary of another financial institution that were included in loans receivable at *December 31, 2016* and *2015* and the interim periods ended *March 31, 2017* and *June 30, 2017.* Management determined that these financial instruments are in fact securities and upon identification reclassified the recorded investment in these instruments of *$3.0* million from loans receivable to available-for-sale securities. Management also conducted an assessment of materiality of the reclassification to determine if FNCB's previously-issued consolidated financial statements should be amended. Based on its qualitative and quantitative assessment of materiality, management determined that the reclassification did *not* have a material impact to FNCB's financial position or results of operations as of and for the years, and interim periods within those years, ended *December 31, 2016* and *2015,* and interim periods ended *March 31, 2017* and *June 30, 2017.* Accordingly, management concluded that FNCB's previously-issued consolidated financial statements and notes to the consolidated financial statements could still be relied upon. However, management has elected to correct the error in these current-period consolidated financial statements and notes to the consolidated financial statements by adjusting the prior-period information for comparability. These reclassifications and valuations had *no* effect on the consolidated statements of income, the consolidated statements of cash flows, or on earnings per share for the annual and interim periods of *2016* and *first two* interim periods of *2017.*

Debt Securities

The following tables present the amortized cost, gross unrealized gains and losses, and the fair value of FNCB's available-for-sale debt securities at *June 30, 2018* and *December 31, 2017:*

	June 30, 2018			
(in thousands)	**Amortized Cost**	**Gross Unrealized Holding Gains**	**Gross Unrealized Holding Losses**	**Fair Value**
Available-for-sale debt securities:				
Obligations of state and political subdivisions	$*154,461*	$ *9*	$ *4,015*	$*150,455*
U.S. government/government-sponsored agencies:				
Collateralized mortgage obligations - residential	*35,144*	-	*1,183*	*33,961*
Collateralized mortgage obligations - commercial	*76,219*	-	*3,145*	*73,074*
Mortgage-backed securities	*24,666*	*21*	*531*	*24,156*
Corporate debt securities	*4,000*	-	*43*	*3,957*
Asset-backed securities	*2,388*	-	*33*	*2,355*
Negotiable certificates of deposit	*2,924*	-	*19*	*2,905*
Total available-for-sale debt securities	$*299,802*	$ *30*	$ *8,969*	$*290,863*

	December 31, 2017			
(in thousands)	**Amortized Cost**	**Gross Unrealized Holding Gains**	**Gross Unrealized Holding Losses**	**Fair Value**
Available-for-sale debt securities:				
Obligations of state and political subdivisions	$*146,812*	$ *567*	$ *1,380*	$*145,999*
U.S. government/government-sponsored agencies:				
Collateralized mortgage obligations - residential	*36,100*	*73*	*516*	*35,657*
Collateralized mortgage obligations - commercial	*76,396*	-	*978*	*75,418*
Mortgage-backed securities	*22,254*	*174*	*117*	*22,311*
Corporate debt securities	*4,000*	*58*	-	*4,058*
Asset-backed securities	*3,100*	*3*	*17*	*3,086*
Negotiable certificates of deposit	*2,924*	*6*	-	*2,930*
Total available-for-sale debt securities	$*291,586*	$ *881*	$ *3,008*	$*289,459*

Except for securities of U.S. government and government-sponsored agencies there were *no* securities of any individual issuer that exceeded *10.0%* of shareholders' equity at *June 30, 2018.*

At *June 30, 2018* and *December 31, 2017,* securities with a carrying amount of *$284.6* million and *$282.3* million, respectively, were pledged as collateral to secure public deposits and for other purposes.

The following table presents the maturity information of FNCB's available-for-sale debt securities at *June 30, 2018.* Expected maturities will differ from contractual maturity because issuers *may* have the right to call or prepay obligations with or without call or prepayment penalties. Because collateralized mortgage obligations, mortgage-backed securities and asset-backed securities are *not* due at a single maturity date, they are *not* included in the maturity categories in the following maturity summary:

(in thousands)	**June 30, 2018** **Amortized Cost**	 **Fair Value**
Amounts maturing in:		
One year or less	$*496*	$*495*
After one year through five years	*54,566*	*53,649*
After five years through ten years	*102,255*	*99,240*
After ten years	*4,068*	*3,933*
Asset-backed securities	*2,388*	*2,355*
Collateralized mortgage obligations	*111,363*	*107,035*
Mortgage-backed securities	*24,666*	*24,156*
Total	$*299,802*	$*290,863*

Gross proceeds from the sale of available-for-sale debt securities were *$4.6* million for the *three* and *six* months ended *June 30, 2018,* with gross losses of *$4* thousand realized upon the sales. There were *no* gains realized upon the sales for the *three* and *six* months ended *June 30, 2018.*

Gross proceeds from the sale of available-for-sale debt securities were *$53.3* million and *$76.5* million for the *three* and *six* months ended *June 30, 2017,* respectively, with gross gains of *$736* thousand and *$1,014* thousand, respectively, realized upon the sales. Gross losses realized upon the sales were *$43* thousand for the *three* and *six* months ended *June 30, 2017.*

The following tables present the number, fair value and gross unrealized losses of available-for-sale debt securities with unrealized losses at *June 30, 2018* and *December 31, 2017,* aggregated by investment category and length of time the securities have been in an unrealized loss position.

	June 30, 2018								
	Less than 12 Months			**12 Months or Longer**			**Total**		
(dollars in thousands)	**Number of Securities**	**Fair Value**	**Gross Unrealized Losses**	**Number of Securities**	**Fair Value**	**Gross Unrealized Losses**	**Number of Securities**	**Fair Value**	**Gross Unrealized Losses**
Obligations of state and political subdivisions	*109*	$*121,305*	$*2,492*	*27*	$*26,559*	$*1,523*	*136*	$*147,864*	$*4,015*

U.S. government/government-sponsored agencies:									
Collateralized mortgage obligations - residential	*14*	*32,961*	*1,183*	*1*	*16*	*-*	*15*	*32,977*	*1,183*
Collateralized mortgage obligations - commercial	*23*	*63,283*	*2,578*	*2*	*9,790*	*567*	*25*	*73,073*	*3,145*
Mortgage-backed securities	*8*	*18,650*	*405*	*2*	*1,985*	*126*	*10*	*20,635*	*531*
Corporate debt securities	*3*	*3,957*	*43*	*-*	*-*	*-*	*3*	*3,957*	*43*
Asset-backed securities	*1*	*492*	*3*	*1*	*1,863*	*30*	*2*	*2,355*	*33*
Negotiable certificates of deposit	*12*	*2,905*	*19*	*-*	*-*	*-*	*12*	*2,905*	*19*
Total	*170*	$*243,553*	$*6,723*	*33*	$*40,213*	$*2,246*	*203*	$*283,766*	$*8,969*

	December 31, 2017								
	Less than 12 Months			**12 Months or Longer**			**Total**		
(dollars in thousands)	**Number of Securities**	**Fair Value**	**Gross Unrealized Losses**	**Number of Securities**	**Fair Value**	**Gross Unrealized Losses**	**Number of Securities**	**Fair Value**	**Gross Unrealized Losses**
Obligations of state and political subdivisions	*56*	$*65,056*	$*497*	*26*	$*24,595*	$*883*	*82*	$*89,651*	$*1,380*
U.S. government/government-sponsored agencies:									
Collateralized mortgage obligations - residential	*10*	*24,686*	*516*	*1*	*53*	*-*	*11*	*24,739*	*516*
Collateralized mortgage obligations - commercial	*22*	*64,344*	*672*	*2*	*10,076*	*306*	*24*	*74,420*	*978*
Mortgage-backed securities	*4*	*8,454*	*56*	*2*	*2,058*	*61*	*6*	*10,512*	*117*
Corporate debt securities	-	-	-	-	-	-	-	-	-
Asset-backed securities	*1*	*2,443*	*17*	*-*	*-*	*-*	*1*	*2,443*	*17*
Negotiable certificates of deposit	*1*	*247*	*-*	*-*	*-*	*-*	*1*	*247*	*-*
Total	*94*	$*165,230*	$*1,758*	*31*	$*36,782*	$*1,250*	*125*	$*202,012*	$*3,008*

Management evaluates individual securities in an unrealized loss position quarterly for other than temporary impairment ("OTTI"). As part of its evaluation, management considers, among other things, the length of time a security's fair value is less than its amortized cost, the severity of decline, any credit deterioration of the issuer, whether or *not* management intends to sell the security, and whether it is more likely than *not* that FNCB will be required to sell the security prior to recovery of its amortized cost.

There were *203* securities in an unrealized loss position at *June 30, 2018,* including *136* obligations of state and political subdivisions, *50* securities issued by a U.S. government or government-sponsored agency, *12* negotiable certificates of deposit, *two* asset-backed securities and *three* corporate bonds. Management performed a review of all securities in an unrealized loss position as of *June 30,2018,* and determined that movements in the fair values of the securities were consistent with changes in market interest rates. In addition, as part of its review, management noted that there was *no* material change in the credit quality of any of the issuers or any other event or circumstance that *may* cause a significant adverse effect on the fair value of these securities. Moreover, to date, FNCB has received all scheduled principal and interest payments and expects to fully collect all future contractual principal and interest payments on all securities in an unrealized loss position at *June 30, 2018.* FNCB does *not* intend to sell the securities, nor is it more likely than *not* that it will be required to sell the securities, prior to recovery of their amortized cost. Based on the results of its review and considering the attributes of these debt securities, management concluded that the individual unrealized losses were temporary and OTTI did *not* exist at *June 30, 2018.*

Equity Securities

FNCB's investment in equity securities is comprised entirely of a mutual fund investment comprised of *one*-to *four*-family residential mortgage-backed securities collateralized by properties within FNCB's geographical market. At *December 31, 2017,* this mutual fund had an amortized cost of *$1.0* million and an unrealized loss of *$82* thousand, resulting in a fair value of *$918* thousand. In accordance with ASU *2016-01,* Financial Instruments – Overall (Subtopic *825-10*): "Recognition and Measurement of Financial Assets and Financial Liabilities" which became effective *January 1, 2018,* FNCB will recognize any changes in the fair value of this equity security in the consolidated statements of income on a prospective basis. As a result of the adoption of this new accounting guidance on *January 1, 2018,* FNCB recorded a *one*-time reclassification between retained earnings and accumulated other comprehensive loss for the unrealized loss on this mutual fund, net of taxes, of *$65* thousand. During the *three* and *six* months ended *June 30, 2018,* the fair value of this equity security declined by *$7* thousand and *$26* thousand, respectively, which is included in net loss on equity securities in the consolidated statements of income. The following table presents unrealized and realized gains and losses recognized in net income on equity securities for the *six* months ended *June 30, 2018.*

For the Six Months Ended June 30,	
(in thousands)	**2018**
Net losses recognized on equity securities	$ *(26*)
Less: net gains (losses) recognized on equity securities sold	-
Unrealized losses on equity securities held	$ *(26*)

Restricted Securities

The following table presents FNCB's investment in restricted securities at *June 30, 2018* and *December 31, 2017.* Restricted securities have limited marketability and are carried at cost:

(in thousands)	**June 30, 2018**	**December 31, 2017**
Stock in Federal Home Loan Bank of Pittsburgh	$*7,954*	$ *2,753*
Stock in Atlantic Community Bankers Bank	*10*	*10*
Total restricted securities, at cost	$*7,964*	$ *2,763*

Management noted *no* indicators of impairment for the Federal Home Loan Bank ("FHLB") of Pittsburgh or Atlantic Community Bankers Bank stock at *June 30, 2018* and *December 31, 2017.*

Equity Securities without Readily Determinable Fair Values

FNCB owns a *$1.7* million investment in the common stock of a privately-held bank holding company. The common stock was purchased during *2017* as part of a private placement pursuant to an exemption from the registration requirements of the Securities Act of *1933* for offerings *not* involving any public offering. The common stock of such bank holding company is *not* currently traded on any established market, and is *not* expected to be traded in the near future on any securities exchange or established over-the-counter market. FNCB has elected to account for this transaction as an investment in an equity security without a readily determinable fair value. An equity security without a readily determinable fair value shall be written down to its fair value if a qualitative assessment indicates that the investment is impaired and the fair value of the investment is less than its carrying value. The *$1.7* million investment is included in other assets in the consolidated statements of financial condition at *June 30, 2018.* As part of its qualitative assessment, management engaged an independent *third* party to provide a valuation of this investment as of *June 30, 2018,* which indicated that the investment was *not* impaired. Management determined that *no* adjustment for impairment was required at *June 30, 2018.*

Note *4.* Loans

The following table summarizes loans receivable, net, by category at *June 30, 2018* and *December 31, 2017:*

(in thousands)	**June 30, 2018**	**December 31, 2017**
Residential real estate	$*168,827*	$*158,020*
Commercial real estate	*260,119*	*261,783*
Construction, land acquisition and development	*23,340*	*20,981*
Commercial and industrial	*167,001*	*150,103*
Consumer	*179,088*	*134,653*
State and political subdivisions	*52,954*	*42,529*
Total loans, gross	*851,329*	*768,069*
Unearned income	*(75*)	*(80*)
Net deferred loan costs	*4,137*	*2,654*
Allowance for loan and lease losses	*(9,459*)	*(9,034*)
Loans, net	$*845,932*	$*761,609*

FNCB has granted loans, letters of credit and lines of credit to certain of its executive officers and directors as well as to certain of their related parties. For more information about related party transactions, refer to Note *7,* "Related Party Transactions" to these consolidated financial statements.

FNCB originates *one*- to *four*-family mortgage loans for sale in the secondary market. During the *three* and *six* months ended *June 30, 2018, one*- to *four*-family mortgages sold on the secondary market were *$2.1* million and *$5.0* million, respectively. Net gains on the sale of residential mortgage loans for the *three* and *six* months ended *June 30, 2018* were *$51* thousand and *$100* thousand, respectively, and *$110* thousand and *$135* thousand, respectively, for the comparable periods of *2017.* FNCB retains servicing rights on these mortgages. At *June 30, 2018* and *December 31, 2017,* there were *$629* thousand and *$1.1* million *one*- to *four*-family residential mortgage loans held for sale, respectively.

During the *three* and *six* months ended *June 30, 2018,* FNCB sold the guaranteed principal balance of loans that were guaranteed by the Small Business Administration ("SBA") totaling *$0.8* million and *$5.7* million, respectively. Net gains of *$71* thousand and *$322* thousand were realized upon the sales and included in non-interest income for the *three* and *six* months ended *June 30, 2018,* respectively. FNCB retained the servicing rights on these loans. For both the *three* and *six* months ended *June 30, 2017,* FNCB sold the guaranteed balance of loans of *$0.6* million and realized net gains on the sales of *$56* thousand. The unpaid principal balance of loans serviced for others, including residential mortgages and SBA guaranteed loans were *$108.5* million at *June 30, 2018* and *$103.0* million at *December 31, 2017.*

FNCB does *not* have any lending programs commonly referred to as subprime lending. Subprime lending generally targets borrowers with weakened credit histories typically characterized by payment delinquencies, previous charge-offs, judgments, and bankruptcies, or borrowers with questionable repayment capacity as evidenced by low credit scores or high debt-burden ratios.

There were *no* material changes to the risk characteristics of FNCB's loan segments, loan classification and credit grading systems and methodology for determining the adequacy of the ALLL during the *six* months ended *June 30, 2018.* Refer to Note *2,* "Summary of Significant Accounting Policies" to FNCB's consolidated financial statements included in the *2017* Annual Report on Form *10*-K for information about the risk characteristics related to FNCB's loan segments, loan classification and credit grading systems and methodology for determining the adequacy of the ALLL.

Management evaluates the credit quality of the loan portfolio on an ongoing basis, and performs a formal review of the adequacy of the ALLL on a quarterly basis. This evaluation is inherently subjective, as it requires material estimates that *may* be susceptible to significant revisions based upon changes in economic and real estate market conditions. Actual loan losses *may* be significantly more than the established ALLL, which could have a material negative effect on FNCB's operating results or financial condition. While management uses the best information available to make its evaluations, future adjustments to the ALLL *may* be necessary if conditions differ substantially from the information used in making the evaluations. Banking regulators, as an integral part of their examination of FNCB, also review the ALLL, and *may* require, based on their judgments about information available to them at the time of their examination, that certain loan balances be charged off or require that adjustments be made to the ALLL.

The following table summarizes activity in the ALLL by loan category for the *three* and *six* months ended *June 30, 2018* and *2017:*

(in thousands)	Residential Real Estate	Commercial Real Estate	Construction, Land Acquisition and Development	Commercial and Industrial	Consumer	State and Political Subdivisions	Total
Three months ended June 30, 2018:							
Allowance for loan losses:							
Beginning balance, April 1, 2018	$ *1,249*	$ *3,342*	$ *256*	$ *2,505*	$ *1,822*	$ *388*	$ *9,562*
Charge-offs	-	*(1,126*)	-	*(4*)	*(180*)	-	*(1,310*)
Recoveries	*121*	*2*	-	*75*	*129*	-	*327*
Provisions (credits)	*(169*)	*889*	*(5*)	*(121*)	*235*	*51*	*880*
Ending balance, June 30, 2018	$ *1,201*	$ *3,107*	$ *251*	$ *2,455*	$ *2,006*	$ *439*	$ *9,459*
Three months ended June 30, 2017:							
Allowance for loan losses:							

Beginning balance, April 1, 2017	$ *1,144*	$ *3,501*	$ *223*	$ *1,679*	$ *1,410*	$ *349*	$ *8,306*
Charge-offs	*(31*)	*(29*)	-	*(317*)	*(88*)	-	*(465*)
Recoveries	*11*	*1*	-	*110*	*85*	-	*207*
Provisions (credits)	*24*	*(451*)	*13*	*841*	*35*	*(41*)	*421*
Ending balance, June 30, 2017	$ *1,148*	$ *3,022*	$ *236*	$ *2,313*	$ *1,442*	$ *308*	$ *8,469*
Six months ended June 30, 2018:							
Allowance for loan losses:							
Beginning balance, January 1, 2018	$ *1,236*	$ *3,499*	$ *209*	$ *2,340*	$ *1,395*	$ *355*	$ *9,034*
Charge-offs	*(63*)	*(1,126*)	-	*(81*)	*(440*)	-	*(1,710*)
Recoveries	*127*	*3*	*30*	*147*	*228*	-	*535*
Provisions (credits)	*(99*)	*731*	*12*	*49*	*823*	*84*	*1,600*
Ending balance, June 30, 2018	$ *1,201*	$ *3,107*	$ *251*	$ *2,455*	$ *2,006*	$ *439*	$ *9,459*
Six months ended June 30, 2017:							
Allowance for loan losses:							
Beginning balance, January 1, 2017	$ *1,171*	$ *3,297*	$ *268*	$ *1,736*	$ *1,457*	$ *490*	$ *8,419*
Charge-offs	*(80*)	*(29*)	-	*(347*)	*(306*)	-	*(762*)
Recoveries	*12*	*5*	*421*	*179*	*252*	-	*869*
Provisions (credits)	*45*	*(251*)	*(453*)	*745*	*39*	*(182*)	*(57*)
Ending balance, June 30, 2017	$ *1,148*	$ *3,022*	$ *236*	$ *2,313*	$ *1,442*	$ *308*	$ *8,469*

The following table represents the allocation of the ALLL and the related loan balance, by loan category, disaggregated based on the impairment methodology at *June 30, 2018* and *December 31, 2017:*

(in thousands)	Residential Real Estate	Commercial Real Estate	Construction, Land Acquisition and Development	Commercial and Industrial	Consumer	State and Political Subdivisions	Total
June 30, 2018							
Allowance for loan losses:							
Individually evaluated for impairment	$ *8*	$ *86*	$ *-*	$ *600*	$ *2*	$ *-*	$ *696*
Collectively evaluated for impairment	*1,193*	*3,021*	*251*	*1,855*	*2,004*	*439*	*8,763*
Total	$ *1,201*	$ *3,107*	$ *251*	$ *2,455*	$ *2,006*	$ *439*	$ *9,459*
Loans receivable:							
Individually evaluated for impairment	$ *1,801*	$ *8,464*	$ *83*	$ *793*	$ *388*	$ *-*	$ *11,529*
Collectively evaluated for impairment	*167,026*	*251,655*	*23,257*	*166,208*	*178,700*	*52,954*	*839,800*
Total	$ *168,827*	$ *260,119*	$ *23,340*	$ *167,001*	$ *179,088*	$ *52,954*	$ *851,329*
December 31, 2017							
Allowance for loan losses:							
Individually evaluated for impairment	$ *33*	$ *138*	$ *-*	$ *600*	$ *2*	$ *-*	$ *773*
Collectively evaluated for impairment	*1,203*	*3,361*	*209*	*1,740*	*1,393*	*355*	*8,261*
Total	$ *1,236*	$ *3,499*	$ *209*	$ *2,340*	$ *1,395*	$ *355*	$ *9,034*
Loans receivable:							
Individually evaluated for impairment	$ *1,902*	$ *8,164*	$ *85*	$ *795*	$ *395*	$ *-*	$ *11,341*
Collectively evaluated for impairment	*156,118*	*253,619*	*20,896*	*149,308*	*134,258*	*42,529*	*756,728*
Total	$ *158,020*	$ *261,783*	$ *20,981*	$ *150,103*	$ *134,653*	$ *42,529*	$ *768,069*

Credit Quality Indicators – Commercial Loans

Management continuously monitors and evaluates the credit quality of FNCB’s commercial loans by regularly reviewing certain credit quality indicators. Management utilizes credit risk ratings as the key credit quality indicator for evaluating the credit quality of FNCB’s loan receivables.

FNCB’s loan rating system assigns a degree of risk to commercial loans 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. Management analyzes these non-homogeneous loans individually by grading the loans as to credit risk and probability of collection for each type of loan. Commercial and industrial loans include commercial indirect auto loans which are *not* individually risk rated, and construction, land acquisition and development loans include residential construction loans which are also *not* individually risk rated. These loans are monitored on a pool basis due to their homogeneous nature as described in “Credit Quality Indicators – Other Loans” below. FNCB risk rates certain residential real estate loans and consumer loans that are part of a larger commercial relationship using a credit grading system as described in “Credit Quality Indicators – Commercial Loans.” The grading system contains the following basic risk categories:

1. Minimal Risk

2. Above Average Credit Quality

3. Average Risk

4. Acceptable Risk

5. Pass - Watch

6. Special Mention

7. Substandard - Accruing

8. Substandard - Non-Accrual

9. Doubtful

10. Loss

This analysis is performed on a quarterly basis using the following definitions for risk ratings:

Pass – Assets rated *1* through *5* are considered pass ratings. These assets show *no* current or potential problems and are considered fully collectible. All such loans are evaluated collectively for ALLL calculation purposes. However, accruing loans restructured under a troubled debt restructuring (“TDRs”) that have been performing for an extended period, do *not* represent a higher risk of loss, and have been upgraded to a pass rating are evaluated individually for impairment.

Special Mention – Assets classified as special mention do *not* currently expose FNCB to a sufficient degree of risk to warrant an adverse classification but do possess credit deficiencies or potential weaknesses deserving close attention. Special mention assets have a potential weakness or pose an unwarranted financial risk which, if *not* corrected, could weaken the asset and increase risk in the future.

Substandard – Assets classified as substandard have well defined weaknesses based on objective evidence, and are characterized by the distinct possibility that FNCB will sustain some loss if the deficiencies are *not* corrected.

Doubtful – Assets classified as doubtful have all the weaknesses inherent in those classified as substandard with the added characteristic that such weaknesses make collection or liquidation in full highly questionable and improbable based on current circumstances.

Loss – Assets classified as loss are those considered uncollectible and of such little value that their continuance as assets is *not* warranted.

Credit Quality Indicators – Other Loans

Certain residential real estate loans, consumer loans, and commercial indirect auto loans are monitored on a pool basis due to their homogeneous nature. Loans that are delinquent *90* days or more are placed on non-accrual status unless collection of the loan is in process and reasonably assured. FNCB utilizes accruing versus non-accrual status as the credit quality indicator for these loan pools.

The following tables present the recorded investment in loans receivable by loan category and credit quality indicator at *June 30, 2018* and *December 31, 2017:*

	Credit Quality Indicators June 30, 2018									
	Commercial Loans						**Other Loans**			
(in thousands)	**Pass**	**Special Mention**	**Substandard**	**Doubtful**	**Loss**	**Subtotal Commercial**	**Accruing Loans**	**Non-accrual Loans**	**Subtotal Other**	**Total Loans**
Residential real estate	$ *34,346*	$ *411*	$ *134*	$ -	$ -	$ *34,891*	$ *133,602*	$ *334*	$ *133,936*	$ *168,827*
Commercial real estate	*246,509*	*2,253*	*11,357*	-	-	*260,119*	-	-	-	*260,119*

Construction, land acquisition and development	*20,990*	*324*	*575*	-	-	*21,889*	*1,451*	-	*1,451*	*23,340*
Commercial and industrial	*157,690*	*649*	*2,353*	-	-	*160,692*	*6,309*	-	*6,309*	*167,001*
Consumer	*2,040*	*35*	-	-	-	*2,075*	*176,724*	*289*	*177,013*	*179,088*
State and political subdivisions	*51,768*	*1,020*	*102*	-	-	*52,890*	*64*	-	*64*	*52,954*
Total	$*513,343*	$*4,692*	$ *14,521*	$ -	$ -	$*532,556*	$*318,150*	$ *623*	$*318,773*	$*851,329*

	Credit Quality Indicators December 31, 2017									
	Commercial Loans						**Other Loans**			
(in thousands)	**Pass**	**Special Mention**	**Substandard**	**Doubtful**	**Loss**	**Subtotal Commercial**	**Accruing Loans**	**Non-accrual Loans**	**Subtotal Other**	**Total Loans**
Residential real estate	$*27,186*	$*421*	$ *62*	$ -	$ -	$ *27,669*	$*129,887*	$ *464*	$*130,351*	$*158,020*
Commercial real estate	*245,779*	*2,461*	*13,543*	-	-	*261,783*	-	-	-	*261,783*
Construction, land acquisition and development	*18,280*	*330*	*6*	-	-	*18,616*	*2,365*	-	*2,365*	*20,981*
Commercial and industrial	*142,019*	*479*	*1,597*	-	-	*144,095*	*6,008*	-	*6,008*	*150,103*
Consumer	*1,731*	-	*34*	-	-	*1,765*	*132,584*	*304*	*132,888*	*134,653*
State and political subdivisions	*42,040*	-	*396*	-	-	*42,436*	*93*	-	*93*	*42,529*
Total	$*477,035*	$*3,691*	$ *15,638*	$ -	$ -	$*496,364*	$*270,937*	$ *768*	$*271,705*	$*768,069*

Included in loans receivable are loans for which the accrual of interest income has been discontinued due to deterioration in the financial condition of the borrowers. The recorded investment in these non-accrual loans was *$3.5* million and *$2.6* million at *June 30, 2018* and *December 31, 2017,* respectively. Generally, loans are placed on non-accrual status when they become *90* days or more delinquent and remain on non-accrual status until they are brought current, have *six* months of performance under the loan terms, and factors indicating reasonable doubt about the timely collection of payments *no* longer exist. Therefore, loans *may* be current in accordance with their loan terms, or *may* be less than *90* days delinquent, and still be on a non-accrual status. There were *no* loans past due *90* days or more and still accruing at *June 30, 2018* and *December 31, 2017.*

The following tables present the delinquency status of past due and non-accrual loans at *June 30, 2018* and *December 31, 2017:*

	June 30, 2018 Delinquency Status				
(in thousands)	**0-29 Days Past Due**	**30-59 Days Past Due**	**60-89 Days Past Due**	**>/= 90 Days Past Due**	**Total**
Performing (accruing) loans:					
Residential real estate	$*167,523*	$*827*	$*20*	$-	$*168,370*
Commercial real estate	*258,268*	-	-	-	*258,268*
Construction, land acquisition and development	*23,257*	-	*83*	-	*23,340*
Commercial and industrial	*165,873*	*223*	*33*	-	*166,129*
Consumer	*177,430*	*1,104*	*265*	-	*178,799*
State and political subdivisions	*52,954*	-	-	-	*52,954*
Total performing (accruing) loans	*845,305*	*2,154*	*401*	-	*847,860*
Non-accrual loans:					
Residential real estate	*317*	-	-	*140*	*457*
Commercial real estate	*1,126*	-	-	*725*	*1,851*
Construction, land aquisition and development	-	-	-	-	-
Commercial and industrial	*750*	-	*83*	*39*	*872*
Consumer	*50*	*68*	*53*	*118*	*289*
State and political subdivisions	-	-	-	-	-
Total non-accrual loans	*2,243*	*68*	*136*	*1,022*	*3,469*
Total loans receivable	$*847,548*	$*2,222*	$*537*	$*1,022*	$*851,329*

	December 31, 2017 Delinquency Status				
(in thousands)	**0-29 Days Past Due**	**30-59 Days Past Due**	**60-89 Days Past Due**	**>/= 90 Days Past Due**	**Total**
Performing (accruing) loans:					
Residential real estate	$*156,701*	$*793*	$-	$-	$*157,494*
Commercial real estate	*260,276*	*70*	*473*	-	*260,819*
Construction, land acquisition and development	*20,954*	*27*	-	-	*20,981*
Commercial and industrial	*149,046*	*185*	*88*	-	*149,319*
Consumer	*133,034*	*1,028*	*287*	-	*134,349*
State and political subdivisions	*42,529*	-	-	-	*42,529*
Total peforming (accruing) loans	*762,540*	*2,103*	*848*	-	*765,491*
Non-accrual loans:					

Residential real estate	*342*	*63*	-	*120*	*525*
Commercial real estate	-	-	-	*964*	*964*
Construction, land acquisition and development	-	-	-	-	-
Commercial and industrial	*750*	-	-	*35*	*785*
Consumer	*25*	*92*	*53*	*134*	*304*
State and political subdivisions	-	-	-	-	-
Total non-accrual loans	*1,117*	*155*	*53*	*1,253*	*2,578*
Total loans receivable	$*763,657*	$*2,258*	$*901*	$*1,253*	$*768,069*

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The following tables present a distribution of the recorded investment, unpaid principal balance and the related allowance for FNCB's impaired loans, which have been analyzed for impairment under ASC *310,* at *June 30, 2018* and *December 31, 2017.* Non-accrual loans, other than TDRs, with balances less than the *$100* thousand loan relationship threshold are *not* evaluated individually for impairment and accordingly, are *not* included in the following tables. However, these loans are evaluated collectively for impairment as homogenous pools in the general allowance under ASC Topic *450.* Total non-accrual loans, other than TDRs, with balances less than the *$100* thousand loan relationship threshold that were evaluated under ASC Topic *450* amounted to *$0.7* million at *June 30, 2018* and *$0.5* million at *December 31, 2017.*

	June 30, 2018		
(in thousands)	**Recorded Investment**	**Unpaid Principal Balance**	**Related Allowance**
With no related allowance recorded:			
Residential real estate	$ *205*	$ *277*	$ -
Commercial real estate	*6,160*	*7,023*	-
Construction, land acquisition and development	*83*	*83*	-
Commercial and industrial	*20*	*52*	-
Consumer	*28*	*29*	-
State and political subdivisions	-	-	-
Total impaired loans with no related allowance recorded	*6,496*	*7,464*	-
With a related allowance recorded:			
Residential real estate	*1,596*	*1,596*	*8*
Commercial real estate	*2,304*	*2,304*	*86*
Construction, land acquisition and development	-	-	-
Commercial and industrial	*773*	*773*	*600*
Consumer	*360*	*360*	*2*
State and political subdivisions	-	-	-
Total impaired loans with a related allowance recorded	*5,033*	*5,033*	*696*
Total impaired loans:			
Residential real estate	*1,801*	*1,873*	*8*
Commercial real estate	*8,464*	*9,327*	*86*
Construction, land acquisition and development	*83*	*83*	-
Commercial and industrial	*793*	*825*	*600*
Consumer	*388*	*389*	*2*
State and political subdivisions	-	-	-
Total impaired loans	$ *11,529*	$ *12,497*	$ *696*

(in thousands)	December 31, 2017 Recorded Investment	Unpaid Principal Balance	Related Allowance
With no related allowance recorded:			
Residential real estate	$ *190*	$ *216*	$ -
Commercial real estate	*5,174*	*5,295*	-
Construction, land acquisition and development	*85*	*85*	-
Commercial and industrial	*21*	*53*	-
Consumer	*30*	*30*	-
State and political subdivisions	-	-	-
Total impaired loans with no related allowance recorded	*5,500*	*5,679*	-
With a related allowance recorded:			
Residential real estate	*1,712*	*1,751*	*33*
Commercial real estate	*2,990*	*2,990*	*138*
Construction, land acquisition and development	-	-	-
Commercial and industrial	*774*	*774*	*600*
Consumer	*365*	*365*	*2*
State and political subdivisions	-	-	-
Total impaired loans with a related allowance recorded	*5,841*	*5,880*	*773*
Total impaired loans:			
Residential real estate	*1,902*	*1,967*	*33*
Commercial real estate	*8,164*	*8,285*	*138*
Construction, land acquisition and development	*85*	*85*	-
Commercial and industrial	*795*	*827*	*600*
Consumer	*395*	*395*	*2*
State and political subdivisions	-	-	-
Total impaired loans	$ *11,341*	$ *11,559*	$ *773*

The following table presents the average balance of, and interest income recognized on, impaired loans summarized by loan category for the *three* and *six* months ended *June 30, 2018* and *2017:*

(in thousands)	Three Months Ended June 30, 2018 Average Balance	Interest Income (1)	2017 Average Balance	Interest Income (1)	Six Months Ended June 30, 2018 Average Balance	Interest Income (1)	2017 Average Balance	Interest Income (1)
Residential real estate	$ *1,805*	$ *21*	$ *1,841*	$ *21*	$ *1,837*	$ *42*	$ *1,884*	$ *42*
Commercial real estate	*7,826*	*75*	*7,452*	*72*	*7,833*	*152*	*6,133*	*112*
Construction, land acquisition and development	*84*	*1*	*87*	*1*	*84*	*2*	*123*	*2*

Commercial and industrial	*794*	*1*	*1,059*	*9*	*794*	*1*	*879*	*14*
Consumer	*389*	*3*	*295*	*3*	*391*	*7*	*296*	*6*
State and political subdivisions	-	-	-	-	-	-	-	-
Total impaired loans	$*10,898*	$ *101*	$*10,734*	$ *106*	$*10,939*	$ *204*	$*9,315*	$ *176*

(*1*) Interest income represents income recognized on accruing TDRs.

The additional interest income that would have been earned on non-accrual and restructured loans had these loans performed in accordance with their original terms approximated *$45* thousand and *$85* thousand for the *three* and *six* months ended *June 30, 2018,* respectively, and *$39* thousand and *$66* thousand for the *three* and *six* months ended *June 30, 2017,* respectively.

Troubled Debt Restructured Loans

TDRs at *June 30, 2018* and *December 31, 2017* were *$9.6* million and *$10.2* million, respectively. Accruing and non-accruing TDRs were *$8.7* million and *$0.9* million, respectively at *June 30, 2018,* and *$9.3* million and *$0.9* million, respectively at *December 31, 2017.* Approximately *$696* thousand and *$750* thousand in specific reserves have been established for TDRs as of *June 30, 2018,* and *December 31, 2017,* respectively. FNCB was *not* committed to lend additional funds to any loan classified as a TDR at *June 30, 2018.*

The modification of the terms of such loans *may* include *one* or a combination of the following, among others: a reduction of the stated interest rate of the loan, an extension of the maturity date, capitalization of real estate taxes, a payment modification under a forbearance agreement, or a permanent reduction of the recorded investment in the loan.

There were *no* loans modified as TDRs during the *three* and *six* months ended *June 30, 2018.* The following tables present the pre- and post-modification recorded investment in loans modified as TDRs and type of modifications made during the *three* and *six* months ended *June 30, 2017.*

Three Months Ended June 30, 2017

		Pre-Modification Outstanding Recorded Investment by Type of Modification				Post-Modification
(in thousands)	**Number of Contracts**	**Forebearance**	**Extension of Term**	**Extension of Term and Forebearance**	**Total**	**Outstanding Recorded Investment**
Troubled debt restructurings:						
Residential real estate	*1*	$-	$ *63*	$ -	$*63*	$ *63*
Commercial real estate	*7*	*1,228*	-	-	*1,228*	*1,228*
Construction, land acquisition and development	-	-	-	-	-	-
Commercial and industrial	*3*	*1,125*	-	*25*	*1,150*	*1,150*
Consumer	-	-	-	-	-	-
States and political subdivisions	-	-	-	-	-	-
Total new troubled debt restructurings	*11*	$*2,353*	$ *63*	$ *25*	$*2,441*	$ *2,441*

Six Months Ended June 30, 2017

		Pre-Modification Outstanding Recorded Investment by Type of Modification				Post-Modification
(in thousands)	**Number of Contracts**	**Forebearance**	**Extension of Term**	**Extension of Term and Forebearance**	**Total**	**Outstanding Recorded Investment**
Troubled debt restructurings:						
Residential real estate	*1*	$-	$ *63*	$ -	$*63*	$ *63*

Commercial real estate	*8*	*5,250*	-	-	*5,250*	*5,250*
Construction, land acquisition and development	-	-	-	-	-	-
Commercial and industrial	*4*	*1,820*	-	*25*	*1,845*	*1,845*
Consumer	-	-	-	-	-	-
States and political subdivisions	-	-	-	-	-	-
Total new troubled debt restructurings	*13*	$*7,070*	$ *63*	$ *25*	$*7,158*	$ *7,158*

There were *six* loan relationships modified as TDRs during the *six* months ended *June 30, 2017,* which incorporated a total of *thirteen* individual loans. There were *three* loan relationships, comprised of *eight* commercial real estate loans totaling *$5.3* million, and *two* loan relationships comprised of *four* commercial and industrial loans totaling *$1.8* million, that were modified under varying forms of forbearance agreements during the *six* months ended *June 30, 2017.* In addition, there was *one* residential real estate loan in the amount of *$63* thousand that had its terms extended under a TDR. The commercial real estate modifications included a principal forbearance agreement for *one* loan in the amount of *$4.0* million and reductions in required monthly principal payments resulting in balloon payments due at maturity for *seven* loans to *two* borrowers aggregating *$1.2* million. The *four* commercial and industrial loan modifications involved the delay of required principal and interest payments for predefined time periods. In addition, a charge-off in the amount of *$0.3* million was recorded as part of the modification of *three* commercial and industrial loans aggregating *$1.8* million to *one* borrower.

There were *no* TDRs modified within the previous *12* months that defaulted (defined as past due *90* days or more) during the *three* and *six* months ended *June 30, 2018.* There was *one* construction, land acquisition and development loan in the amount of *$10* thousand that was modified during the previous *12* months that defaulted during the *six* months ended *June 30, 2017.*

Residential Real Estate Loan Foreclosures

There were *three* consumer mortgage loans secured by residential real estate properties with *no* aggregate recorded investment in the process of foreclosure at *June 30, 2018.* For the *three* and *six* months ended *June 30, 2018,* there were *no* residential real estate properties foreclosed upon, and there was *one* residential real estate property with an aggregate carrying value of *$63* thousand included in OREO at *June 30, 2018.*

There were *two* consumer mortgage loans secured by residential real estate properties with an aggregate recorded investment of *$89* thousand that were in the process of foreclosure at *June 30, 2017.* There was *one* residential real estate property with a carrying value of *$80* thousand that was foreclosed upon during the *three* months ended *June 30, 2017.* For the *six* months ended *June 30, 2017,* there were *two* residential real estate properties with an aggregate carrying value of *$125* thousand that were foreclosed upon. Of the *two* loans foreclosed upon during the *six* months ended *June 30, 2017, one* was an investor-owned residential real estate property with a carrying value of *$45* thousand. There were *four* residential real estate properties with an aggregate carrying value of *$166* thousand included in OREO at *June 30, 2017.*

Note *5.* Borrowed Funds

Short-term borrowings available to FNCB include overnight FHLB of Pittsburgh advances, federal funds purchased and the Federal Reserve Discount Window, which generally represent overnight or less than *30*-day borrowings.

FNCB has an agreement with the FHLB of Pittsburgh which allows for borrowings, either overnight or term, up to its maximum borrowing capacity, which is based on a percentage of qualifying loans pledged under a blanket pledge agreement. Loans of *$469.3* million and *$448.2* million at *June 30, 2018* and *December 31, 2017,* respectively, were pledged to collateralize borrowings under this agreement. FNCB's maximum borrowing capacity was *$328.6* million at *June 30, 2018,* of which *$101.7* million in fixed-rate advances having original maturities between *three* months and *five* years, as well as *$72.6* million in overnight advances, were outstanding. At *June 30, 2018,* FNCB also had *$39.5* million in deposit letters of credit outstanding, which are used to provide pledging for public deposits. In addition to pledging loans, FNCB is required to purchase FHLB of Pittsburgh stock based upon the amount of advances and letters of credit outstanding.

(in thousands)	**June 30, 2018**	**December 31, 2017**
FHLB of Pittsburgh advances - overnight	$72,590	$ -
FHLB of Pittsburgh advances - term	101,661	44,968
Subtotal FHLB of Pittsburgh advances	174,251	44,968
Subordinated debentures	5,000	5,000
Junior subordinated debentures	10,310	10,310
Total borrowed funds	$189,561	$ 60,278

Advances from the FHLB of Pittsburgh were *$174.3* million as of *June 30, 2018,* an increase of *$129.3* million, or *287.5%,* from *$45.0* million at *December 31, 2017.* The increase in FHLB borrowings during the *first six* months of *2018* was used primarily to fund growth in interest-earning assets.

There have been *no* other material changes in the status of FNCB's borrowed funds during the *six* months ended *June 30, 2018.* For additional information related to FNCB's borrowings, refer to Note *8* "Borrowed Funds", to the consolidated financial statements included in FNCB's Annual Report on Form *10*-K for the year ended *December 31, 2017.*

Note *6.* Income Taxes

On *December 22, 2017,* President Trump signed into law H.R 1, An Act to provide for reconciliation pursuant to titles II and V of the concurrent resolution on the budget for fiscal year *2018,* originally introduced in Congress and informally known as the "Tax Cuts and Jobs Act," which among other things, reduced the maximum federal corporate income tax rate from *35.0%* to *21.0%* effective *January 1, 2018.* The following table presents a reconciliation between the effective income tax expense and the income tax expense that would have been provided at the federal statutory tax rate of *21.0%* for the *three* and *six* months ended *June 30, 2018* and *34.0%* for the *three* and *six* months ended *June 30, 2017:*

	For the Three Months Ended June 30,				**For the Six Months Ended June 30,**			
	2018		**2017**		**2018**		**2017**	
(in thousands)	**Amount**	**%**	**Amount**	**%**	**Amount**	**%**	**Amount**	**%**
Provision at statutory tax rates	$*613*	*21.00*%	$*919*	*34.00*%	$*1,126*	*21.00*%	$*1,940*	*34.00*%
Add (deduct):								
Tax effects of non-taxable income	*(92*)	*(3.16* %)	*(112*)	*(4.14* %)	*(170*)	*(3.18* %)	*(234*)	*(4.10* %)
Non-deductible interest expense	*4*	*0.13* %	*3*	*0.09* %	*6*	*0.11* %	*6*	*0.10* %
Bank-owned life insurance	*(29*)	*(1.00* %)	*(46*)	*(1.70* %)	*(57*)	*(1.06* %)	*(92*)	*(1.61* %)
Other items, net	*12*	*0.43* %	*146*	*5.43* %	*29*	*0.54* %	*96*	*1.69* %
Income tax expense	$*508*	*17.40*%	$*910*	*33.68*%	$*934*	*17.41*%	$*1,716*	*30.08*%

FNCB had net deferred tax assets of *$16.3* million at *June 30, 2018,* of which *$8.5* million was related to *$40.5* million in net operating loss carryovers. At *December 31, 2017,* FNCB's net deferred tax assets were *$15.8* million.

Management evaluates the carrying amount of its deferred tax assets on a quarterly basis, or more frequently if necessary, in accordance with guidance set forth in ASC Topic *740* "Income Taxes," and applies the criteria in the guidance to determine whether it is more likely than *not* that some portion, or all, of the deferred tax asset will *not* be realized within its life cycle, based on the weight of available evidence. In evaluating available evidence, management considers, among other factors, historical financial performance, expectation of future earnings, the ability to carry back losses to recoup taxes previously paid, length of statutory carry forward periods, experience with operating loss and tax credit carry forwards *not* expiring unused, tax planning strategies and timing of reversals of temporary differences. In assessing the need for a valuation allowance, management carefully weighs both positive and negative evidence currently available. The weight given to the potential effect of positive and negative evidence must be commensurate with the extent to which it can be objectively verified. If management determines, based on available evidence, both positive and negative, that it is more likely than *not* that some portion or all of the deferred tax asset will *not* be realized in future periods, a valuation allowance is calculated and recorded. These determinations are inherently subjective and depend upon management's estimates and judgments used in their evaluation of both positive and negative evidence.

Management performed an evaluation of FNCB's deferred tax assets at *June 30, 2018* taking into consideration all available positive and negative evidence at that time. Based on this evaluation, management believes that FNCB's future taxable income will be sufficient to utilize deferred tax assets. Accordingly, a valuation allowance for deferred tax assets was *not* required at *June 30, 2018* and *December 31, 2017.*

Note *7.* **Related Party Transactions**

In conducting its business, FNCB has engaged in, and intends to continue to engage in, banking and financial transactions with directors, executive officers and their related parties.

FNCB has granted loans, letters of credit and lines of credit to directors, executive officers and their related parties. The following table summarizes the changes in the total amounts of such outstanding loans, advances under lines of credit, net of any participations sold, as well as repayments during the *three* and *six* months ended *June 30, 2018* and *2017:*

(in thousands)	**For the Three Months Ended June 30, 2018**	**2017**	**For the Six Months Ended June 30, 2018**	**2017**
Balance, beginning of period	$*65,884*	$*44,189*	$*55,576*	$*42,007*
Additions, new loans and advances	*11,946*	*10,562*	*43,115*	*36,772*
Repayments	*(8,004*)	*(13,326*)	*(28,865*)	*(37,354*)
Balance, end of period	$*69,826*	$*41,425*	$*69,826*	$*41,425*

At *June 30, 2018,* there were *no* loans made to directors, executive officers and their related parties that were *not* performing in accordance with the terms of the loan agreements.

Deposits from directors, executive officers and their related parties held by the Bank at *June 30, 2018* and *December 31, 2017* amounted to *$83.3* million and *$139.2* million, respectively, a decrease of *$55.9* million. The decrease was due to cyclical outflows from several large commercial deposit relationships that are owned by, or a related party to, certain directors. Interest paid on the deposits amounted to *$157* thousand and *$131* thousand, respectively, for the *six* months ended on *June 30, 2018* and *2017.*

In the course of its operations, FNCB acquires goods and services from, and transacts business with, various companies of related parties, which include, but are *not* limited to, employee health insurance, fidelity bond and errors and omissions insurance, legal services, and repair of repossessed automobiles for resale. FNCB recorded payments to related parties for goods and services of *$0.6* million and *$1.0* million for the *three* and *six* months ended *June 30, 2018,* respectively, and *$0.6* million and *$1.1* million for the respective periods of *2017.*

Subordinated notes (the "Notes") held by directors and/or their related parties totaled *$3.1* million at both *June 30, 2018* and *December 31, 2017.* Regular quarterly interest payments on the Notes paid by FNCB to its directors and/or their related parties totaled *$35* thousand and *$70* thousand for the *three* and *six* months ended *June 30, 2018,* respectively and *$71* thousand and *$140* thousand for the same time periods of *2017.*

Note *8.* Contingencies

On *May 24, 2012,* a putative shareholder filed a complaint in the Court of Common Pleas for Lackawanna County ("Shareholder Derivative Suit") against certain present and former directors and officers of FNCB (the "Individual Defendants") alleging, inter alia, breach of fiduciary duty, abuse of control, corporate waste, and unjust enrichment. FNCB was named as a nominal defendant. On *February 4, 2014,* the Court issued a Final Order and Judgment for the matter granting approval of a Stipulation of Settlement (the "Settlement") and dismissing all claims against FNCB and the Individual Defendants. As part of the Settlement, without admitting any fault, wrongdoing or liability, the Individual Defendants agreed to settle the derivative litigation for *$5.0* million. The *$5.0* million Settlement payment was made to FNCB on *March 28, 2014.* The Individual Defendants reserved their rights to indemnification under FNCB's Articles of Incorporation and Bylaws, resolutions adopted by the Board, the Pennsylvania Business Corporation Law and any and all rights they have against FNCB's and the Bank's insurance carriers. In addition, in conjunction with the Settlement, FNCB accrued *$2.5* million related to fees and costs of the plaintiff's attorneys, which was included in non-interest expense in the consolidated statements of income for the year ended *December 31, 2013.* On *April 1, 2014,* FNCB paid the *$2.5* million related to fees and costs of the plaintiff's attorneys and partial indemnification of the Individual Defendants in the amount of *$2.5* million. Commencing on *July 1, 2017,* FNCB made partial indemnifications to the Individual Defendants through monthly principal payments, made on behalf of the Individual Defendants, of *$25,000* plus accrued interest to First Northern Bank and Trust Co. On *April 11, 2018,* FNCB indemnified the Individual Defendants by paying in full the *$2.5* million, plus accrued interest to First Northern Bank & Trust Co.

On *September 5, 2012,* Fidelity and Deposit Company of Maryland ("F&D") filed an action against FNCB and the Bank, as well as several current and former officers and directors of FNCB, in the United States District Court for the Middle District of Pennsylvania. F&D has asserted a claim for the rescission of a directors' and officers' insurance policy and a bond that it had issued to FNCB. On *November 9, 2012,* FNCB and the Bank answered the claim and asserted counterclaims for the losses and expenses already incurred by FNCB and the Bank. FNCB and the other defendants are defending the claims and have opposed F&D's requested relief by way of counterclaims, breaches of contract and bad faith claims against F&D for its failure to fulfill its obligations to FNCB and the Bank under the insurance policy. Discovery is complete and the parties have exchanged expert reports. Dispositive motions have been submitted by the parties and the Court heard oral arguments on the motions on *August 9, 2017.* FNCB is awaiting the Court's rulings on the dispositive motions. At this time, FNCB cannot reasonably determine the outcome of potential range of loss, if any, in connection with this matter.

FNCB has been subject to tax audits, and is also a party to routine litigation involving various aspects of its business, such as employment practice claims, workers compensation claims, claims to enforce liens, condemnation proceedings on properties in which FNCB holds security interests, claims involving the making and servicing of real property loans and other issues incident to its business, *none* of which has or is expected to have a material adverse impact on the consolidated financial condition, results of operations or liquidity of FNCB.

Except as disclosed in this Note *8* "Contingencies," there have been *no* changes in the status of the other litigation disclosed in FNCB's Annual Report on Form *10*-K for the year ended *December 31, 2017.*

Note *9.* Stock Compensation Plans

FNCB has a Long-Term Incentive Compensation Plan ("LTIP") for directors, executive officers and key employees. The LTIP authorizes up to *1,200,000* shares of common stock for issuance and provides the Board of Directors with the authority to offer several different types of long-term incentives, including stock options, stock appreciation rights, restricted stock, restricted stock units, performance units and performance shares. During the *six* months ended *June 30, 2018* and *2017,* the Board of Directors granted *57,829* and *54,549* shares of restricted stock, respectively, under the LTIP. At *June 30, 2018,* there were *921,069* shares of common stock available for award under the LTIP. For the *six* months ended *June 30, 2018* and *2017,* stock-based compensation expense, which is included in salaries and employee benefits expense in the consolidated statements of income, totaled *$137* thousand and *$167* thousand, respectively. Total unrecognized compensation expense related to unvested restricted stock awards was *$819* thousand and *$608* thousand at *June 30, 2018* and *2017,* respectively.

The following table summarizes the activity related to FNCB's unvested restricted stock awards during the *three* and *six* months ended *June 30, 2018* and *2017:*

	Three Months Ended June 30,				**Six Months Ended June 30,**			
	2018		**2017**		**2018**		**2017**	
(dollars in thousands)	**Restricted Shares**	**Weighted-Average Grant Date Fair Value**	**Restricted Shares**	**Weighted-Average Grant Date Fair Value**	**Restricted Shares**	**Weighted-Average Grant Date Fair Value**	**Restricted Shares**	**Weighted-Average Grant Date Fair Value**
Unvested, beginning of period	*162,679*	$ *7.05*	*142,283*	$ *6.09*	*106,129*	$ *6.23*	*103,874*	$ *5.74*
Awards granted	-	-	-	-	*57,829*	*8.54*	*54,549*	*6.83*
Forfeitures	-	-	-	-	*(1,279*)	*6.88*	*(5,050*)	*5.65*
Vestings	*(46,358*)	*5.93*	*(35,788*)	*5.65*	*(46,358*)	*5.93*	*(46,878*)	*5.90*
Unvested, end of period	*116,321*	$ *7.50*	*106,495*	$ *6.24*	*116,321*	$ *7.50*	*106,495*	$ *6.24*

FNCB had an Employee Stock Incentive Plan (the "Stock Incentive Plan"), where options were granted to key officers and other employees of FNCB. The aggregate number of shares authorized to be issued upon exercise of the options under the Stock Incentive Plan could *not* exceed *1,100,000* shares. Options and rights granted under the Stock Incentive Plan became exercisable *six* months after the date the options were awarded and expire *ten* years after the award date. Upon exercise, the shares are issued from FNCB's authorized but unissued stock. The Stock Incentive Plan expired on *August 30, 2010.* Accordingly, *no* further grants will be made under the Stock Incentive Plan. *No* compensation expense related to options under the Stock Incentive Plan was required to be recorded in the *three* and *six* months ended *June 30, 2018* and *2017.*

There have been *no* changes to the status of FNCB's Stock Incentive Plan as of or for the *six* months ended *June 30, 2018.* For additional information related to the Stock Incentive Plan, refer to Note *13* to the consolidated financial statements included in FNCB's Annual Report on Form *10*-K for the year ended *December 31, 2017.*

Note *10.* Regulatory Matters/Subsequent Event

FNCB's ability to pay dividends to its shareholders is largely dependent on the Bank's ability to pay dividends to FNCB. Bank regulations limit the amount of dividends that *may* be paid without prior approval of the Bank's regulatory agency. For the *three* and *six* months ended *June 30, 2018,* cash dividends declared and paid by FNCB were *$0.04* per share and *$0.08* per share, respectively, and *$0.03* per share and *$0.06* per share for the same periods of *2017.* FNCB offers a Dividend Reinvestment and Stock Purchase Plan ("DRP") to its shareholders. Effective *July 1, 2017,* shares acquired under the DRP were purchased in open market transactions. Previously, FNCB issued shares under the DRP from authorized but unissued common shares. In *January 2018,* FNCB elected to continue purchasing dividend reinvestment shares in open market transactions, but decided to issue shares from authorized but unissued common shares for optional cash purchases. Common shares issued under the DRP for the *three* and *six* months ended *June 30, 2018* totaled *4,139* and *12,776,* respectively, and totaled *29,861* and *65,240* for the respective comparable periods of *2017.* Additionally, on *July 26, 2018,* FNCB declared a cash dividend for the *third* quarter of *2018* of *$0.04* per share, which is payable on *September 17, 2018,* to shareholders of record as of *September 4, 2018.*

FNCB is subject to various regulatory capital requirements administered by the federal banking agencies. 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 adverse effect on FNCB's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, specific capital guidelines that involve quantitative measures of assets, liabilities, and certain off-balance sheet items as calculated under regulatory accounting practices must be met. Capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

Current quantitative measures established by regulation to ensure capital adequacy require FNCB to maintain minimum amounts and ratios (set forth in the tables below) of Total capital, Tier I capital, and Tier I common equity (as defined in the regulations) to risk-weighted assets (as defined), and of Tier I capital (as defined) to average assets (as defined).

The following tables present summary information regarding FNCB's and the Bank's risk-based capital and related ratios at *June 30, 2018* and *December 31, 2017:*

	Consolidated		**Bank Only**		**Minimum Required For Capital Adequacy Purposes**	**Minimum Required For Capital Adequacy Purposes with Conservation Buffer**	**Minimum Required To Be Well Capitalized Under Prompt Corrective Action Regulations***
(in thousands)	**Amount**	**Ratio**	**Amount**	**Ratio**	**Ratio**	**Ratio**	**Ratio**
June 30, 2018							
Total capital (to risk-weighted assets)	$*105,477*	*11.31*%	$*106,594*	*11.46*%	*8.00* %	*9.875* %	*10.00* %
Tier I capital (to risk-weighted assets)	*93,692*	*10.05*%	*96,809*	*10.41*%	*6.00* %	*7.875* %	*8.00* %
Tier I common equity (to risk-weighted assets)	*85,778*	*9.20* %	*96,809*	*10.41*%	*4.50* %	*6.375* %	*6.50* %
Tier I capital (to average assets)	*93,692*	*7.69* %	*96,809*	*7.96* %	*4.00* %	*4.000* %	*5.00* %
Total risk-weighted assets	*932,367*		*930,273*				
Total average assets	*1,217,970*		*1,216,360*				

(in thousands)	Consolidated Amount	Consolidated Ratio	Bank Only Amount	Bank Only Ratio	Minimum Required For Capital Adequacy Purposes Ratio	Minimum Required For Capital Adequacy Purposes with Conservation Buffer Ratio	Minimum Required To Be Well Capitalized Under Prompt Corrective Action Regulations* Ratio
December 31, 2017							
Total capital (to risk-weighted assets)	$*101,135*	*12.08*%	$*104,272*	*12.49*%	*8.00* %	*9.25* %	*10.00* %
Tier I capital (to risk-weighted assets)	*89,220*	*10.66*%	*94,856*	*11.36*%	*6.00* %	*7.25* %	*8.00* %
Tier I common equity (to risk-weighted assets)	*81,493*	*9.74* %	*94,856*	*11.36*%	*4.50* %	*5.75* %	*6.50* %
Tier I capital (to average assets)	*89,220*	*7.74* %	*94,856*	*8.24* %	*4.00* %	*4.00* %	*5.00* %
Total risk-weighted assets	*837,032*		*834,959*				
Total average assets	*1,152,776*		*1,151,539*				

*Applies to the Bank only.

Note *11.* Fair Value Measurements

In determining fair value, FNCB uses various valuation approaches, including market, income and cost approaches. Accounting standards establish a hierarchy for inputs used in measuring fair value that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that observable inputs be used when available. Observable inputs are inputs that market participants would use in pricing the asset or liability, which are developed based on market data obtained from sources independent of FNCB. Unobservable inputs reflect FNCB’s knowledge about the assumptions the market participants would use in pricing an asset or liability, which are developed based on the best information available in the circumstances.

The fair value hierarchy gives the highest priority to unadjusted quoted market prices in active markets for identical assets or liabilities (Level *1* measurement) and the lowest priority to unobservable inputs (Level *3* measurement). A financial asset or liability's level within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement. The fair value hierarchy is broken down into *three* levels based on the reliability of inputs as follows:

Level *1* valuation is based upon unadjusted quoted market prices for identical instruments traded in active markets.

Level *2* valuation is based upon quoted market prices for similar instruments traded in active markets, quoted market prices for identical or similar instruments traded in markets that are *not* active and model-based valuation techniques for which all significant assumptions are observable in the market or can be corroborated by market data; and

Level *3* valuation is derived from other valuation methodologies including discounted cash flow models and similar techniques that use significant assumptions *not* observable in the market. These unobservable assumptions reflect estimates of assumptions that market participants would use in determining fair value.

A description of the valuation methodologies used for assets recorded at fair value is set forth below.

Available-for-Sale Debt Securities

The estimated fair values for FNCB's investments in obligations of U.S. government agencies, obligations of state and political subdivisions, government-sponsored agency CMOs and mortgage-backed securities, corporate debt securities, asset-backed securities and negotiable certificates of deposit are obtained by FNCB from a nationally-recognized pricing service. This pricing service develops estimated fair values by analyzing like securities and applying available market information through processes such as benchmark curves, benchmarking of like securities, sector groupings and matrix pricing (Level *2* inputs), to prepare valuations. Matrix pricing is a mathematical technique widely used in the industry to value debt securities without relying exclusively on quoted prices for the specific securities, but rather by relying on the securities' relationship to other benchmark quoted securities. The fair value measurements consider observable data that *may* include, among other things, dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, live trading levels, trade execution data, market consensus prepayment speeds, credit information and the bond's terms and conditions, and are based on market data obtained from sources independent from FNCB. The Level *2* investments in FNCB's portfolio are priced using those inputs that, based on the analysis prepared by the pricing service, reflect the assumptions that market participants would use to price the assets. Management has determined that the Level *2* designation is appropriate for these securities because, as with most fixed-income securities, those in FNCB's portfolio are *not* exchange-traded, and such non-exchange-traded fixed income securities are typically priced by correlation to observed market data. FNCB has reviewed the pricing service's methodology to confirm its understanding that such methodology results in a valuation based on quoted market prices for similar instruments traded in active markets, quoted markets for identical or similar instruments traded in markets that are *not* active and model-based valuation techniques for which the significant assumptions can be corroborated by market data as appropriate to a Level *2* designation.

For those securities for which the inputs used by an independent pricing service were derived from unobservable market information, FNCB evaluated the appropriateness and quality of each price. Management reviewed the volume and level of activity for all classes of securities and attempted to identify transactions which *may not* be orderly or reflective of a significant level of activity and volume. For securities meeting these criteria, the quoted prices received from either market participants or an independent pricing service *may* be adjusted, as necessary, to estimate fair value (fair values based on Level *3* inputs). If applicable, the adjustment to fair value was derived based on present value cash flow model projections obtained from *third* party providers using assumptions similar to those incorporated by market participants.

At *June 30, 2018,* FNCB owned *three* corporate debt securities with an aggregate amortized cost and fair value of *$4.0* million. The market for these securities at *June 30, 2018* was *not* active and markets for similar securities are also *not* active. FNCB obtained valuations for these securities from a *third*-party service provider that prepared the valuations using a discounted cash flow approach. Management takes measures to validate the service provider's analysis and is actively involved in the valuation process, including reviewing and verifying the assumptions used in the valuation calculations. Results of a discounted cash flow test are significantly affected by variables such as the estimate of the probability of default, estimates of future cash flows, discount rates, prepayment rates and the creditworthiness of the underlying issuers. FNCB considers these inputs to be unobservable Level *3* inputs because they are based on estimates about the assumptions market participants would use in pricing this type of asset and developed based on the best information available in the circumstances rather than on observable inputs. As it relates to fair value measurements, once each issuer is categorized and the forecasted default rates have been applied, the expected cash flows are modeled using the variables described above. Discount rates ranging from *6.37%* to *7.12%* were applied to the expected cash flows to estimate fair value. Management will continue to monitor the market for these securities to assess the market activity and the availability of observable inputs and will continue to apply these controls and procedures to the valuations received from its *third*-party service provider for the period it continues to use an outside valuation service.

Equity Securities

The estimated fair values of equity securities are determined by obtaining quoted prices on nationally recognized exchanges (Level *1* inputs).

Assets Measured at Fair Value on a Recurring Basis

The following tables present the financial assets that are measured at fair value on a recurring basis at *June 30, 2018* and *December 31, 2017,* and the fair value hierarchy of the respective valuation techniques utilized by FNCB to determine the fair value:

	Fair Value Measurements at June 30, 2018			
(in thousands)	**Fair Value**	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Other Unobservable Inputs (Level 3)**
Available-for-sale debt securities:				
Obligations of state and political subdivisions	$*150,455*	$ -	$ *150,455*	$ -
U.S. government/government-sponsored agencies:				
Collateralized mortgage obligations - residential	*33,961*	-	*33,961*	-
Collateralized mortgage obligations - commercial	*73,074*	-	*73,074*	-
Mortgage-backed securities	*24,156*	-	*24,156*	-
Corporate debt securities	*3,957*	-	-	*3,957*
Asset-backed securities	*2,355*	-	*2,355*	-
Negotiable certificates of deposit	*2,905*	-	*2,905*	-
Total available-for-sale debt securities	$*290,863*	$ -	$ *286,906*	$ *3,957*
Equity securities:				
Mutual fund	$*892*	$ *892*	$ -	$ -

Fair Value Measurements at December 31, 2017

(in thousands)	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Other Unobservable Inputs (Level 3)
Available-for-sale debt securities:				
Obligations of state and political subdivisions	$*145,999*	$ -	$ *145,999*	$ -
U.S. government/government-sponsored agencies:				
Collateralized mortgage obligations - residential	*35,657*	-	*35,657*	-
Collateralized mortgage obligations - commercial	*75,418*	-	*75,418*	-
Mortgage-backed securities	*22,311*	-	*22,311*	-
Corporate debt securities	*4,058*	-	-	*4,058*
Asset-backed securities	*3,086*	-	*3,086*	-
Negotiable certificates of deposit	*2,930*	-	*2,930*	-
Total available-for-sale debt securities	$*289,459*	$ -	$ *285,401*	$ *4,058*
Equity securities:				
Mutual fund	$*918*	$ *918*	$ -	$ -

There were *no* transfers between levels within the fair value hierarchy during the *six* months ended *June 30, 2018* and *2017.*

The following table presents a reconciliation and statement of operations classifications of gains and losses for all assets measured at fair value on a recurring basis using significant unobservable inputs (Level *3*), which consisted entirely of corporate debt securities, for the *six* months ended *June 30, 2018* and *2017.*

Fair Value Measurements

Using Significant Unobservable Inputs (Level 3)

	Corporate Debt Securities For the Six Months Ended June 30,	
(in thousands)	**2018**	**2017**
Balance at January 1,	$*4,058*	$*3,339*
Additions	-	*2,000*
Payments Received	-	-
Sales	-	-
Total gains or losses (realized/unrealized):		
Included in earnings	-	-
Included in other comprehensive (loss) income	*(101*)	*83*
Balance at June 30,	$*3,957*	$*5,422*

Assets Measured at Fair Value on a Non-Recurring Basis

The following tables present assets and liabilities measured at fair value on a non-recurring basis at *June 30, 2018* and *December 31, 2017,* and additional quantitative information about the valuation techniques and inputs utilized by FNCB to determine fair value. All such assets were measured using Level *3* inputs.

	June 30, 2018					
	Fair Value Measurement			**Quantitative Information**		
(in thousands)	**Recorded Investment**	**Valuation Allowance**	**Fair Value**	**Valuation Technique**	**Unobservable Inputs**	**Value/ Range**
Impaired loans - collateral dependent	$*750*	$ *600*	$*150*	Appraisal of collateral	Selling cost	*10.0%*
Impaired loans - other	*4,284*	*96*	*4,188*	Discounted cash flows	Discount rate	*3.7%* - *7.5%*
Other real estate owned	*63*	-	*63*	Appraisal of collateral	Selling cost	*10.0%*

	December 31, 2017					
	Fair Value Measurement			Quantitative Information		
(in thousands)	Recorded Investment	Valuation Allowance	Fair Value	Valuation Technique	Unobservable Inputs	Value/ Range
Impaired loans - collateral dependent	$ *1,262*	$ *636*	$ *626*	Appraisal of collateral	Selling cost	*10.0%*
Impaired loans - other	*4,578*	*137*	*4,441*	Discounted cash flows	Discount rate	*3.7%* - *7.5%*
Other real estate owned	*1,023*	-	*1,023*	Appraisal of collateral	Selling cost	*10.0%*

The fair value of collateral-dependent impaired loans is determined through independent appraisals or other reasonable offers, which generally include various Level *3* inputs which are *not* identifiable. Management reduces the appraised value by the estimated costs to sell the property and *may* make adjustments to the appraised values as necessary to consider any declines in real estate values since the time of the appraisal. For impaired loans that are *not* collateral-dependent, fair value is determined using the discounted cash flow method. When the measure of the impaired loan is less than the recorded investment in the loan, the impairment is recorded through a valuation allowance or is charged off. The amount shown is the balance of impaired loans, net of any charge-offs and the related allowance for loan losses.

OREO properties are recorded at fair value less the estimated cost to sell at the date of FNCB's acquisition of the property. Subsequent to acquisition of the property, the balance *may* be written down further. It is FNCB's policy to obtain certified external appraisals of real estate collateral underlying impaired loans and OREO, and estimate fair value using those appraisals. Other valuation sources *may* be used, including broker price opinions, letters of intent and executed sale agreements.

The following table summarizes the estimated fair values of FNCB's financial instruments at *June 30, 2018* and at *December 31, 2017.* FNCB discloses fair value information about financial instruments, whether or *not* recognized in the statements of financial condition, for which it is practicable to estimate that value. The following estimated fair value amounts have been determined using available market information and appropriate valuation methodologies. However, management judgment is required to interpret data and develop fair value estimates. Accordingly, the estimates below are *not* necessarily indicative of the amounts FNCB could realize in a current market exchange. The use of different market assumptions and/or estimation methodologies *may* have a material effect on the estimated fair value amounts.

During the *first* quarter of *2018,* FNCB adopted ASU *2016-01* Financial Instruments – Overall (Subtopic *825-10*): "Recognition and Measurement of Financial Assets and Financial Liabilities", which among other things, requires a public business entity to base their fair value disclosures for financial instruments that are *not* measured at fair value in the financial statements on the exit price notion. In accordance with this guidance, FNCB has presented the exit price disclosure requirements for the below table on a prospective basis at *June 30, 2018.* The disclosure at *December 31, 2017* continues to be presented utilizing the entry price assumption previously utilized.

(in thousands)	**Fair Value Measurement**	**June 30, 2018**		**December 31, 2017**	
		Carrying Value	**Fair Value**	**Carrying Value**	**Fair Value**
Financial assets					
Cash and short term investments	Level 1	$*21,124*	$*21,124*	$*37,746*	$*37,746*
Securities available for sale	See previous table	*290,863*	*290,863*	*289,459*	*289,459*
Equity securities	Level 1	*892*	*892*	*918*	*918*
Restricted stock	Level 2	*7,964*	*7,964*	*2,763*	*2,763*
Loans held for sale	Level 2	*629*	*629*	*1,095*	*1,095*
Loans, net	Level 3	*845,932*	*825,818*	*761,609*	*752,222*
Accrued interest receivable	Level 2	*3,654*	*3,654*	*3,234*	*3,234*
Equity securities without readily determinable fair values	Level 3	*1,658*	*1,658*	*1,658*	*1,658*
Servicing rights	Level 3	*338*	*821*	*265*	*774*
Financial liabilities					
Deposits	Level 2	*955,243*	*953,202*	*1,002,448*	*962,586*
Borrowed funds	Level 2	*174,251*	*189,420*	*60,278*	*60,214*
Accrued interest payable	Level 2	*331*	*331*	*241*	*241*

Note *12.* Earnings per Share

For FNCB, the numerator of both the basic and diluted earnings per share of common stock is net income available to common shareholders. The weighted average number of common shares outstanding used in the denominator for basic earnings per common share is increased to determine the denominator used for diluted earnings per common share by the effect of potentially dilutive common share equivalents utilizing the treasury stock method. Common share equivalents are outstanding stock options to purchase FNCB's common shares and unvested restricted stock.

The following table presents the calculation of both basic and diluted earnings per share of common stock for the *three* and *six* months ended *June 30, 2018* and *2017:*

	Three Months Ended June 30,		**Six Months Ended June 30,**	
(in thousands, except share data)	**2018**	**2017**	**2018**	**2017**
Net income	$*2,412*	$*1,792*	$*4,431*	$*3,989*
Basic weighted-average number of common shares outstanding	*16,792,812*	*16,716,899*	*16,778,188*	*16,687,389*
Plus: Common share equivalents	*26,474*	*20,096*	*23,238*	*16,667*
Diluted weighted-average number of common shares outstanding	*16,819,286*	*16,736,995*	*16,801,426*	*16,704,056*
Income per common share:				
Basic	$*0.14*	$*0.11*	$*0.26*	$*0.24*
Diluted	$*0.14*	$*0.11*	$*0.26*	$*0.24*

For the *three* and *six* months ended *June 30, 2018* and *2017,* common stock equivalents reflected in the table above were related entirely to the incremental shares of unvested restricted stock. Stock options of *19,200* and *31,200* for the *six* months ended *June 30, 2018* and *2017,* respectively, were excluded from common stock equivalents. The exercise prices of stock options exceeded the average market price of FNCB's common shares during the periods presented; therefore, inclusion of these common stock equivalents would be anti-dilutive to the diluted earnings per common share calculation.

Note *13.* Other Comprehensive Income

The following tables summarize the reclassifications out of accumulated other comprehensive income (loss) for the *three* and *six* months ended *June 30, 2018* and *2017,* which are comprised entirely of unrealized gains and losses on available-for-sale debt securities:

	Three Months Ended June 30, 2018		**Six Months Ended June 30, 2018**	
(in thousands)	**Amount Reclassifed from Accumulated Other Comprehensive Income (Loss)**	**Affected Line Item in the Consolidated Statements of Income**	**Amount Reclassifed from Accumulated Other Comprehensive Income (Loss)**	**Affected Line Item in the Consolidated Statements of Income**
Available-for-sale securities:				
Reclassification adjustment for net losses reclassified into net income	$*4*	Net (loss) gain on sale of securities	$*4*	Net (loss) gain on sale of securities
Taxes	*(1)*	Income taxes	*(1)*	Income taxes
Net of tax amount	$*3*		$*3*	

	Three Months Ended June 30, 2017		**Six Months Ended June 30, 2017**	
(in thousands)	**Amount Reclassifed from Accumulated Other Comprehensive Income (Loss)**	**Affected Line Item in the Consolidated Statements of Income**	**Amount Reclassifed from Accumulated Other Comprehensive Income (Loss)**	**Affected Line Item in the Consolidated Statements of Income**
Available-for-sale securities:				
Reclassification adjustment for net gains reclassified into net income	$*(693)*	Net (loss) gain on sale of securities	$*(971)*	Net (loss) gain on sale of securities
Taxes	*235*	Income taxes	*330*	Income taxes
Net of tax amount	$*(458)*		$*(641)*	

The following table summarizes the changes in accumulated other comprehensive (loss) income, net of tax for the *three* and *six* months ended *June 30, 2018* and *2017:*

(in thousands)	**Three Months Ended June 30, 2018**	**2017**	**Six Months Ended June 30, 2018**	**2017**
Balance, beginning of period	$*(5,612)*	$*(532)*	$*(1,745)*	$*(1,560)*
Other comprehensive (loss) income before reclassifications	*(1,453)*	*2,194*	*(5,385)*	*3,405*
Amounts reclassified from accumulated other comprehensive (loss) income	*3*	*(458)*	*3*	*(641)*
Net other comprehensive (loss) income during the period	*(1,450)*	*1,736*	*(5,382)*	*2,764*
Reclassification of net loss on equity securities upon adoption of ASU 2016-01	-	-	*65*	-
Balance, end of period	$*(7,062)*	$*1,204*		