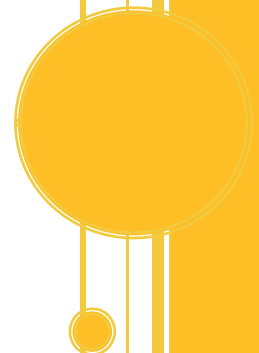


IBW FINANCIAL CORPORATION AND SUBSIDIARY

2020 FINANCIALS

IBW FINANCIAL CORPORATION
4812 GEORGIA AVE NW
WASHINGTON, DC 20011





CliftonLarsonAllen LLP
CLAconnect.com

INDEPENDENT AUDITORS' REPORT

Shareholders and Board of Directors
IBW Financial Corporation and Subsidiary
Washington, DC

Report on Financial Statements

We have audited the accompanying consolidated financial statements of IBW Financial Corporation and Subsidiary, which comprise the consolidated balance sheets as of December 31, 2020 and 2019, and the related consolidated statements of income, comprehensive income, changes in shareholders' equity, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

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

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

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



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Shareholders and Board of Directors
IBW Financial Corporation and Subsidiary
Washington, DC

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of IBW Financial Corporation and Subsidiary as of December 31, 2020 and 2019, and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

CliftonLarsonAllen LLP

CliftonLarsonAllen LLP

Plymouth Meeting, Pennsylvania
August 19, 2021

CONSOLIDATED BALANCE SHEETS

December 31, 2020 and 2019

(dollars in thousands)	2020	2019
ASSETS		
Cash and due from banks	\$ 5,055	\$ 6,933
Interest-bearing deposits with banks	84,659	64,280
Total cash and cash equivalents	89,714	71,213
Short-term Investments	2,559	2,659
Investment securities available-for-sale, at fair value	88,877	86,930
Equity investments	945	910
Restricted stock, at cost	563	475
Loans held for sale	2,431	1,200
Loans receivable, net of unearned income and deferred fees	352,412	343,380
Less: Allowance for loan losses	(5,179)	(3,796)
Net loans	347,233	339,584
Premises and equipment, net	9,166	8,776
Real estate owned (REO)	260	260
Bank owned life insurance (BOLI)	9,754	9,467
Other assets	8,124	9,523
Total assets	\$ 559,626	\$ 530,997
LIABILITIES AND SHAREHOLDERS' EQUITY		
LIABILITIES		
Non-interest bearing deposits	\$ 156,805	\$ 120,123
Interest bearing deposits	345,228	358,886
Total deposits	502,033	479,009
Short-term borrowings	4,626	3,335
Accounts payable, accrued expenses and other liabilities	5,012	8,162
Total liabilities	511,671	490,506
SHAREHOLDERS' EQUITY		
Preferred stock \$1 par value per share; (500,000 voting and 480,000 nonvoting) authorized; \$25 par value, 20,000 Series A nonvoting issued and outstanding, stated liquidation value	500	500
Common stock, \$1 par value; 1,000,000 shares authorized, 597,058 issued and outstanding for 2020 and 597,058 for 2019	597	597
Additional paid-in-capital	3,169	3,169
Retained earnings	40,988	35,488
Accumulated other comprehensive (loss) income	2,701	737
Total shareholders' equity	47,955	40,491
Total liabilities and shareholders' equity	\$ 559,626	\$ 530,997

See Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENTS OF INCOME
Years Ended December 31, 2020 and 2019

(dollars in thousands)	2020	2019
Interest income:		
Interest and fees on loans	\$ 18,310	\$ 18,171
Interest on investment securities	2,173	1,951
Interest on interest-bearing deposits and short-term investments	557	375
Total interest income	21,040	20,497
Interest expense:		
Interest on deposits	1,773	1,997
Interest on short-term borrowings	41	409
Total interest expense	1,814	2,406
Net interest income	19,226	18,091
Provision for loan losses	1,869	500
Net interest income after provision for loan losses	17,357	17,591
Noninterest income (expense):		
Impairment on equity securities without readily determinable fair value	-	(123)
Gain on sale of available for sale investment securities	-	101
Gain on sale of loans	313	210
Loss on sale of REO	-	(345)
Service charges and other fees on deposits	1,920	1,801
Other fee income	241	288
Bargain purchase gain	-	2,415
Gain on sale of Bank owned real estate	7,553	2,449
Other income	6,645	2,137
Total non-interest income	16,672	8,933
Noninterest expense:		
Salaries and benefits	13,787	11,238
Occupancy	2,921	1,814
Furniture and equipment	544	617
Data processing and information technology	3,275	2,302
Office expense	978	826
Professional fees	1,378	1,148
Security	390	527
FDIC insurance assessment	531	258
Lending expense	311	139
Other	2,153	2,027
Total non-interest expense	26,268	20,896
Income before income taxes	7,761	5,628
Income tax expense	2,087	1,592
Net income	5,674	4,036
Preferred stock dividends	(25)	(25)
Net income available to common shareholders	\$ 5,649	\$ 4,011
Basic and diluted net income per common share	\$ 9.46	\$ 6.71
Dividend per common share	\$ 0.25	\$ 0.12
Weighted average number of common shares outstanding	597,058	597,871

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
Years Ended December 31, 2020 and 2019

(dollars in thousands)	2020	2019
Net income	\$ 5,674	\$ 4,036
Other comprehensive income:		
Unrealized gain on available-for-sale investment securities	2,729	1,416
Reclassification adjustment for (gains) realized in income	-	(101)
Income tax expense	(765)	(319)
Total other comprehensive income	1,964	996
Total comprehensive income	<u>\$ 7,638</u>	<u>\$ 5,032</u>

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
Years Ended December 31, 2020 and 2019

(dollars in thousands)	Preferred Stock	Common Stock	Additional Paid-in-Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
Net income	\$ —	\$ —	\$ —	\$ 4,036	\$ —	\$ 4,036
Repurchase & retirement of common stock	—	(1)	(28)	—	—	(29)
Cash dividends paid:						
Preferred stock -						
Series A - \$1.25 per share	—	—	—	(25)	—	(25)
Common stock - \$.12 per share	—	—	—	(72)	—	(72)
Other comprehensive income	—	—	—	—	996	996
Balance December 31, 2019	<u>500</u>	<u>597</u>	<u>3,169</u>	<u>35,488</u>	<u>737</u>	<u>40,491</u>
Net income	—	—	—	5,674	—	5,674
Repurchase & retirement of common stock	—	—	—	—	—	-
Cash dividends paid:						
Preferred stock -						
Series A - \$1.25 per share	—	—	—	(25)	—	(25)
Common stock - \$.25 per share	—	—	—	(149)	—	(149)
Other comprehensive income	—	—	—	—	1,964	1,964
Balance December 31, 2020	<u>\$ 500</u>	<u>\$ 597</u>	<u>\$ 3,169</u>	<u>\$ 40,988</u>	<u>\$ 2,701</u>	<u>\$ 47,955</u>

See Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS
Years Ended December 31, 2020 and 2019

(dollars in thousands)	2020	2019
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	\$ 5,674	\$ 4,036
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	442	979
Amortization of deposit intangible	222	42
Provision for loan losses	1,869	500
Deferred income taxes	(868)	397
Net amortization of investment securities	636	389
Gain on sale of investment securities available-for-sale	-	(101)
Impairment loss on equity security	-	123
Unrealized gain on equity security	(35)	(2)
Increase in value of BOLI	(153)	(122)
Gain on sale of loans	(313)	(210)
Originations of loans held for sale	(12,893)	(10,791)
Proceeds from sales of loans held for sale	11,975	9,801
Loss on sale of REO	-	345
Bargain purchase gain	-	(2,415)
Gain on sale of premises and equipment	(7,553)	(2,449)
Changes in:		
(Increase) decrease in accrued interest receivable	(1,269)	155
Decrease in other assets	2,337	1,942
(Decrease) Increase in other liabilities	(3,150)	1,271
Net cash (used in) provided by operating activities	(3,079)	3,890
CASH FLOWS FROM INVESTING ACTIVITIES:		
(Decrease) Increase in loans receivable, net	(9,518)	20,291
Purchase of short-term investments	-	(249)
Purchases of investment securities available-for-sale	(17,610)	(3,962)
Purchase of restricted stock	(88)	-
Proceeds from maturity of short-term investments	100	1,055
Proceeds received from maturity and sales of available-for-sale investment securities	17,834	12,364
Proceeds received from redemption of restricted stock	-	1,564
Purchases of premises and equipment	(1,258)	(608)
Proceeds from the sale of premises and equipment	7,979	3,175
Proceeds from sale of REO	-	2,269
Cash and cash equivalents acquired in acquisition	-	32,348
Net cash (used in) provided by investing activities	(2,561)	68,247
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net increase in total deposits	23,024	17,934
Net increase (decrease) increase in short-term borrowing	1,291	(42,009)
Cash dividends paid	(174)	(97)
Retirement of common stock	-	(29)
Net cash (used in) provided by financing activities	24,141	(24,201)
Net increase in cash and cash equivalents	18,501	47,936
Cash and cash equivalents at beginning of year	71,213	23,277
Cash and cash equivalents at end of year	\$ 89,714	\$ 71,213

See Notes to Consolidated Financial Statements.

Consolidated Statements of Cash Flows (continued)

(dollars in thousands)	2020	2019
SUPPLEMENTAL DISCLOSURES OF CASH FLOW AND NONCASH INFORMATION:		
Cash paid during the year for:		
Interest on deposits and other borrowings	\$ 1,999	\$ 2,247
Income taxes	3,868	5
Noncash transactions:		
Transfer of loans to REO	\$ -	\$ 300
Initial recognition of operating lease right-to-use assets	-	4,758
Initial recognition of operating lease liabilities	-	4,758
Assets acquired and liabilities assumed in the merger with CNB:		
Investment securities	\$ -	\$ 26,316
Loans	-	52,974
Other assets	-	1,063
Deposits	-	(110,163)
Other liabilities	-	(123)
Bargain purchase gain recognized	-	(2,415)
Cash and cash equivalents received and acquired	<u>\$ -</u>	<u>\$ (32,348)</u>

See Notes to Consolidated Financial Statements.

Notes to Consolidated Statements**Years Ended December 31, 2020 and 2019 (dollars in thousands)**

1. Summary Of Significant Accounting Policies

IBW Financial Corporation (the “Company”) is a one bank holding company for its wholly owned subsidiary, Industrial Bank, (the “Bank”). The Bank wholly owns 96 HST LLC which holds property to be used for Bank facilities. The accounting and reporting policies of IBW Financial Corporation and subsidiary (the “Company”) conform to accounting principles generally accepted in the United States of America and prevailing practices within the banking industry. The following summarizes the significant accounting policies.

Consolidation – The consolidated financial statements include the accounts of the Company and the Bank. All significant inter-company transactions and balances have been eliminated.

Nature of Business – The principal business of the Company is to make loans and other investments and to accept time and demand deposits. The Company’s primary market areas are in the District of Columbia and surrounding areas, although the Company’s business development efforts generate business outside of these areas. The Company offers a broad range of banking products, including a full line of business and personal savings and certificates of deposit, and other banking services. The Company funds a variety of loan types including commercial term loans and residential real estate loans, and lines of credit, consumer loans, and letters of credit. The Company’s customers are primarily individuals and small businesses.

Use of Estimates – The preparation of consolidated financial statements in accordance with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results could differ from those estimates. In addition, there are inherent risks and uncertainties related to the operation of a financial institution, such as credit and interest rate risk. The possibility exists that because of changing economic conditions,

unforeseen changes could occur and have an adverse effect on the Company’s financial position.

Material estimates that are particularly susceptible to significant change in the near-term relate to the determination of the allowance for loan losses. Management believes that the allowance for loan losses is sufficient to address the risks in the current loan portfolio. While management uses available information to recognize losses on loans, future additions to the allowance may be necessary based on changes in economic conditions. In addition, various regulatory agencies, as an integral part of their examination processes, periodically review the Bank’s allowance for loan losses. Such agencies may require the Bank to recognize additions to the allowance based on their judgments about information available to them at the time of their examinations.

Other material estimates that are particularly susceptible to significant change in the near-term relate to the determination of the valuation of foreclosed real estate, deferred income taxes and other than temporary impairment of investment securities.

In March 2020, the World Health Organization declared the spread of Coronavirus Disease (COVID-19) a worldwide pandemic. The COVID-19 pandemic may impact various parts of the Bank’s future operations and financial results, including additional loan loss reserves. Management believes the Bank is taking appropriate actions to mitigate the negative impact. However, the full impact of COVID-19 on future allowance for loan losses is difficult to reasonably estimate as these events are still developing.

Investment Securities – The Company may segregate its investments securities into the following three categories: trading, held-to-maturity, and available-for-sale. Trading securities are purchased and held principally for the purpose of reselling them within a short period of time. Their unrealized gains and losses are included in earnings.

Securities classified as held-to-maturity are accounted for at amortized cost and require the Company to have both positive intent and ability to hold these securities to maturity. Debt securities not classified as either trading or held-to-maturity are considered to be available-for-sale. Unrealized gains and losses on available-for-sale debt securities are excluded from earnings and reported, net of deferred taxes, as accumulated other comprehensive income, a separate component of shareholders' equity. Premiums are amortized and discounts accreted using the level yield method. For callable debt securities purchased at a premium, the amortization period is shortened to the earliest call date.

Purchases and sales of securities are recorded on a trade date basis. Realized gains or losses on the sale of investment securities are reported in earnings and determined using the adjusted cost of the specific security sold. Investment in Federal Reserve Bank and Federal Home Loan Bank stock are considered restricted as to marketability. Because no ready market exists for these stocks, the Bank's investment is carried at cost. Declines in the fair value of individual securities below their cost that are other than temporary result in write-downs of the individual securities to their fair value. Factors affecting the determination of whether other-than-temporary impairment has occurred include a downgrading of the security by a rating agency, a significant deterioration in the financial condition of the issuer or that management would not have the intent and ability to hold a security for a period of time sufficient to allow for any anticipated recovery in fair value.

Equity Investments — The Company's mutual fund acquired in the merger with CNB on November 1, 2019, is considered an equity investment with a readily determinable fair value and changes to fair value are recorded in other noninterest income. The Company's investments in correspondent bank stock (FHLB) other bank holding company stocks are equity investments without readily determinable fair values. Equity investments without readily determinable fair values are measured at cost, less impairment, and are adjusted for observable price changes which is recorded in noninterest income. During 2020 and 2019 the Company recorded

impairment charges of \$-0- and \$123, respectively, to impair the Company's investment in other bank holding company stocks.

Loans — Loans are reported at the principal amount outstanding net of deferred fees and costs and the allowance for loan losses. Interest on loans is accrued at the contractual rate based upon the principal amount outstanding. Loans fees and related direct loan origination costs are deferred and recognized as a part of interest income over the life of the loan as an adjustment to the loan yield. Loans are placed on non-accrual status when management deems the collectibility of interest is doubtful. Interest ultimately collected is recorded in the period received as a reduction of the principal loan balance. Accruals are resumed on loans only when they are brought fully current with respect to interest and principal and when, in the judgment of management, the loan is estimated to be fully collectible as to both principal and interest.

Loans are considered impaired when, based on current information, it is probable that the Company will not collect all principal and interest payments according to contractual terms. Generally, loans are considered impaired once principal and interest payments are past due more than 90 days and they are placed on non-accrual. Management also considers the financial condition of the borrower, cash flows of the loan and the value of the related collateral. Impaired loans do not include large groups of smaller balance homogenous credits such as residential real estate, consumer installment loans, and commercial leases, which are evaluated collectively for impairment. Loans specifically reviewed for impairment are not considered impaired during periods of "minimal delay" in payment (usually ninety days or less) provided eventual collection of all amounts due is expected. The impairment of a loan is measured based upon the present value of future cash flows discounted at the loan's effective interest rate, except that as a practical alternative, the Company may measure impairment based on a loan's observable market price or the fair value of the collateral, if the loan is collateral dependent. The Company recognizes interest income on impaired loans on a cash basis if the borrower demonstrates the ability to meet the contractual obligation and collateral is sufficient. If

there is doubt regarding the borrower's ability to make payments or the collateral is not sufficient, payments received are accounted for as reduction in principal.

Purchased Credit Impaired Loans - As a part of a previous acquisition, we acquired certain loans for which there was, at acquisition, evidence of deterioration of credit quality since origination. These purchased credit impaired loans were recorded at the acquisition date fair value, such that there is no carryover of the seller's allowance for loan losses. After acquisition, losses are recognized by an increase in the allowance for loan losses. Such purchased credit impaired loans are accounted for individually. We estimate the amount and timing of expected cash flows for each loan, and the expected cash flows in excess of the amount paid are recorded as interest income over the remaining life of the loan (accretable yield). The excess of the loan's contractual principal and interest over expected cash flows is not recorded (non-accretable difference). Over the life of the loan, expected cash flows continue to be estimated. If the present value of the expected cash flows is less than the carrying amount, a loss is recorded. If the present value of the expected cash flows is greater than the carrying amount, it is recognized as part of future interest income.

Trouble Debt Restructuring (TDR) - Under certain circumstances, the Company will provide borrowers relief through loan restructurings. A restructuring of debt constitutes a TDR if the Company for economic or legal reasons related to the borrower's financial difficulties grants a concession to the borrower that it would not otherwise consider. Restructured loans typically present an elevated level of credit risk as the borrowers are not able to perform according to the original contractual terms. Loans that are reported as TDRs are considered impaired and measured for impairment as described above in the calendar year of the restructuring. In subsequent years, a restructured loan may cease being classified as impaired if the loan was modified at a market rate and is performing according to the modified terms. TDR concessions can include reduction of interest rates, extension of maturity dates, forgiveness of principal or interest due, or acceptance of other assets in full or partial satisfaction of the debt.

Restructured loans can involve loans remaining on nonaccrual, moving to nonaccrual, or continuing on accrual status, depending on the individual facts and circumstances of the borrower. Nonaccrual restructured loans are included and treated with other nonaccrual loans.

Loans Held for Sale – Loans originated for sale are carried at the lower of aggregate cost or market. Market value is based on commitments from investors. Gains and losses on sales are determined using the specific identification method.

Allowance for Loan Losses – The allowance for loan losses is maintained at a level management believes to be adequate to absorb probable losses inherent in the loan portfolio. The calculation is based on the size and current risk characteristics of the loan portfolio, an assessment of individual problem loans and actual loss experience, current economic events in specific industries or geographical areas, these events would include unemployment levels, and other pertinent factors, including regulatory guidance and general economic conditions. Determination of the allowance is inherently subjective as it requires significant estimates, including the amounts and timing of expected future cash flows on impaired loans, estimated losses on pools of homogenous loans based on historical loss experience, and consideration of current economic trends, all of which may be susceptible to significant change. Loan losses are charged off against the allowance, while recoveries of amounts previously charged off are credited to the allowance. A provision for loan losses is charged to operations based on management's periodic evaluation of the factors previously mentioned, as well as other pertinent factors. Evaluations are conducted at least quarterly or more often if deemed necessary.

The allowance for loan losses consists of a specific component and a nonspecific component. The components of the allowance for loan losses represent an estimation done pursuant to Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") Topic 450 *Contingencies* and ASC Topic 310 *Receivables*. The specific component of the allowance for loan losses reflects expected losses resulting from analysis developed through credit allocations for individual

loans and historical loss experience for each loan category. The specific credit allocations are based on a regular analysis of all loans over a fixed-dollar amount where the internal credit rating is at or below a predetermined classification. The historical loan loss rate is determined by using a rolling average annual loss over the most recent eight quarters. The loss analysis is performed quarterly and loss factors are updated regularly based on actual experience. The specific component of the allowance for loan losses also includes management's determination of the amounts necessary for concentrations and changes in portfolio mix and volume.

The nonspecific portion of the allowance reflects management's estimate of probable inherent but undetected losses within the portfolio due to uncertainties in economic conditions, delays in obtaining information, including unfavorable information about a borrower's financial condition, the difficulty in identifying triggering events that correlate perfectly to subsequent loss rates, and risk factors that have not yet manifested themselves in loss allocation factors. In addition, the nonspecific allowance includes a component that explicitly accounts for the inherent imprecision in loan loss migration models. Historical loss experience data used to establish estimates may not precisely correspond to the current portfolio. The uncertainty surrounding the strength and timing of economic cycles, including management's concerns over the effects of the prolonged economic downturn and also losses used in the migration analysis may not be representative of actual losses inherent in the portfolio that have not yet been realized.

On March 27, 2020, the President of the United States signed into law the Coronavirus Aid, Relief, and Economic Security (CARES) Act. The CARES Act sought to provide relief when structuring loan modifications with borrowers impacted by COVID-19. In order to qualify, the modification must be related to COVID-19, the loan must have been current at December 31, 2019, and the modification must have been granted prior to December 31, 2020. Under the CARES Act, these loan modifications are not considered to be TDRs.

In response to the COVID-19 pandemic and related economic disruption to nonessential businesses and resulting increased unemployment, the Bank provided additional reserves in its allowance for loan losses to account for the credit quality implications of these economic factors. The qualitative factors were added based on the risk of the various loan types in the portfolio. As the full impact of the pandemic and related economic disruption are still developing, the actual COVID-19 related losses may be higher or lower than the reserves added.

Bank Premises and Equipment – Properties and equipment are stated at cost less accumulated depreciation and amortization. Depreciation and amortization are calculated using the straight-line method over the estimated useful lives of the assets. Useful lives range from three to 10 years for furniture, fixtures, and equipment; three to five years for software, hardware, and data handling equipment; and 10 to 40 years for buildings and building improvements. Land is carried at cost and is not depreciated. Land improvements are amortized over a period of 15 years; and leasehold improvements amortized over the shorter of their estimated useful lives, or the stated duration of the lease plus the optional renewal period, if applicable. Maintenance and repairs are charged to expense as incurred, while improvements which extend the useful life are capitalized and depreciated over the estimated remaining life of the asset.

Leases - The Company adopted ASU 2016-02 effective January 1, 2019. The Company is obligated under non-cancelable operating leases for premises for certain branches, other office locations and office equipment. These leases have original terms ranging from 2 years to over 10 years and at December 31, 2020 have remaining terms of up to 8 years. Certain leases contain renewal options and escalation clauses which can increase rental expenses based principally on the consumer price index and fair market rental value provisions. Right-Of-Use Lease Assets are carried on the balance sheet, in other assets, at amortized cost and corresponding lease liabilities are carried on the balance sheet, in other liabilities, at present value of the future minimum lease payments, adjusted for any initial direct costs and incentives. All of the Company's current outstanding leases are classified as operating leases.

Valuation of long-lived assets - The Company accounts for the valuation of long-lived assets under ASC Topic 360 *Property, Plant and Equipment*. This guidance requires that long-lived assets and certain identifiable intangible assets be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of the long-lived asset is measured by a comparison of the carrying amount of the asset to future undiscounted net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the estimated fair value of the assets. Assets to be disposed of are reportable at the lower of the carrying amount or fair value, less costs to sell.

Advertising Costs – Advertising costs are generally expensed as incurred. Advertising expenses totaled \$52 and \$106 for the years ended December 31, 2020 and 2019, respectively.

Real Estate Owned– Real estate owned (REO) represents properties acquired through foreclosures or other proceedings in satisfaction of indebtedness. At the date of acquisition such property is recorded at the fair value less estimated costs to sell. A write-down to fair value, less estimated costs to sell, at the date of acquisition is charged to the allowance for loan losses. Subsequent declines in fair value, operating expenses, and gains or losses on the disposition of real estate are reported in noninterest income. The amounts the Company will ultimately realize on disposition of these properties could differ from management’s current estimates.

Transfer of Financial Assets – Transfer of financial assets are accounted for as sales, when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when (1) the assets have been isolated from the Company, (2) the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets, and (3) the Company does not maintain effective control over the transferred assets through

an agreement to repurchase them before their maturity.

Fair Value Measurements – The Company follows the guidance of ASC Topic 825, *Financial Instruments* and ASC Topic 820, *Fair Value Measurements*. ASC Topic 825 permits entities to measure many financial instruments and certain other items at fair value. The objective is to improve financial reporting by providing entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. ASC Topic 820 clarifies that fair value is an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. Under ASC Topic 820, fair value measurements are not adjusted for transaction costs. ASC topic 820 establishes a fair value hierarchy that prioritizes unadjusted quoted prices in active markets for identical financial assets or liabilities (Level 1 measurements) and gives the lowest priority to unobservable inputs (Level 3 measurements).

Earnings Per Share (“EPS”) – Net income (loss) available to common shareholders is adjusted to give effect to dividends on preferred stock. Net income available to common shareholders for basic and diluted EPS purposes is \$5,649 and \$4,011 for the years ended December 31, 2020 and 2019, respectively. EPS is computed based on the weighted average number of common shares outstanding during the year (597,058 for 2020 and 597,871 for 2019). Basic and diluted EPS are the same, as the Company had no dilutive common stock equivalents outstanding as of December 31, 2020 or 2019 and for the years then ended.

Income Taxes – The Company and its wholly owned subsidiary file a consolidated federal income tax return. Deferred income tax assets and liabilities are computed annually for differences between financial statement and tax basis of assets and liabilities that will result in taxable or deductible amounts in the future based on the enacted tax laws and rates applicable to periods in which the differences are expected to affect taxable income.

Valuation allowances are established, when necessary, to reduce deferred tax assets to the amount expected to be realized. Income tax expense is based upon the results of operations, adjusted for permanent differences between items of income or expense reported in the financial statements and those reported for tax purposes. The Company does not have any uncertain tax positions and did not recognize any adjustments for unrecognized tax benefits. With limited exception, the Company is no longer subject to federal income tax examination by taxing authorities for years before 2017.

Cash and Cash Equivalents – For purposes of the consolidated statements of cash flows, cash equivalents include due from banks, federal funds sold, and interest-bearing deposits with banks with original maturities of three months or less. Included in cash and due from banks were required deposits at the Federal Reserve Bank of approximately \$4,087 for 2020 and \$3,545 for 2019.

Short-term Investments – Short-term investments consist of interest-bearing deposits due from banks with original maturities of more than three months.

Bank owned life insurance - The Bank purchased single-premium life insurance on certain employees of the Bank. Appreciation in value of the insurance policies is classified as noninterest income.

Comprehensive income - Accounting principles generally require that recognized revenue, expenses, gains, and losses be included in net income. Certain changes in assets and liabilities, such as unrealized gains and losses on available-for-sale securities, are reported as a separate component of the equity section of the balance sheet. Such items, along with net income, are components of comprehensive income.

Compensating Balances - Compensating balance arrangements exist with various correspondent banks. These noninterest-bearing deposits are maintained in lieu of cash payments for standard bank services. The required balances amounted to \$250 at December 31, 2020 and 2019.

Business Combination - The Company accounts for business combinations under the acquisition method of accounting in accordance with Accounting Standards Codification (“ASC”) 805, *Business Combinations*. The Company recognizes the full fair value of the assets acquired and liabilities assumed and immediately expenses transaction costs. There is no separate recognition of the acquired allowance for loan losses on the acquirer’s balance sheet as credit-related factors are incorporated directly into the fair value of the net tangible and intangible assets acquired. If the amount of consideration exceeds the fair value of assets purchased less the fair value of liabilities assumed, goodwill is recorded. Alternatively, if the amount by which the fair value of assets purchased exceeds the fair value of liabilities assumed and consideration paid, a gain (“bargain purchase gain”) is recorded. Fair values are subject to refinement for up to one year after the closing date of an acquisition as information relative to closing date fair values becomes available. Results of operations of the acquired business are included in the statement of income from the effective date of the acquisition.

All identifiable intangible assets that are acquired in a business combination are recognized at fair value on the acquisition date. Identifiable intangible assets are recognized separately if they arise from contractual or other legal rights or if they are separable (i.e., capable of being sold, transferred, licensed, rented, or exchanged separately from the entity).

Intangible Assets - Intangible assets consist of core deposit intangibles acquired in connection with business acquisitions. The core deposit intangibles are initially recognized based on a valuation performed as of the consummation date. The core deposit intangibles are amortized over the average remaining life of the acquired customer deposits, or approximately 5 years, and evaluated for impairment annually.

Noninterest Income -

Specific guidelines are established for recognition of certain noninterest income components related to the Company's consolidated financial statements. In accordance with Topic 606, revenues are recognized when control of promised goods or services is transferred to customers in an amount that reflects the consideration the Company expects to be entitled to in exchange for those goods or services. To determine revenue recognition for arrangements that an entity determines are within the scope of Topic 606, the Company performs the following five steps: (1) identify the contract(s) with a customer; (2) identify the performance obligations in the contract; (3) determine the transaction price; (4) allocate the transaction price to the performance obligations in the contract; and (5) recognize revenue when (or as) the Company satisfies a performance obligation.

The Company only applies the five-step model to contracts when it is probable that the entity will collect the consideration it is entitled to in exchange for the goods or services it transfers to the customer. At contract inception, once the contract is determined to be within the scope of Topic 606, the Company assesses the goods or services that are promised within each contract and identifies those that contain performance obligations and assesses whether each promised good or service is distinct. The Company then recognizes as revenue the amount of the transaction price that is allocated to the respective performance obligation when (or as) the performance obligation is satisfied. The material groups of noninterest income that this methodology is applied to are defined as follows:

Service charges on deposit accounts: Service charges on deposit accounts primarily consist of account analysis fees, monthly maintenance fees, overdraft fees, and other deposit account related fees. Overdraft fees and certain service charges are fixed and the performance obligation is typically satisfied at the time of the related transaction. The consideration for analysis fees and monthly maintenance fees are variable as the fee can be reduced if the customer meets certain qualifying metrics. The Company's performance obligations are satisfied at the time of the transaction or over the course of a month.

Other noninterest income: Other noninterest income components include debit card interchange fees, and miscellaneous transactional fees. Income earned from these revenue streams is generally recognized concurrently with the satisfaction of the performance obligation.

Certain prior year amounts have been reclassified to conform to the current year's method of presentation. None of these reclassifications were significant.

New Accounting Pronouncements –

In June 2016, the FASB issued ASU No. 2016-13, Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments, (ASU 2016-13), which addresses concerns regarding the perceived delay in recognition of credit losses under the existing incurred loss model. The amendment introduces a new, single model for recognizing credit losses on all financial instruments presented on cost basis. Under the new model, entities must estimate current expected credit losses by considering all available relevant information, including historical and current information, as well as reasonable and supportable forecasts of future events. The update also requires additional qualitative and quantitative information to allow users to better understand the credit risk within the portfolio and the methodologies for determining allowance. ASU 2016-13 is effective for public business entities that are not U.S. Securities and Exchange Commission (SEC) filers for annual periods beginning after December 15, 2022, and interim periods within those annual periods and must be applied using the modified retrospective approach with limited exceptions. Early adoption is permitted. The Company and Bank is currently in the process of evaluating the impact of the amended guidance on its consolidated financial statements. It is reasonable to predict that the ALLL will increase upon adoption given that the allowance will be required to cover the full remaining expected life of the portfolio upon adoption, rather than the incurred loss model under current U.S. GAAP.

In January 2017, the FASB issued ASU No. 2017-04, "Intangibles—Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment." The amendments in this ASU simplify how an entity is required to test goodwill for impairment by eliminating Step 2 from the goodwill impairment test. Step 2 measures a goodwill impairment loss by comparing the implied fair value of a reporting unit's goodwill with the carrying amount of that goodwill. Instead, under the amendments in this ASU, an entity should perform its annual, or interim, goodwill impairment test by comparing the fair value of a reporting unit with its carrying amount. An entity still has the option to perform the qualitative assessment for a reporting unit to determine if the quantitative impairment test is necessary. Public business entities that are SEC filers should adopt the amendments in this ASU for annual or interim goodwill impairment tests in fiscal years

beginning after December 15, 2022. The Company does not expect the adoption of ASU 2017-04 to have a material impact on its consolidated financial statements.

In November 2019, the FASB issued ASU 2019-11, "Codification Improvements to Topic 326, Financial Instruments—Credit Losses." This ASU addresses issues raised by stakeholders during the implementation of ASU No. 2016-13, "Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments." Among other narrow-scope improvements, the new ASU clarifies guidance around how to report expected recoveries. "Expected recoveries" describes a situation in which an organization recognizes a full or partial write-off of the amortized cost basis of a financial asset, but then later determines that the amount written off, or a portion of that amount, will in fact be recovered. While applying the credit losses standard, stakeholders questioned whether expected recoveries were permitted on assets that had already shown credit deterioration at the time of purchase (also known as PCD assets). In response to this question, the ASU permits organizations to record expected recoveries on PCD assets. In addition to other narrow technical improvements, the ASU also reinforces existing guidance that prohibits organizations from recording negative allowances for available-for-sale debt securities. The ASU includes effective dates and transition requirements that vary depending on whether or not an entity has already adopted ASU 2016-13. The Company is currently assessing the impact that ASU 2019-11 will have on its consolidated financial statements.

In December 2019, the FASB issued ASU 2019-12, "Income Taxes (Topic 740)—Simplifying the Accounting for Income Taxes." The ASU is expected to reduce cost and complexity related to the accounting for income taxes by removing specific exceptions to general principles in Topic 740 (eliminating the need for an organization to analyze whether certain exceptions apply in a given period) and improving financial statement preparers' application of certain income tax-related guidance. This ASU is part of the FASB's simplification initiative to make narrow-scope simplifications and improvements to accounting standards through a series of short-term projects. The amendments are effective for fiscal years beginning after December 15, 2020, and interim periods within those fiscal years. Early adoption is permitted. The

Company does not expect the adoption of ASU 2019-12 to have a material impact on its consolidated financial statements.

In January 2020, the FASB issued ASU 2020-01, "Investments—Equity Securities (Topic 321), Investments—Equity Method and Joint Ventures (Topic 323), and Derivatives and Hedging (Topic 815)—Clarifying the Interactions between Topic 321, Topic 323, and Topic 815." The ASU is based on a consensus of the Emerging Issues Task Force and is expected to increase comparability in accounting for these transactions. ASU 2016-01 made targeted improvements to accounting for financial instruments, including providing an entity the ability to measure certain equity securities without a readily determinable fair value at cost, less any impairment, plus or minus changes resulting from observable price changes in orderly transactions for the identical or a similar investment of the same issuer. Among other topics, the amendments clarify that an entity should consider observable transactions that require it to either apply or discontinue the equity method of accounting. For public business entities, the amendments in the ASU are effective for fiscal years beginning after December 15, 2020, and interim periods within those fiscal years. Early adoption is permitted. The Company does not expect the adoption of ASU 2020-01 to have a material impact on its consolidated financial statements.

In March 2020, the FASB issued ASU No. 2020-04 "Reference Rate Reform (Topic 848): Facilitation of the Effects of Reference Rate Reform on Financial Reporting." These amendments provide temporary optional guidance to ease the potential burden in accounting for reference rate reform. The ASU provides optional expedients and exceptions for applying generally accepted accounting principles to contract modifications and hedging relationships, subject to meeting certain criteria, that reference the London Interbank Offered Rate ("LIBOR") or another reference rate expected to be discontinued. It is intended to help shareholders during the global market-wide reference rate transition period. The guidance is effective for all entities as of March 12, 2020 through December 31, 2022. Subsequently, in January 2021, the FASB issued ASU 2021-01 "Reference Rate Reform (Topic 848): Scope." This ASU

clarifies that certain optional expedients and exceptions in Topic 848 for contract modifications and hedge accounting apply to derivatives that are affected by the discounting transition. The ASU also amends the expedients and exceptions in Topic 848 to capture the incremental consequences of the scope clarification and to tailor the existing guidance to derivative instruments affected by the discounting transition. An entity may elect to apply ASU 2021-01 on contract modifications that change the interest rate used for margining, discounting, or contract price alignment retrospectively as of any date from the beginning of the interim period that includes March 12, 2020, or prospectively to new modifications from any date within the interim period that includes or is subsequent to January 7, 2021, up to the date that financial statements are available to be issued. An entity may elect to apply ASU 2021-01 to eligible hedging relationships existing as of the beginning of the interim period that includes March 12, 2020, and to new eligible hedging relationships entered into after the beginning of the interim period that includes March 12, 2020. The Company does expect the change from LIBOR to have a material impact on the Company. However, continues to assess ASU 2020-04 and its impact on the Company's transition away from LIBOR for its loan and other financial instruments.

In October 2020, the FASB issued ASU 2020-08, "Codification Improvements to Subtopic 310-20, Receivables – Nonrefundable fees and Other Costs." This ASU clarifies that an entity should reevaluate whether a callable debt security is within the scope of ASC paragraph 310-20-35-33 for each reporting period. For public business entities, the ASU is effective for fiscal years beginning after December 15, 2021, and interim periods within those fiscal years. Early adoption is not permitted. All entities should apply ASU No. 2020-08 on a prospective basis as of the beginning of the period of adoption for existing or newly purchased callable debt securities. The Company does not expect the adoption of ASU 2020-08 to have a material impact on its consolidated financial statements.

2. Business Combination

On November 1, 2019, City National Bank of New Jersey (CNB) was closed by the Office of the Comptroller of the Currency, which appointed the Federal Deposit Insurance Corporation (the "FDIC") as Receiver. Industrial Bank (the Bank) simultaneously entered into a Purchase and Assumption Agreement ("P&A Agreement") with the FDIC to acquire certain assets and assume certain liabilities of CNB. Pursuant to the Agreement, the Bank received a cash payment from the FDIC in the amount of \$7,136. There was no loss-sharing arrangement with the FDIC with respect to the transaction.

The FDIC-assisted acquisition of CNB was accounted for using the acquisition method of accounting and, accordingly, assets acquired, liabilities assumed, and consideration paid were recorded at their estimated fair values as of the merger date. The following table summarizes the fair value recorded as of November 1, 2019:

<u>(dollars in thousands)</u>	<u>Amount Recorded</u>	<u>Fair Value Adjustments</u>	<u>Fair Value Recorded</u>
Consideration Received:			
Fair value of total consideration received	\$ 7,136	\$ -	\$ 7,136
Identifiable Assets Acquired:			
Cash and cash equivalents	23,644	-	23,644
Interest-bearing time deposits	1,568	-	1,568
Investment securities available-for-sale	26,316		26,316
Net loans receivable	58,027	(5,053)	52,974
Core deposits and other intangibles	-	610	610
Other real estate owned	167	-	167
Other assets	547	(261)	286
Total identifiable assets acquired:	<u>110,269</u>	<u>(4,704)</u>	<u>105,565</u>
Liabilities Assumed:			
Deposits	110,082	81	110,163
Other liabilities	<u>123</u>	<u>-</u>	<u>123</u>
Total liabilities assumed	<u>110,205</u>	<u>81</u>	<u>110,286</u>
Total identified net assets acquired (liabilities assumed)	<u>64</u>	<u>(4,785)</u>	<u>(4,721)</u>
Gain on acquisition	<u>\$ 7,200</u>	<u>\$ (4,785)</u>	<u>\$ 2,415</u>

As permitted by ASC No. 805-10-25, Business Combinations, the above estimates may be adjusted up to one year after closing date of the acquisition to reflect any new information obtained about facts and circumstances existing at the acquisition date. Any changes in the estimated fair values will be recognized in the period the adjustment is identified. There were no adjustments made in 2020 subsequent to the acquisition on November 1, 2019.

3. Investment Securities

At December 31, 2020 and 2019, the amortized cost and fair value of investment securities available-for-sale, with gross unrealized gains and losses, are summarized as follows:

(dollars in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
December 31, 2020:				
U.S. Government Agencies	\$ 8,851	\$ 428	\$ (11)	\$ 9,268
Mortgage-Backed Securities:				
Pass-through securities:				
Issued by FNMA, GNMA and FHLMC	12,977	505	-	13,482
Collateralized Mortgage Obligations:				
Collateralized by FNMA, FHLMC and GNMA mortgage-backed securities	41,842	1,783	(6)	43,619
Private label mortgage-backed securities	1,402	-	(3)	1,399
Municipal securities	20,053	1,074	(18)	21,109
Total available-for-sale	\$ 85,125	\$ 3,790	\$ (38)	\$ 88,877
December 31, 2019:				
U.S. Government Agencies	\$ 9,329	\$ 367	\$ (22)	\$ 9,674
Mortgage-Backed Securities:				
Pass-through securities:				
Issued by FNMA, GNMA and FHLMC	18,193	154	(55)	18,292
Collateralized Mortgage Obligations:				
Collateralized by FNMA, FHLMC and GNMA mortgage-backed securities	49,795	599	(157)	50,237
Private label mortgage-backed securities	2,000	5	-	2,005
Municipal securities	6,590	180	(48)	6,722
Total available-for-sale	\$ 85,907	\$ 1,305	\$ (282)	\$ 86,930

3. Investment Securities (continued)

Gross unrealized losses and fair value by length of time that the individual available-for-sale investment securities have been in a continuous unrealized loss position that are not deemed to be other-than-temporarily impaired at December 31, 2020 and 2019 are as follows:

(dollars in thousands)	Number of Securities	Fair Value	Less than 12 Months	12 months or More	Total Unrealized Losses
December 31, 2020:					
U.S. Government Agencies	3	\$ 1,252	\$ -	\$ 11	\$ 11
Mortgage-Backed Securities	3	1,324	6	-	6
Private label mortgage-backed securities	1	1,399	3	-	3
Municipal securities	3	3,154	18	-	18
	<u>10</u>	<u>\$ 7,129</u>	<u>\$ 27</u>	<u>\$ 11</u>	<u>\$ 38</u>
December 31, 2019:					
U.S. Government Agencies	4	\$ 1,793	\$ -	\$ 22	\$ 22
Mortgage-Backed Securities	32	36,002	154	58	212
Private label mortgage-backed securities	-	-	-	-	-
Municipal securities	4	2,510	48	-	48
	<u>40</u>	<u>\$ 40,305</u>	<u>\$ 202</u>	<u>\$ 80</u>	<u>\$ 282</u>

At December 31, 2020, the entire available-for-sale investment portfolio had a fair value of approximately \$88.9 million of which \$7.1 million of the securities had some unrealized losses from their purchase price. The securities representing the unrealized losses in the available-for-sale portfolio all have modest duration risk, high credit ratings, and represented 8% of the portfolio carrying value. The unrealized losses that exist are the result of market changes in interest rates since the original purchase and not credit deterioration.

Management systematically evaluates investment securities for other-than-temporary declines in fair value on a quarterly basis. This analysis requires management to consider various factors, which include (1) duration and magnitude of the decline in value, (2) the financial condition of the issuer and (3) structure of the security. An impairment loss is recognized in earnings only when (1) the Company intends to sell the debt security; (2) it is more likely than not that the Company will be required to sell the security before recovery of its amortized cost basis or (3) the Company does not expect to recover the entire amortized cost basis of the security. In situations where the Company intends to sell or when it is more likely than not that the Company will be required to sell the security, the entire impairment loss must be recognized in earnings. In all other situations, only the portion of the impairment loss representing the credit loss must be recognized in earnings, with the remaining loss recognized in shareholder's equity as a component of other comprehensive income, net of deferred taxes. Losses in the available-for-sale portfolio are temporary.

3. Investment Securities (continued)

The following is a summary of the amortized cost and approximate fair value of debt and equity securities available-for-sale by contractual maturity as of December 31, 2020 and 2019. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	2020		2019	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
(dollars in thousands)				
U.S. Government Agency maturing				
Due 1 year or less	\$ 4,998	\$ 5,071	\$ -	\$ -
Due after 1 year through 5 years	2,722	3,076	7,799	8,164
Due after 5 years through 10 years	-	-	-	-
Due after 10 years	1,131	1,121	1,530	1,510
Mortgage-backed securities maturing				
Due 1 year or less	-	-	-	-
Due after 1 year through 5 years	7,689	7,995	8,648	8,731
Due after 5 years through 10 years	22,439	23,449	26,210	26,379
Due after 10 years	24,691	25,657	33,130	33,419
Private label mortgage-backed security maturing				
Due after 10 years	1,402	1,399	2,000	2,005
Municipal securities maturing				
Due 1 year or less	-	-	-	-
Due after 1 year through 5 years	1,010	1,179	-	-
Due after 5 years through 10 years	1,982	2,034	1,513	1,639
Due after 10 years	17,061	17,896	5,077	5,083
Total	<u>\$ 85,125</u>	<u>\$ 88,877</u>	<u>\$ 85,907</u>	<u>\$ 86,930</u>

Proceeds from the sale of securities available-for-sale were \$-0- and \$2.2 million for the years ended December 31, 2020 and 2019, respectively, and resulted in gross realized gains of \$-0- for 2020 and gross realized gains of \$101 thousand for 2019.

Securities of \$57.2 and \$39.4 million at December 31, 2020 and 2019, respectively, were pledged as collateral for public deposits and for other purposes required by law. At December 31, 2020 and 2019, the carrying value of securities underlying repurchase agreements were \$6.5 and \$6.8 million, respectively.

4. Loans Receivable

Loans receivable and allowance for loan losses consist of the following at December 31, 2020 and 2019:

(dollars in thousands)	2020			2019		
	Originated	Acquired	Total	Originated	Acquired	Total
Construction and land development	\$ 25,370	\$ 1,152	\$ 26,522	\$ 34,587	\$ 2,435	\$ 37,022
Real estate mortgage:						
Commercial properties	146,410	27,188	173,598	131,254	33,785	165,039
Residential properties	90,870	3,867	94,737	97,756	5,962	103,718
Total real estate mortgage	262,650	32,207	294,857	263,597	42,182	305,779
Commercial and industrial	48,431	5,343	53,774	26,235	7,363	33,598
Consumer	4,700	518	5,218	4,512	635	5,147
Total gross loans	315,781	38,068	353,849	294,344	50,180	344,524
Less unearned income and deferred fees, net	(1,437)	-	(1,437)	(1,144)	-	(1,144)
Loans, net	314,344	38,068	352,412	293,200	50,180	343,380
Allowance for loan/lease losses	(5,179)	-	(5,179)	(3,796)	-	(3,796)
Loans, net of allowance	<u>\$ 309,165</u>	<u>\$ 38,068</u>	<u>\$ 347,233</u>	<u>\$ 289,404</u>	<u>\$ 50,180</u>	<u>\$ 339,584</u>

On November 1, 2019, the Bank acquired City National Bank. As a result of this acquisition, the Bank recorded loans with a fair value of \$52.6 million. Of those loans, \$42.8 million were considered to be purchased credit impaired (PCI) loans, which are loans for which it is probable at acquisition date that all contractually required payments will not be collected. The remaining loans, \$9.8 million, were considered to be purchased non-impaired loans and their related fair value discount or premium is being recognized as an adjustment to yield over the remaining life of each loan.

The following table relates to acquired City National Bank PCI loans and summarizes the contractually required payments, which includes principal and interest, expected cash flows to be collected, and the fair value of acquired PCI loans at the acquisition date.

(dollars in thousands)	
Contractually-required principal and interest	\$ 59,990
Non-accretable difference	<u>(9,786)</u>
Cash flows expected to be collected	50,204
Accretable yield	<u>(7,424)</u>
Fair value of loans accounted for under ASC 310-30	<u>\$ 42,780</u>

4. Loans Receivable

The following table presents changes in the carrying value of PCI Loans:

	For the Year Ended December 31, 2020	For the Year Ended December 31, 2019
(dollars in thousands)		
Balance at beginning of period	\$ 40,490	\$ -
Additions due to acquisition of City National Bank	-	42,780
Change due to payments received and accretion	(11,217)	(2,335)
Change due to loan charge-offs	-	-
Transfers to foreclosed real estate	-	-
Other	1,480	45
Balance at end of period	<u>\$ 30,753</u>	<u>\$ 40,490</u>

The following table presents changes for the years ended December 31, 2020 and 2019 in the accretable yield on purchased credit impaired loans for which the Company applies ASC 310-30.

	2020	2019
Accretable yield at beginning of period, January 1	\$ 7,061	\$ -
Additions	-	7,424
Accretion	(1,901)	(363)
Reclassification of nonaccretable difference due to improvement in expected cash flows	323	-
Other changes, net	848	-
Accretable yield at end of period, December 31	<u>\$ 6,331</u>	<u>\$ 7,061</u>

4. Loans Receivable (continued)

Major loan concentrations are as follows:

(dollars in thousands)	2020			2019		
	Originated	Acquired	Total	Originated	Acquired	Total
Church loans collateralized by real estate	\$ 61,012	\$ 17,543	\$ 78,555	\$ 59,191	\$ 22,221	\$ 81,412
Commercial loans to churches	39	-	39	21	-	21
Total loans to churches	<u>\$ 61,051</u>	<u>\$ 17,543</u>	<u>\$ 78,594</u>	<u>\$ 59,212</u>	<u>\$ 22,221</u>	<u>\$ 81,433</u>

Substantially all of the Bank's originated loans have been made to borrowers within the Washington, DC metropolitan area. Accordingly, the ability of the Bank's borrowers to repay their loans is dependent upon the economy in the Washington, DC metropolitan area. The acquired loans were primarily made to borrowers in the New Jersey and New York City region. Accordingly, the ability of the Bank's acquired borrowers to repay their loans is dependent upon the economy in the New Jersey / New York metropolitan area.

The Company's goal is to mitigate risks from an unforeseen threat to the loan portfolio as a result of an economic downturn or other negative influences. Plans that aid in mitigating these potential risks in managing the loan portfolio include: enforcing loan policies and procedures, evaluating the borrower's business plan through the loan term, identifying and monitoring primary and alternative sources of repayment, and obtaining adequate collateral to mitigate loss in the event of liquidation. Specific reserves are established based upon credit and/or collateral risks on an individual loan basis. A risk rating system is used to estimate potential loss exposure and to provide a measuring system for setting general and specific reserve allocations.

The Company maintains a general valuation allowance for each portfolio segment. These portfolio segments include commercial and industrial, commercial real estate, real estate construction, residential real estate, and consumer with risk characteristics described as follows:

As of December 31, 2020, the real estate loan portfolio constituted 83% of the total loan portfolio. This can be broken down further into the following categories: 7% construction and land development, 49% commercial real estate and 27% residential real estate loans, as a percent of total gross loans.

The Company's construction and land development loans are secured by real property where the loan funds will be used to acquire land and to construct or improve appropriately zoned real property for the creation of income producing or owner-occupied commercial properties. Borrowers are generally required to put equity into the project at levels determined by the loan committee and usually are underwritten with a maximum term of 24 months.

Commercial real estate loans are secured by improved real property which is generating income in the normal course of business. Debt service coverage, assuming stabilized occupancy, must be satisfied to support a permanent loan. The debt service coverage ratio is ordinarily at 1.40 to 1.00. These loans are generally underwritten with a term not greater than 10 years or the remaining useful life of the property, whichever is lower. The preferred term is between 5 to 7 years, with amortization to a maximum of 25 years.

Residential real estate loans are secured by the improved real property of the borrower and are usually underwritten with a term of 1 to 5 years but may be underwritten with terms up to 30 years.

4. Loans Receivable (continued)

The Company also makes commercial and industrial loans for a variety of purposes, which include working capital, equipment and accounts receivable financing. This category represented about 15% of the loan portfolio at December 31, 2020. Loans in this category generally carry a variable interest rate. Commercial loans meet reasonable underwriting standards, including appropriate collateral and cash flow necessary to support debt service. Personal guarantees are generally required but may be limited.

Approximately 1% of the loan portfolio at December 31, 2020 consisted of home equity loans and lines of credit and other consumer loans. These loans, while making up a small portion of the loan portfolio, demand the same emphasis on underwriting and credit evaluation as other types of loans advanced by the Company.

A summary of transactions in the allowance for loan losses is as follows for the years ended December 31, 2020 and 2019. The beginning balances and provision amounts have changed to more closely reflect the underlying calculation of the allowance for loan losses:

(dollars in thousands)	Construction and Land Development	Commercial Real Estate	Residential Real Estate	Commercial and Industrial	Consumer	Total
Balance, beginning of year 2020	\$ 282	\$ 1,293	\$ 566	\$ 1,533	\$ 122	\$ 3,796
Provision charged to operations	194	1,667	352	(358)	14	1,869
Loans charged off	-	(232)	(127)	(169)	(183)	(711)
Recoveries	-	45	77	5	98	225
Balance, end of year 2020	<u>\$ 476</u>	<u>\$ 2,773</u>	<u>\$ 868</u>	<u>\$ 1,011</u>	<u>\$ 51</u>	<u>\$ 5,179</u>
Ending balance:						
Individually evaluated for impairment	\$ -	\$ -	\$ -	\$ 590	\$ -	\$ 590
Purchase credit impaired loans	-	-	-	-	-	-
Collectively evaluated for impairment	476	2,773	868	421	51	4,589
Total	<u>\$ 476</u>	<u>\$ 2,773</u>	<u>\$ 868</u>	<u>\$ 1,011</u>	<u>\$ 51</u>	<u>\$ 5,179</u>
Loans:						
Individually evaluated for impairment	\$ -	\$ 5,134	\$ 1,888	\$ 3,727	\$ -	\$ 10,749
Purchase credit impaired loans	1,152	23,371	2,724	3,441	65	30,753
Collectively evaluated for impairment	25,370	145,093	90,125	46,606	5,153	312,347
Total	<u>\$ 26,522</u>	<u>\$ 173,598</u>	<u>\$ 94,737</u>	<u>\$ 53,774</u>	<u>\$ 5,218</u>	<u>\$ 353,849</u>
Balance, beginning of year 2019	\$ 312	\$ 2,238	\$ 1,180	\$ 363	\$ 40	\$ 4,133
Provision charged to operations	(30)	(909)	(596)	1,926	109	500
Loans charged off	-	(140)	(38)	(948)	(30)	(1,156)
Recoveries	-	104	20	192	3	319
Balance, end of year 2019	<u>\$ 282</u>	<u>\$ 1,293</u>	<u>\$ 566</u>	<u>\$ 1,533</u>	<u>\$ 122</u>	<u>\$ 3,796</u>
Ending balance:						
Individually evaluated for impairment	\$ -	\$ -	\$ 5	\$ 948	\$ -	\$ 953
Purchase credit impaired loans	-	-	-	-	-	-
Collectively evaluated for impairment	282	1,293	561	585	122	2,843
Total	<u>\$ 282</u>	<u>\$ 1,293</u>	<u>\$ 566</u>	<u>\$ 1,533</u>	<u>\$ 122</u>	<u>\$ 3,796</u>
Loans:						
Individually evaluated for impairment	\$ -	\$ 5,516	\$ 802	\$ 2,429	\$ -	\$ 8,747
Purchase credit impaired loans	1,967	29,638	4,066	4,727	92	40,490
Collectively evaluated for impairment	35,055	129,885	98,850	26,442	5,055	295,287
Total	<u>\$ 37,022</u>	<u>\$ 165,039</u>	<u>\$ 103,718</u>	<u>\$ 33,598</u>	<u>\$ 5,147</u>	<u>\$ 344,524</u>

Impairment is based on estimated collateral values for loans individually evaluated for impairment.

4. Loans Receivable (continued)

Credit quality indicators as of December 31, 2020 and 2019 are as follows:

Internally assigned grade:

Pass – loans in this category have strong asset quality and liquidity along with a multi-year track record of profitability.

Special mention – loans in this category are currently protected but are potentially weak. The credit risk may be relatively minor yet constitute an increased risk in light of the circumstances surrounding a specific loan.

Substandard – loans in this category show signs of continuing negative financial trends and unprofitability and therefore, are inadequately protected by the current soundness and paying capacity of the obligor or of the collateral pledged, if any.

Doubtful – loans in this category are illiquid and highly leveraged, have negative net worth, cash flow, and trending serious losses. The possibility of loss is extremely high; however, because of certain important and reasonably specific pending factors which may work to the advantage and strengthening of the asset, its classification as loss is deferred until a more exact status may be determined.

The information for each of the credit quality indicators is updated on a quarterly basis in conjunction with the determination of the adequacy of the allowance for loan losses.

Loan portfolio credit exposure - Credit risk profile by internally assigned grade:

Originated Loan Portfolio

(dollars in thousands)	Construction and Land Development	Commercial Real Estate	Residential Real Estate	Commercial and Industrial	Consumer	Total
December 31, 2020						
Pass	\$ 25,370	\$ 113,349	\$ 89,211	\$ 41,397	\$ 4,700	\$ 274,027
Special Mention	-	27,806	-	4,587	-	32,393
Substandard	-	5,255	1,659	2,447	-	9,361
Doubtful	-	-	-	-	-	-
Loss	-	-	-	-	-	-
Total	\$ 25,370	\$ 146,410	\$ 90,870	\$ 48,431	\$ 4,700	\$ 315,781

Acquired Loan Portfolio

	Construction and Land Development	Commercial Real Estate	Residential Real Estate	Commercial and Industrial	Consumer	Total
December 31, 2020						
Pass	\$ 965	\$ 20,244	\$ 3,645	\$ 4,390	\$ 518	\$ 29,762
Special Mention	187	6,944	222	953	-	8,306
Substandard	-	-	-	-	-	-
Doubtful	-	-	-	-	-	-
Loss	-	-	-	-	-	-
Total	\$ 1,152	\$ 27,188	\$ 3,867	\$ 5,343	\$ 518	\$ 38,068

4. Loans Receivable (continued)
Originated Loan Portfolio

(dollars in thousands)	Construction and Land Development	Commercial Real Estate	Residential Real Estate	Commercial and Industrial	Consumer	Total
December 31, 2019						
Pass	\$ 34,587	\$ 119,606	\$ 96,045	\$ 19,252	\$ 4,512	\$ 274,002
Special Mention	-	5,866	-	4,168	-	10,034
Substandard	-	5,782	1,711	2,591	-	10,084
Doubtful	-	-	-	224	-	224
Loss	-	-	-	-	-	-
Total	\$ 34,587	\$ 131,254	\$ 97,756	\$ 26,235	\$ 4,512	\$ 294,344

Acquired Loan Portfolio

	Construction and Land Development	Commercial Real Estate	Residential Real Estate	Commercial and Industrial	Consumer	Total
December 31, 2019						
Pass	\$ 1,217	\$ 23,837	\$ 5,711	\$ 6,867	\$ 635	\$ 38,267
Special Mention	1,024	3,714	-	496	-	5,234
Substandard	194	6,234	251	-	-	6,679
Doubtful	-	-	-	-	-	-
Loss	-	-	-	-	-	-
Total	\$ 2,435	\$ 33,785	\$ 5,962	\$ 7,363	\$ 635	\$ 50,180

Information on impaired loans for the years ended December 31, 2020 and 2019 is as follows:

(dollars in thousands)	Unpaid Contractual Principal Balance	Recorded Investment With No Allowance	Recorded Investment With Allowance	Total Recorded Investment	Related Allowance	Average Recorded Investment	Interest Income Recognized
December 31, 2020							
Construction and land development	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Commercial real estate	5,134	5,134	-	5,134	-	5,915	143
Residential real estate	1,888	1,888	-	1,888	-	2,129	-
Commercial and industrial	3,727	1,674	2,053	3,727	590	3,878	54
Consumer	-	-	-	-	-	-	-
Total	\$ 10,749	\$ 8,696	\$ 2,053	\$ 10,749	\$ 590	\$ 11,922	\$ 197
December 31, 2019							
Construction and land development	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Commercial real estate	5,516	5,516	-	5,516	-	5,827	232
Residential real estate	802	595	207	802	5	1,005	42
Commercial and industrial	2,429	12	2,417	2,429	948	2,803	110
Consumer	-	-	-	-	-	-	-
Total	\$ 8,747	\$ 6,123	\$ 2,624	\$ 8,747	\$ 953	\$ 9,635	\$ 384

4. Loans Receivable (continued)

The following table presents, by class of loan, an aging analysis and the recorded investments in loans past due as of December 31, 2020 and 2019:

Originated Loan Portfolio	Accruing Interest			Total Nonaccrual	Total Loans
	Current	30-89 Days Past Due	More Than 90 Days Past Due		
(dollars in thousands)					
December 31, 2020					
Construction and land development	\$ 17,876	\$ 7,224	\$ 270	\$ -	\$ 25,370
Commercial real estate	120,389	17,050	6,351	2,620	146,410
Residential real estate	81,320	3,085	3,529	2,936	90,870
Commercial and industrial	44,610	1,802	1,571	448	48,431
Consumer	4,306	80	314	-	4,700
Total	\$ 268,501	\$ 29,241	\$ 12,035	\$ 6,004	\$ 315,781

Acquired Loan Portfolio	Accruing Interest			Total Nonaccrual	Total Loans
	Current	30-89 Days Past Due	More Than 90 Days Past Due		
(dollars in thousands)					
December 31, 2020					
Construction and land development	\$ 965	\$ -	\$ 187	\$ -	\$ 1,152
Commercial real estate	20,076	5,070	2,042	-	27,188
Residential real estate	3,169	526	172	-	3,867
Commercial and industrial	4,686	448	209	-	5,343
Consumer	518	-	-	-	518
Total	\$ 29,414	\$ 6,044	\$ 2,610	\$ -	\$ 38,068

Originated Loan Portfolio	Accruing Interest			Total Nonaccrual	Total Loans
	Current	30-89 Days Past Due	More Than 90 Days Past Due		
(dollars in thousands)					
December 31, 2019					
Construction and land development	\$ 34,530	\$ 57	\$ -	\$ -	\$ 34,587
Commercial real estate	123,983	4,709	465	2,097	131,254
Residential real estate	89,646	6,238	-	1,872	97,756
Commercial and industrial	23,723	267	1,616	629	26,235
Consumer	3,519	701	49	243	4,512
Total	\$ 275,401	\$ 11,972	\$ 2,130	\$ 4,841	\$ 294,344

Acquired Loan Portfolio	Accruing Interest			Total Nonaccrual	Total Loans
	Current	30-89 Days Past Due	More Than 90 Days Past Due		
(dollars in thousands)					
December 31, 2019					
Construction and land development	\$ 2,241	\$ 194	\$ -	\$ -	\$ 2,435
Commercial real estate	30,077	3,186	522	-	33,785
Residential real estate	5,674	288	-	-	5,962
Commercial and industrial	6,108	1,198	57	-	7,363
Consumer	626	3	6	-	635
Total	\$ 44,726	\$ 4,869	\$ 585	\$ -	\$ 50,180

4. Loans Receivable (continued)

The Bank's loan portfolio also includes certain loans with deferments that have been modified in connection with COVID-19. A summary of modified loans in connection with COVID-19 not categorized as troubled debt restructurings are as follows:

(dollars in thousands)	Modified During the Year Ended		Still Under Modification at	
	December 31, 2020		December 31, 2020	
Construction and land development	5	\$ 9,534	-	\$ -
Commercial real estate	91	72,823	1	793
Residential real estate	15	7,283	-	-
Commercial and industrial	11	2,835	-	-
Consumer	10	783	-	-
Total	132	\$ 93,258	1	\$ 793

The following table presents Information on performing, restructured and nonperforming loans as of December 31, 2020 and 2019:

(dollars in thousands)	Construction and Land	Commercial	Residential	Commercial and		
December 31, 2020	Development	Real Estate	Real Estate	Industrial	Consumer	Total
Purchase credit impaired loans	\$ 1,152	\$ 23,371	\$ 2,724	\$ 3,441	\$ 65	\$ 30,753
Restructured performing	-	-	2,367	-	-	2,367
Nonperforming	-	3,321	1,139	3,727	-	8,187
Restructured nonperforming	-	1,813	749	-	-	2,562
	\$ 1,152	\$ 28,505	\$ 6,979	\$ 7,168	\$ 65	\$ 43,869
Performing	25,370	145,093	87,758	46,606	5,153	309,980
Total	\$ 26,522	\$ 173,598	\$ 94,737	\$ 53,774	\$ 5,218	\$ 353,849
December 31, 2019						
Purchase credit impaired loans	\$ 1,967	\$ 29,638	\$ 4,066	\$ 4,727	\$ 92	\$ 40,490
Restructured performing	-	-	2,737	-	-	2,737
Nonperforming	-	5,516	-	2,429	-	7,945
Restructured nonperforming	-	-	802	-	-	802
	\$ 1,967	\$ 35,154	\$ 7,605	\$ 7,156	\$ 92	\$ 51,974
Performing	35,055	129,885	96,113	26,442	5,055	292,550
Total	\$ 37,022	\$ 165,039	\$ 103,718	\$ 33,598	\$ 5,147	\$ 344,524

4. Loans Receivable (continued)

The following tables present Information on troubled debt restructurings for the years ended December 31, 2020 and 2019:

<i>(dollars in thousands)</i>	Number of	Pre-modification Outstanding Recorded	Post-modification Outstanding
	Loans	Investment	Recorded Investment
December 31, 2020	2	\$2,036	\$2,036
December 31, 2019	3	\$609	\$609

There were no troubled debt restructurings which have re-defaulted (defined as past due 90 days) during the years ended December 31, 2020 and 2019 that were restructured within the twelve months prior to such re-default.

Modifications consisted of one commercial and one residential loan in the year ended 2020 and were only residential loans in the year ended 2019.

Troubled debt restructuring modifications during the years ended December 31, 2020 and 2019 consisted of reductions in principal, changes in interest rates and maturity extensions. Troubled debt restructurings are considered as part of the qualitative and quantitative analysis in the determining the adequacy of the allowance for loan losses.

Performing TDRs were in compliance with their modified terms and there are no further commitments associated with these loans.

Consumer mortgage loans collateralized by residential real estate property that were in process of foreclosure totaled \$-0- as of December 31, 2020 and 2019, respectively. Commercial mortgage loans collateralized by commercial real estate property that were in process of foreclosure totaled \$-0-as of December 31, 2020 and 2019. At December 31, 2020 and 2019, the Bank held one residential property in REO totaling \$260.

Loans serviced for others and not reflected in the balance sheets are \$1,148 and \$1,209 at December 31, 2020 and 2019, respectively. Servicing loans for others generally consists of collecting mortgage payments, maintaining escrow accounts, disbursing payments to investors and foreclosure processing. Loan servicing income is recorded on the accrual basis and includes servicing fees from investors and certain charges collected from borrowers, such as late payment fees. There were no mortgage servicing rights capitalized during 2020 and 2019.

5. Premises and Equipment

The major categories of premises and equipment are as follows:

<u>(dollars in thousands)</u>	<u>2020</u>	<u>2019</u>
Land	\$ 1,619	\$ 1,675
Bank premises	8,346	8,919
Furniture, fixtures and equipment	10,112	9,675
Leasehold improvements	1,008	1,016
Construction in progress	642	175
Total	21,727	21,460
Accumulated depreciation and amortization	(12,561)	(12,684)
Premises and equipment, net	<u>\$ 9,166</u>	<u>\$ 8,776</u>

Construction in process contains all expenses incurred on various assets until they are converted into working condition. The construction in process account primarily contained expenses related to building renovation. Both properties are owned by the Bank.

Depreciation expense for the years ended December 31, 2020 and 2019 was \$441 and \$491, respectively.

The Bank did not immediately acquire the furniture or equipment of CNB as part of the purchase and assumption agreement. However, the Bank subsequently purchased certain furniture and equipment, associated with leased facilities that the Bank agreed to assume, from the FDIC at fair value in the amount of \$584 during 2020.

6. Intangible Assets

Acquired intangible assets from the CNB transaction consisted of a core deposit intangible with a gross carrying amount of \$610 on November 1, 2019. Accumulated amortization was \$265 at December 31, 2020 for a net carrying amount of \$345. Amortization expense for the year ended December 31, 2020 and 2019 was \$223 and \$42, respectively. Amortization expense is expected to be approximately \$131 per year through 2023.

7. Deposits

At December 31, 2020 and 2019, certificates of deposit of \$250 or more totaled \$13 million and \$15 million, respectively. These deposit totals do not include certificates of deposit held through the Certificate of Deposit Account Registry Service (CDARS) program which holds reciprocal balances at less than \$250. At December 31, 2020 and 2019, the Bank held certificates of deposit through the CDARS program which totaled \$32 million and \$52 million, respectively. At December 31, 2020, the scheduled maturities of certificates of deposits are as follows:

<u>(dollars in thousands)</u>	
2021	\$ 69,106
2022	11,951
2023	1,668
2024	1,093
2025 and thereafter	1,518
	<u>\$ 85,336</u>

8. Short-Term Borrowing

The following table summarizes information for short-term borrowings for the years ended December 31:

(dollars in thousands)	2020		2019	
	Amount	Rate	Amount	Rate
At year end:				
Federal Home Loan Bank advances	\$ -		\$ -	
Retail repurchase agreements	4,626	0.20%	3,335	0.20%
Other short-term borrowings	-		-	
Total	<u>\$ 4,626</u>		<u>\$ 3,335</u>	
Average for the year:				
Federal Home Loan Bank advances	\$ -	0.00%	\$ 17,500	1.85%
Retail repurchase agreements	4,812	0.20%	4,265	0.20%
Other short-term borrowings	-	0.00%	16	3.95%
Total	<u>\$ 4,812</u>		<u>\$ 21,781</u>	
Maximum month end balance:				
Federal Home Loan Bank advances	\$ -		\$ 34,000	
Retail repurchase agreements	9,216		5,503	
Other short-term borrowings	-		3,000	
Total	<u>\$ 9,216</u>		<u>\$ 42,503</u>	

Securities sold under agreements to repurchase are securities sold to customers, at the customers' request, under a "roll-over" contract that matures in one business day. The underlying securities sold are Government agency securities which are segregated in the Bank's custodial accounts from other investment securities.

The Bank periodically borrows under a secured line of credit from the Federal Home Loan Bank of Atlanta to meet short-term liquidity needs. At December 31, 2020 and 2019, advances totaled \$-0- from the Federal Home Loan Bank of Atlanta were secured by a blanket lien on the Bank's qualifying commercial and residential mortgages and investment securities. The total credit available to the Bank at December 31, 2020 and 2019 was \$138 and \$106 million respectively, based on qualifying collateral of \$76 and \$84 million, respectively. The Bank normally borrows in short term increments of 90 days or less maturities at fixed rates; however, varied rates and term products are available to the Bank.

The Bank also had an unsecured line of credit of \$3 million with a correspondent available for overnight borrowing during 2020 and 2019. During 2020, the \$3 million line was not drawn upon. During 2019, \$3 million was drawn for 2 days. There was none outstanding on the line of credit at December 31, 2020 or December 31, 2019.

9. Leases

Substantially all of the leases in which the Company is the lessee are comprised of real estate property for branches, office locations and office equipment rentals with terms extending through July 2028. All of the Company's leases are classified as operating leases.

The following table provides information with respect to the Company's operating leases:

(dollars in thousands)	2020	2019
Operating lease cost	\$ 717	\$ 482
Short-term lease cost	388	68
Total lease cost	<u>\$ 1,105</u>	<u>\$ 550</u>

Cash paid for amounts included in the measurement of lease liabilities:

Operating cash flows from leases	\$ 782	\$ 559
Weighted-average remaining lease term in years	6	7
Weighted-average discount rate	2.76%	2.75%

Sublease income amounted to \$-0- for the years ending December 31, 2020 and 2019.

Net gains recognized from sale and leaseback transactions amounted to \$7,553 and \$2,449 for the years ending December 31, 2020 and 2019, respectively.

The following table presents the unamortized balance of the Company's ROU assets and lease liabilities on the consolidated financial statements at December 31, 2020 and 2019:

(dollars in thousands)	2020	2019
Operating right-to-use assets	\$ 2,239	\$ 2,682
Operating right-to-use assets recorded in connection with acquisition of CNB	1,319	1,594
Total lease right-of-use assets	<u>\$ 3,558</u>	<u>\$ 4,276</u>
Operating lease liabilities	\$ 2,276	\$ 2,722
Operating lease liabilities recorded in connection with acquisition of CNB	1,313	1,572
Total lease liabilities	<u>\$ 3,589</u>	<u>\$ 4,294</u>

At December 31, 2020, maturities of lease liabilities were as follows:

(dollars in thousands)	Operating Leases
2021	\$ 779
2022	674
2023	685
2024	708
2025	475
Years thereafter	513
Total future minimum lease payments	<u>\$ 3,834</u>
Amounts representing interest	(245)
Total operating lease liabilities	<u>\$ 3,589</u>

10. Regulatory Matters

The Company and the Bank are subject to various regulatory capital requirements 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 effect on the Company's and the Bank's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Company and the Bank must meet specific capital guidelines that involve quantitative measures of their assets, liabilities, and certain off-balance sheet items as calculated under regulatory accounting practices. The Bank's capital amounts and its classification under the regulatory framework for prompt corrective action are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

In August 2018, the Federal Reserve updated the Small Bank Holding Company Policy Statement (the "Statement"), in compliance with the Economic Growth, Regulatory Relief and Consumer Protection Act of 2018 ("EGRRCPA"). The Statement, among other things, exempts bank holding companies with consolidated total assets of less than \$3 billion from being subject to regulatory capital requirements on a consolidated basis.

The final rules implementing Basel Committee on Banking Supervision's capital guidelines for U.S. banks (the Basel III rules) became effective for the Bank on January 1, 2015 with full compliance with all of the requirements being phased in over a multi-year schedule, and fully phased in by January 1, 2019. As a part of the new requirements, the Common Equity Tier 1 Capital ratio is calculated and utilized in the assessment of capital for all institutions. The Company has made an election to not have the net unrealized gain or loss on available-for-sale securities included in computing regulatory capital. Under the Basel III rules, the Bank must hold a capital conservation buffer above the adequately capitalized risk-based capital ratios. The capital conservation buffer was phased in from 0.625%

or 2016 to 2.50% by 2019. The capital conservation buffer for 2019 is 2.50%. Management believes as of December 31, 2020 and 2019, the Bank meets all capital adequacy requirement to which they are subject. (1) Except regarding the Bank's Tier 1 to average assets ratio, the Bank's minimum capital requirement includes the phased-in portion of the Basel III Capital Rules and capital conservation buffer.

Prompt corrective action regulations provide five classifications: well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized, and critically undercapitalized, although these terms are not used to represent overall financial condition. If adequately capitalized, regulatory approval is required to accept brokered deposits. If undercapitalized, capital distributions are limited, as is asset growth and expansion, and capital restoration plans are required. At year-end 2019 and 2018, the most recent regulatory notification categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. There are no conditions or events since that notification that management believes have changed the institution's category.

Federal and state banking regulations place certain restrictions on dividends paid by the Company. The total amount of dividends which may be paid at any date is generally limited to retained earnings of the Company. Pursuant to the EGRRCPA, regulators have provided for an optional, simplified measure of capital adequacy, the community bank leverage ratio framework ("CBLR"), for qualifying community bank organizations. Banks that qualify may opt in to the CBLR framework beginning January 1, 2020 or any time thereafter. The CBLR framework eliminates the four required capital ratios disclosed below and requires the disclosure of a single leverage ratio, with a minimum requirement of 9%. The Company is evaluating whether to opt in to the CBLR framework.

(dollars in thousands)	Actual		Minimum (1) Required for Capital Adequacy Purposes		To be Categorized as Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2020:						
Total capital (to risk-weighted assets)	\$ 49,035	14.27%	\$ 36,075	10.50%	\$ 34,357	10.00%
Tier 1 capital (to risk-weighted assets)	44,729	13.02%	29,203	8.50%	27,486	8.00%
CET1 (to risk-weighted assets)	44,729	13.02%	24,050	7.00%	22,332	6.50%
Tier 1 capital (to average assets)	44,729	7.98%	36,440	6.50%	28,031	5.00%
As of December 31, 2019:						
Total capital (to risk-weighted assets)	\$ 42,918	12.14%	\$ 37,124	10.000%	\$ 35,356	10.00%
Tier 1 capital (to risk-weighted assets)	39,122	11.07%	30,053	8.000%	28,285	8.00%
CET1 (to risk-weighted assets)	39,122	11.07%	24,749	6.500%	22,982	6.50%
Tier 1 capital (to average assets)	39,122	8.12%	31,310	5.000%	24,085	5.00%

11. Income Taxes

The provision for income taxes consists of the following (**in thousands**) for the years ended December 31:

	2020	2019
Current income tax expense (benefit):		
Federal income tax	\$ 2,752	\$ 1,317
State income tax	203	(122)
Total current income tax expense	2,955	1,195
Deferred income tax expense (benefit):		
Federal income tax	\$ (665)	\$ 293
State income tax	(203)	104
Total deferred income tax expense	(868)	397
Total income tax expense	\$ 2,087	\$ 1,592

The components of the deferred tax benefit resulting from net temporary differences are as follows (**in thousands**) for the years ended December 31:

	2020	2019
Income before taxes	\$ 7,761	\$ 5,628
Federal income tax rate	21%	21%
Tax expense at statutory rate	1,630	1,182
Differences resulting from:		
State tax expense, net of federal tax effect	469	322
Bank owned life insurance	(48)	(95)
Tax-exempt interest	(26)	(17)
Nondeductible expenses	4	9
Federal tax rate change	-	-
True ups and other	58	191
Provision for income taxes	\$ 2,087	\$ 1,592
Effective tax rate	27%	28%

The major components of deferred tax assets and (liabilities) are summarized at December 31, 2020 and 2019, as follows (**in thousands**):

	2020	2019
Allowance for loan losses	\$ 1,145	\$ 674
Accrued bonus and Retirement benefits	97	90
Deferred loan costs	771	690
Nonaccrual interest income	200	153
Depreciation	(571)	(480)
Acquisition accounting adjustments	(267)	(621)
Right-of-use asset	(976)	(1,173)
Lease liability	984	1,178
Unrealized gain on equity securities	(4)	-
Impairment of equity securities	34	34
Unrealized losses (gains) on AFS securities	(1,050)	(351)
Net deferred tax asset	\$ 363	\$ 194

**Notes to Consolidated Statements
Years Ended December 31, 2020 and 2019
(dollars in thousands)**

12. Profit Sharing Plan

The Company has a profit sharing plan, qualifying under Section 401(k) of the Internal Revenue Code, for those employees who meet the eligibility requirements set forth in the plan. The plan does not require the Company to match the participants' contributions. The Company contributions to the plan were \$241 for years 2020 and 2019.

13. Employee Stock Ownership Plan

In 1986, the Bank implemented an Employee Stock Ownership Plan ("ESOP") that covered substantially all full-time employees. No contributions were made in 2020 or 2019. Shares held by the ESOP participants totaled 11,758 or 1.97% of the Company's stock at December 31, 2020.

14. Commitments and Contingencies

In the normal course of business, there are outstanding various commitments and contingent liabilities, such as commitments to extend credit, which are not shown in the accompanying consolidated financial statements (dollars in thousands). The Company does not anticipate any material losses as a result of these transactions. At December 31, 2020 and 2019 the Bank had commitments to fund loans outstanding for approximately \$22 million and \$25 million, respectively. The Bank also had standby letters of credit outstanding at December 31, 2020 and 2019 in the amount of \$1,156 and \$1,169 respectively. Such commitments and standby letters of credit are subject to the Bank's normal underwriting standards. Since many of the commitments are expected to expire without being completely drawn upon, the total commitment amounts do not necessarily represent future cash requirements.

15. Fair Value Measurements and Estimated Fair Value of Financial Instruments

The Company has adopted FASB ASC Topic 820, "Fair Value Measurements " and FASB ASC Topic 825, "the Fair Value Option for Financial Assets and Financial Liabilities" which provides a framework for measuring and disclosing fair value under generally accepted accounting principles. FASB ASC Topic 820 requires disclosures about the fair value of assets and liabilities recognized in the balance sheet in periods subsequent to initial recognition, whether the measurements are made on a recurring basis (for example, available-for-sale investment securities) or on a nonrecurring basis (for example, impaired loans).

FASB ASC Topic 820 defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. FASB ASC Topic 820 also establishes a fair value hierarchy, which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The Company utilizes fair value measurements to record fair value adjustments to certain assets and to determine fair value disclosures. Securities available for sale and loans held for sale are recorded at fair value on a recurring basis. Additionally, from time to time, the Company may be required to record at fair value other assets on a nonrecurring basis, such as impaired loans and REO. These nonrecurring fair value adjustments typically involve application of lower of cost or market accounting or write-downs of individual assets.

Under FASB ASC Topic 820, the Company groups assets and liabilities at fair value in three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine the fair value.

These hierarchy levels are:

Level 1 Valuation for assets and liabilities traded in active exchange markets. Valuations are obtained from readily available pricing sources for Market transactions involving identical assets or liabilities.

Level 2 Valuations for assets and liabilities traded in less active dealer or broker markets. Valuations are obtained from third party pricing services for identical or comparable assets or liabilities which use observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in active markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3 Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

A financial instrument's level within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement.

The types of instruments valued based on quoted market prices in active markets include most U.S. government and agency securities, liquid mortgage products, active listed equities and most money market securities. Such instruments are generally classified within Level 1 or Level 2 of the fair value hierarchy. As required by FASB ASC Topic 820, the Company does not adjust the quoted price for such instruments.

The types of instruments valued based on quoted prices in markets that are not active, broker or dealer quotations, or alternative pricing sources with reasonable levels of price transparency include most investment-grade and high-yield corporate bonds, less liquid mortgage products, less liquid equities, state, municipal and provincial obligations and certain physical commodities.

Such instruments are generally classified within Level 2 of the fair value hierarchy. Level 3 is for positions that are not traded in actual markets or are subject to transfer restrictions, valuations are adjusted to reflect illiquidity and/or non-transferability, and such adjustments are generally based on available market evidence, management's best estimate is used.

15. Fair Value Measurements and Estimated Fair Value of Financial Instruments (continued)

The following table sets forth assets of the Company for which fair values are determined on a recurring basis as of December 31, 2020 and 2019:

(dollars in thousands)	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Fair Value
December 31, 2020				
Assets:				
Investments securities available-for-sale :				
U.S. Government Agency	\$ -	\$ 9,268	\$ -	\$ 9,268
Mortgage-Backed Securities	-	13,482	-	13,482
Collateralized Mortgage Obligations	-	43,619	-	43,619
Private label mortgage-backed securities	-	1,399	-	1,399
Municipal securities	-	21,109	-	21,109
Total	<u>\$ -</u>	<u>\$ 88,877</u>	<u>\$ -</u>	<u>\$ 88,877</u>
Equity investments with readily determinable fair value	<u>\$ 945</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 945</u>
December 31, 2019				
Assets:				
Investments securities available-for-sale :				
U.S. Government Agency	\$ -	\$ 9,674	\$ -	\$ 9,674
Mortgage-Backed Securities	-	18,292	-	18,292
Collateralized Mortgage Obligations	-	50,237	-	50,237
Private label mortgage-backed securities	-	2,005	-	2,005
Municipal securities	-	6,722	-	6,722
Total	<u>\$ -</u>	<u>\$ 86,930</u>	<u>\$ -</u>	<u>\$ 86,930</u>
Equity investments with readily determinable fair value	<u>\$ 910</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 910</u>

15. Fair Value Measurements and Estimated Fair Value of Financial Instruments (continued)

The following table sets forth the Company's financial assets and liabilities that were accounted for or disclosed at fair value on a nonrecurring basis as of December 31, 2020 and 2019:

(dollars in thousands)	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Impairment Losses
December 31, 2020				
Assets:				
Impaired loans	\$ -	\$ -	\$ 2,066	\$ 590
Real estate owned	-	-	260	260
Total	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 2,326</u>	<u>\$ 850</u>
December 31, 2019				
Assets:				
Impaired loans	\$ -	\$ -	\$ 1,671	\$ 953
Real estate owned	-	-	260	260
Total	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 1,931</u>	<u>\$ 1,213</u>

Impaired loans are evaluated and valued at the time the loan is identified as impaired, at the lower of cost or market value. Market value is measured based on the value of the collateral securing these loans and is classified at a Level 3 in the fair value hierarchy. Collateral may be real estate and/or accounts receivable. The value of real estate collateral is determined based on appraisal by qualified licensed appraisers hired by the Company. The value of business equipment, inventory and accounts receivable collateral is based on the net book value on the business' financial statements and, if necessary, discounted based on management's review and analysis. Appraised and reported values may be based upon knowledge changes in market conditions from the time of valuation, and/or management's expertise and knowledge of the client and client's business. Impaired loans are reviewed and evaluated on at least a quarterly

basis for additional impairment and adjusted accordingly, based on the same factors identified above.

Foreclosed properties are adjusted to fair value upon transfer of the loans to foreclosed properties. Subsequently, foreclosed properties are carried at the lower of carrying value or fair value. The estimated fair value for foreclosed properties included in Level 3 is determined by independent market based appraisals and other available market information, less cost to sell, that may be reduced further based on market expectations or an executed sales agreement. If fair value of the collateral deteriorates subsequent to initial recognition, the Company records the foreclosed properties as a nonrecurring Level 3 adjustment. Valuation techniques are consistent with those techniques applied in prior periods.

15. Fair Value Measurements and Estimated Fair Value of Financial Instruments (continued)

The following methods and assumptions were used to estimate the fair value of each category of financial instrument for which it is practicable to estimate value:

Cash and Cash Equivalents

The carrying amount of cash and cash equivalents approximates their fair value.

Short-term investments

The carrying amount of short-term investments approximates its fair value.

Investment Securities Available-for-Sale

The fair values of securities were based upon quoted market prices.

Restricted Stock

The carrying amount of restricted stock approximates its fair value.

Loans Held for Sale

The fair values of loans held for sale were based upon quoted market prices for loans with similar interest rates and terms to maturity.

Loans Receivable, net

The fair value of the loan portfolio, with the exception of the adjustable rate portfolio, was calculated by discounting the scheduled cash flows through the estimated maturity using anticipated prepayment speeds and using discount rates that reflect the credit and interest rate risk inherent in each loan portfolio. The fair value of the adjustable loan portfolio was estimated by grouping the loans with similar characteristics and comparing the characteristics of each group to the prices quoted for similar types of loans in the secondary market. The fair value disclosures for both the fixed and adjustable rate portfolios were adjusted to reflect the exit price amount anticipated to be received from the sale of the portfolio in an open market transaction as required upon adoption of ASU 2016-01, *Financial Instruments – Overall (Subtopic 825-10) Recognition and Measurement of Financial Assets and Financial Liabilities* beginning in the first quarter of 2018.

Bank Owned Life Insurance

The fair value of bank owned life insurance is the current cash surrender value, which is the carrying value.

Equity Investments with Readily Determinable Fair Value

The fair value of the Company's equity investment with readily determinable fair value is comprised of a mutual fund, the fair value for which is obtained from unadjusted quoted prices in active markets on the date

of measurement.

Accrued Interest Receivable

The carrying amount of accrued interest receivable approximates its fair value since it is short-term in nature and does not present unanticipated credit concerns.

Deposits

The fair value of demand deposits, savings accounts and certain money market account deposits is the amount payable on demand at the reporting date. The fair value of fixed maturity certificates of deposit is estimated using the rates currently offered for deposits of similar remaining maturities. The fair value disclosures for all of the deposits were adjusted to reflect the exit price amount anticipated to be received from the sale of the deposits in an open market transaction as required upon adoption of ASU 2016-01, *Financial Instruments – Overall (Subtopic 825-10) Recognition and Measurement of Financial Assets and Financial Liabilities* beginning in the first quarter of 2018.

Short-term Borrowings

The carrying amounts of federal funds purchased, borrowings under repurchase agreements, and other short-term borrowings, generally maturing within ninety days, approximate their fair values.

Accrued Interest Payable

The carrying amount of accrued interest payable approximates its fair value since it is short-term in nature.

Limitations

The fair value estimates are made at a discrete point in time based on relevant market information and information about the financial instruments. Fair value estimates are based on judgments regarding future expected loss experience, current economic conditions, risk characteristics of various financial instruments, and other factors.

These estimates are subjective in nature and involve uncertainties and matters of significant judgment and, therefore, cannot be determined with precision. Changes in assumptions could significantly affect the estimates. Further, the foregoing estimates may not reflect the actual amount that could be realized if all or substantially all of the financial instruments were offered for sale.

15. Fair Value Measurements and Estimated Fair Value of Financial Instruments (continued)

The estimated fair values of the Company's financial instruments at December 31, 2020 and 2019 are as follows:

(dollars in thousands)	Carrying Value	Estimated Fair Value	Fair Value Measurements as of December 31, 2020		
			Quoted Prices in	Significant Other	Significant
			Active Markets for Identical Assets	Observable Inputs	Unobservable Inputs
			Level 1	Level 2	Level 3
Financial Assets:					
Cash and cash equivalents	\$ 89,714	\$ 89,714	\$ 89,714	\$ -	\$ -
Short-term investments	2,559	2,559	2,559	-	-
Investment securities available-for-sale	88,877	88,877	-	88,877	-
Restricted stock	563	563	-	563	-
Loans held for sale	2,431	2,431	-	2,431	-
Loans receivable, net	347,233	360,494	-	-	360,494
Bank owned life insurance	9,620	9,620	-	9,620	-
Accrued interest receivable	2,496	2,496	-	2,496	-
Financial Liabilities:					
Deposits	502,033	519,032	-	519,032	-
Short-term borrowings	4,626	4,626	-	4,626	-
Accrued interest payable	139	139	-	139	-

(dollars in thousands)	Carrying Value	Estimated Fair Value	Fair Value Measurements as of December 31, 2019		
			Quoted Prices in	Significant Other	Significant
			Active Markets for Identical Assets	Observable Inputs	Unobservable Inputs
			Level 1	Level 2	Level 3
Financial Assets:					
Cash and cash equivalents	\$ 71,213	\$ 71,213	\$ 71,213	\$ -	\$ -
Short-term investments	2,659	2,659	2,659	-	-
Investment securities available-for-sale	86,930	86,930	-	86,930	-
Restricted stock	475	475	-	475	-
Loans held for sale	1,200	1,200	-	1,200	-
Loans receivable, net	339,584	345,994	-	-	345,994
Bank owned life insurance	9,467	9,467	-	9,467	-
Accrued interest receivable	1,227	1,227	-	1,227	-
Financial Liabilities:					
Deposits	479,009	473,723	-	473,723	-
Short-term borrowings	3,335	3,335	-	3,335	-
Accrued interest payable	324	324	-	324	-

16. Related Party Transactions

In the normal course of banking business, loans are made to officers and directors on substantially the same terms, including interest rates and collateral on loans, as those prevailing at the same time for comparable transactions with non-related parties and do not involve more than normal risk of collectability or present other unfavorable features. The following table presents an analysis of activity for loans to related parties at December 31, 2020 and 2019:

<u>(dollars in thousands)</u>	<u>2020</u>	<u>2019</u>
Balance, beginning of year	\$ 3,715	\$ 3,891
Principal additions	906	-
Principal payments	(126)	(176)
Balance, end of year	<u>\$ 4,495</u>	<u>\$ 3,715</u>

At December 31, 2020 and 2019, related party deposits totaled \$1,219 and \$479, respectively.

17. Other Noninterest Expense

Other expenses in the Consolidated Statements of Income include the following:

<u>(dollars in thousands)</u>	<u>2020</u>	<u>2019</u>
Marketing, advertising and business development	\$ 172	\$ 281
Retail service cost	103	171
Director fees	187	178
Other taxes	216	134
Other insurance	100	128
Subscriptions and memberships	181	187
Bank service charges	87	59
Training	24	170
Other	1,083	719
	<u>\$ 2,153</u>	<u>\$ 2,027</u>

18. Revenue Recognition - Noninterest Income

The following table presents the Company's noninterest income for the years ended December 31, 2020 and 2019 with identification of revenue streams in-scope and out-of-scope of Topic 606:

<u>(dollars in thousands)</u>	<u>2020</u>	<u>2019</u>
Service charges on deposit accounts	\$ 1,920	\$ 1,801
Gain on sale of Bank owned property (1)	7,553	2,449
Bargain purchase gain (1)	-	2,415
Net gains (losses) on investment securities (1)	-	101
Net gains (losses) on sales of loans (1)	313	210
Net gains (losses) on the sales of REO (1)	-	(345)
Other:		
Interchange fees	882	686
Lock box servicing (1)	4	562
Grants and awards (1)	5,494	246
Bank-owned life insurance income (1)	229	238
Life insurance proceeds (1)	-	209
Loss on impairment of equity securities (1)	-	(123)
Other noninterest income	277	484
	<u>\$ 16,672</u>	<u>\$ 8,933</u>

(1) Not within the scope of ASC 606

Contract balances and contract acquisition costs: The Company does not typically enter into long-term revenue contracts with customers and therefore, does not experience significant contract balances. As of December 31, 2020 and 2019, the Company did not have any significant contract balances. As of December 31, 2020 and 2019, the Company did not capitalize any contract acquisition costs.

19. Subsequent Events for 2020

Subsequent to year-end, the Company received \$10.5MM in capital from three large financial institutions. The Company down streamed \$10.0M of the capital to the Bank. The capital raised in May 2021, consisted of Tier 1 eligible preferred stock totaling \$8.5MM and \$2.0MM of common stock.

In preparing these consolidated financial statements, the Bank has evaluated events and transactions for potential recognition or disclosure through August 19, 2021, the date the consolidated financial statements were available to be issued.