

**FEDERAL DEPOSIT INSURANCE CORPORATION
WASHINGTON, DC 20429**

FORM 10-Q

(Mark One)

☒ **QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended September 30, 2019

☐ **TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from _____ to _____

FDIC Certificate Number: 19101

HARFORD BANK

(Name of registrant as specified in its charter)

Maryland
(State or other jurisdiction of
organization)

52-0799113
(IRS Employer incorporation or
Identification No.)

8 West Bel Air Avenue, Aberdeen, Maryland 21001
(Address of principal executive offices)

(410) 272-5000
(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act: None.

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

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes ☐ No ☐ (Not Applicable)

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

Large accelerated filer ☐

Accelerated filer ☐

Non-accelerated filer ☒

Smaller reporting company ☒

Emerging growth company ☐

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

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

State the number of shares outstanding of each of the issuer's classes of common equity, as of the latest practicable date.
1,422,564 shares of common stock as of November 5, 2019.

This Quarterly Report of Harford Bank (the “Bank”) on Form 10-Q may contain forward-looking statements within the meaning of The Private Securities Litigation Reform Act of 1995. Readers of this report should be aware of the speculative nature of “forward-looking statements”. Statements that are not historical in nature, including those that include the words “anticipate”, “estimate”, “should”, “expect”, “believe”, “intend”, and similar expressions, are forward-looking statements and are based on current expectations, estimates and projections about, among other things, the industry and the markets in which the Bank operates, and they are not guarantees of future performance. Whether actual results will conform to expectations and predictions is subject to known and unknown risks and uncertainties, including risks and uncertainties discussed in this report; general economic, market, or business conditions; changes in interest rates, deposit flow, the cost of funds, and demand for loan products and financial services; changes in the Bank’s competitive position or competitive actions by other companies; changes in the quality or composition of loan and investment portfolios; the ability to manage growth; changes in laws or regulations or policies of federal and state regulators and agencies; and other circumstances beyond the Bank’s control. Consequently, all of the forward-looking statements made in this document are qualified by these cautionary statements, and there can be no assurance that the actual results anticipated will be realized, or if substantially realized, will have the expected consequences on the Bank’s business or operations. These and other risks are discussed in detail in the periodic reports that the Bank files with the Federal Deposit Insurance Corporation (“FDIC”) (see Item 1A of Part II of this report for further information). Except as required by applicable laws, the Bank does not intend to publish updates or revisions of forward-looking statements it makes to reflect new information, future events or otherwise.

PART I

Item 1. Financial Statements

The information required by this item can be found beginning on page F-1 immediately following the signatures to this report and is incorporated herein by reference.

AVAILABLE INFORMATION

The Bank maintains an internet website at www.HarfordBank.com on which it makes available its most recent periodic report filed with the FDIC pursuant to the Exchange Act. All of the periodic and other reports filed by the Bank with the FDIC pursuant to the Exchange Act are generally available for public inspection at: Federal Deposit Insurance Corporation, Accounting and Securities Disclosure Section, Division of Supervision and Consumer Protection, 550 17th Street, NW, Washington, DC 20429.

Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations

The following discussion should be read and reviewed in conjunction with the interim consolidated financial statements and the notes thereto included elsewhere in this report, and with Management’s Discussion and Analysis of Financial Condition and Results of Operations, the audited consolidated financial statements and notes thereto, and the other statistical information contained in the Bank’s Annual Report on Form 10-K for the year ended December 31, 2018.

The Bank is a Maryland-chartered bank with its principal office in Aberdeen, Harford County, Maryland. Through its eight branches, seven of which are located throughout Harford County and one in Cecil County, the Bank offers a full range of deposit services that are typically offered by most banks, savings and loan associations, and credit unions, including checking accounts, NOW accounts, savings accounts and other time deposits of various types, ranging from money market accounts to longer-term certificates of deposit. In addition, the Bank offers Individual Retirement Accounts (“IRAs”). The Bank also offers a full range of commercial and personal loans, including fixed-rate consumer mortgage loans, variable rate home equity lines of credit and fixed rate home equity loans, commercial lines of credit, commercial mortgage loans, and real estate construction loans. Other banking services include safe deposit boxes, direct deposit of payroll and social security checks, Internet banking with bill pay service, mobile banking, ATM services, Visa debit cards, Visa gift cards, and Visa credit cards issued through a third-party provider.

APPLICATION OF CRITICAL ACCOUNTING POLICIES

The Bank’s consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America and follow general practices within the industry in which the Bank operates. Application of these principles requires management to make estimates, assumptions, and judgments that affect the amounts reported in the consolidated financial statements and accompanying notes. These estimates, assumptions, and judgments are based on information available as of the date of the consolidated financial statements; accordingly, as this information changes, the consolidated financial statements could reflect different estimates, assumptions, and judgments. Certain policies inherently have a greater reliance on the use of estimates, assumptions, and judgments and as such have a greater possibility of producing results that could be materially different than originally reported. Estimates, assumptions, and judgments are necessary when assets and liabilities are required to be recorded at fair value, when a decline in the value of an asset not carried on the consolidated financial statements at fair value warrants an impairment write-down or valuation reserve to be established, or when an asset or liability needs to be recorded contingent upon a future event. Carrying assets and liabilities

at fair value inherently results in more financial statement volatility. The fair values and information used to record valuation adjustments for certain assets and liabilities are based on quoted market prices or are provided by other third-party sources, whenever available.

The most significant accounting policies followed by the Bank are presented in Note 1 to the consolidated financial statements appearing elsewhere in this report. These policies, along with the disclosures presented in the other notes to the consolidated financial statements and in this financial review, provide information on how significant assets and liabilities are valued in the consolidated financial statements and how those values are determined. Based on the valuation techniques used and the sensitivity of financial statement amounts to the methods, assumptions, and estimates underlying those amounts, management has identified the determination of the allowance for loan losses as the accounting area that requires the most subjective or complex judgments, and as such may be most subject to revision as new information becomes available.

The allowance for loan losses represents management's estimate of probable loan losses inherent in the loan portfolio. Determining the amount of the allowance for loan losses is considered a critical accounting estimate because it requires significant judgment and the use of estimates related to the amount and timing of expected future cash flows on impaired loans, estimated losses on pools of homogeneous loans based on historical loss experience, and consideration of current economic trends and conditions, all of which may be susceptible to significant change. The loan portfolio also represents the largest asset type on the balance sheets. Note 1 to the consolidated financial statements describes the methodology used to determine the allowance for loan losses.

RESULTS OF OPERATIONS

Summary

For the three-month period ended September 30, 2019, the Bank reported net income of \$900,049, compared to \$850,561 for the same period of 2018, an increase of \$49,488, or 5.8%. Basic and diluted net income per share of common stock for the three-month period ended September 30, 2019 was \$0.63, compared to \$0.60 for the same period in 2018.

For the nine-month period ended September 30, 2019, the Bank reported net income of \$2,591,318, compared to \$2,326,952 for the same period of 2018, an increase of \$264,366, or 11.4%. Basic net income per share of common stock for the nine-month period ended September 30, 2019 was \$1.83, compared to \$1.66 for the same period in 2018. Diluted net income per share of common stock for the nine-month period ended September 30, 2019 was \$1.81, compared to \$1.64 for the same period in 2018.

Annualized return on average assets was 0.94% for the nine-month period ended September 30, 2019, compared to 0.88% for the same period in 2018. Annualized return on average stockholders' equity was 8.43% for the nine-month period ended September 30, 2019, compared to 8.15% for the same period in 2018.

Details of the changes in the various components of net income are discussed below.

Net Interest Income and Net Interest Margin

The primary source of income for the Bank is net interest income, which is the difference between interest earned on interest-earning assets, such as investment securities and loans, and interest paid on interest-bearing sources of funds, such as deposits and borrowings. The level of net interest income is determined primarily by the average balance of interest-earning assets and funding sources and the various rate spreads between the interest-earning assets and the Bank's funding sources. The table below entitled "Average Balances, Interest, and Yields" shows the Bank's average volume of interest-earning assets and interest-bearing liabilities for the three- and nine-month periods ended September 30, 2019 and 2018 and related interest income, interest expense, and yields. Changes in net interest income from period to period result from increases or decreases in the volumes of interest-earning assets and interest-bearing liabilities, and increases or decreases in the average rates earned and paid on such assets and liabilities. The volumes of interest-earning assets and interest-bearing liabilities are affected by management's ability to effectively and efficiently manage the earning-asset portfolio (which includes loans), and the availability of particular sources of funds, such as noninterest-bearing deposits.

Interest income, on a fully taxable equivalent basis, for the three-month period ended September 30, 2019 was \$4,006,907, compared to \$3,780,978 for the same period in 2018, representing an increase of \$225,929, or 6.0%. Interest income, on a fully taxable equivalent basis, for the nine-month period ended September 30, 2019 was \$11,842,689, compared to \$11,079,641 for the same period in 2018, representing an increase of \$763,049, or 6.9%.

Average Balances, Interest, and Yields

	For the three months ended September 30, 2019 Average			For the three months ended September 30, 2018 Average			For the nine months ended September 30, 2019 Average			For the nine months ended September 30, 2018 Average		
	balance	Interest	Yield	balance	Interest	Yield	balance	Interest	Yield	balance	Interest	Yield
Assets												
FRB interest-bearing deposits	\$ 30,100,712	\$ 184,825	2.44%	\$ 14,497,074	\$ 85,164	2.33%	\$ 25,785,258	\$ 484,278	2.51%	\$ 18,262,368	\$ 271,015	1.98%
FHLBA interest-bearing deposits	207,280	1,202	2.30%	104,121	518	1.97%	158,077	2,794	2.36%	78,240	1,043	1.78%
Federal funds sold	343,474	1,765	2.04%	-	-	0.00%	253,367	4,202	2.22%	114,659	1,379	1.61%
Time deposits in other banks	1,000,000	5,765	2.29%	51,630	335	2.57%	426,740	7,779	2.44%	389,194	5,248	1.80%
Other	1,305,700	22,614	6.87%	1,592,200	27,112	6.76%	1,381,872	74,492	7.21%	1,667,056	78,970	6.33%
Investment securities:												
U.S. Treasury securities	4,016,128	28,404	2.81%	3,490,769	14,394	1.64%	3,971,688	84,930	2.86%	3,218,331	37,594	1.56%
U. S. government agency securities	16,665,009	99,557	2.37%	14,040,499	81,292	2.30%	16,122,088	306,270	2.54%	13,285,886	195,456	1.97%
Mortgage-backed securities	13,861,721	77,041	2.21%	11,325,611	56,102	1.97%	11,812,451	193,338	2.19%	11,533,906	174,720	2.03%
SBA asset-backed securities	3,952,143	30,293	3.04%	3,036,153	19,871	2.60%	3,825,050	75,264	2.63%	3,011,665	64,115	2.85%
State and municipal securities	924,631	5,075	2.18%	1,620,853	7,247	1.77%	1,004,486	15,433	2.05%	1,903,072	25,229	1.77%
Total investment securities	39,419,632	240,370	2.42%	33,513,885	178,906	2.12%	36,735,763	675,235	2.46%	32,952,860	497,114	2.02%
Loans:												
Overdrafts	123,906	-	0.00%	75,015	-	0.00%	91,923	-	0.00%	81,429	-	0.00%
Consumer	7,993,885	116,158	5.76%	9,514,638	130,111	5.43%	8,081,937	323,634	5.35%	9,474,276	407,282	5.75%
Credit lines	11,684,497	154,753	5.25%	11,516,142	143,706	4.95%	11,784,529	472,563	5.36%	11,583,961	408,050	4.71%
Commercial	31,990,332	457,003	5.67%	32,096,274	435,456	5.38%	32,832,485	1,408,756	5.74%	31,406,651	1,241,645	5.29%
Real estate	231,345,601	2,822,452	4.84%	229,860,330	2,779,670	4.80%	230,421,298	8,388,957	4.87%	226,597,699	8,167,895	4.82%
Total loans *	283,138,221	3,550,366	4.97%	283,062,399	3,488,943	4.89%	283,212,172	10,593,910	5.00%	279,144,016	10,224,872	4.90%
Allowance for loan losses	(3,105,352)	-	-	(3,047,488)	-	-	(3,076,249)	-	-	(2,908,862)	-	-
Total loans, net of allowance *	280,032,869	3,550,366	5.03%	280,014,911	3,488,943	4.94%	280,135,923	10,593,910	5.06%	276,235,154	10,224,872	4.95%
Total interest-earning assets	352,409,667	4,006,907	4.51%	329,773,821	3,780,978	4.55%	344,877,000	11,842,690	4.59%	329,699,531	11,079,641	4.49%
Noninterest-bearing cash	6,469,351	-	-	7,395,456	-	-	6,519,092	-	-	7,289,043	-	-
Net bank premises and equipment	8,471,512	-	-	7,789,138	-	-	8,413,443	-	-	7,704,767	-	-
Restricted stock	-	-	-	-	-	-	-	-	-	30,989	-	-
Other assets	9,966,422	-	-	8,916,499	-	-	9,913,228	-	-	8,895,836	-	-
Total assets	\$ 377,316,952			\$ 353,874,914			\$ 369,722,763			\$ 353,620,166		
Liabilities and Stockholders' Equity												
Interest-bearing deposits												
NOW deposits	\$ 69,835,667	15,333	0.09%	\$ 64,864,681	12,823	0.08%	\$ 69,166,467	44,767	0.09%	\$ 65,349,149	38,270	0.08%
Savings	38,656,073	13,753	0.14%	38,090,722	10,171	0.11%	38,605,524	40,771	0.14%	37,703,295	26,604	0.09%
Money market	15,589,125	5,786	0.15%	15,661,690	5,763	0.15%	15,875,651	17,411	0.15%	15,664,501	17,172	0.15%
Personal investment	22,123,953	21,283	0.38%	23,162,165	17,887	0.31%	22,379,262	63,790	0.38%	23,440,741	41,428	0.24%
Time deposits	83,349,613	379,337	1.81%	70,402,201	192,136	1.08%	78,627,572	980,011	1.67%	69,872,658	513,193	0.98%
Total interest-bearing deposits	229,554,431	435,492	0.75%	212,181,459	238,780	0.45%	224,654,476	1,146,750	0.68%	212,030,344	636,667	0.40%
Borrowed overnight funds	11	-	0.00%	3,576,436	20,332	2.26%	51,286	1,032	2.69%	1,366,418	22,981	2.25%
FHLBA term borrowings	23,000,000	139,943	2.41%	26,423,913	158,937	2.39%	24,527,473	443,255	2.42%	29,578,755	579,309	2.62%
Total borrowed funds	23,000,011	139,943	2.41%	30,000,349	179,269	2.37%	24,578,759	444,287	2.42%	30,945,173	602,290	2.60%
Total interest-bearing deposits and borrowed funds	252,554,442	575,435	0.90%	242,181,808	418,049	0.68%	249,233,235	1,591,037	0.85%	242,975,517	1,238,957	0.68%
Noninterest-bearing deposits	80,595,308	-	-	71,053,279	-	-	77,116,718	-	-	70,689,244	-	-
Other liabilities	2,324,270	-	-	1,791,793	-	-	2,275,921	-	-	1,771,627	-	-
Stockholders' equity	41,842,932	-	-	38,848,034	-	-	41,096,889	-	-	38,183,778	-	-
Total liabilities and stockholders' equity	\$ 377,316,952			\$ 353,874,914			\$ 369,722,763			\$ 353,620,166		
Net interest spread			3.61%			3.87%			3.74%			3.81%
Net interest income		\$ 3,431,472			\$ 3,362,929			\$ 10,251,653			\$ 9,840,684	
Net margin on interest-earning assets			3.86%			4.05%			3.97%			3.99%

Interest on tax-exempt securities, loans and dividends are reported on fully taxable equivalent basis, and excludes fee income.

* Includes non accrual loans.

Interest income, on a fully taxable equivalent basis, on loans increased by \$61,423, or 1.8%, for the three-month period ended September 30, 2019 when compared to the same period in 2018. Average balances of loans increased slightly by \$17,958 for the three-month period ended September 30, 2019 when compared to the same period in 2018. The weighted average rate earned on loans, on a fully taxable equivalent basis, increased by nine basis points to 5.03% for the three-month period ended September 30, 2019 when compared to the same period in 2018. Interest income, on a fully taxable equivalent basis, on loans increased by \$369,038, or 3.6%, for the nine-month period ended September 30, 2019 when compared to the same period in 2018. Average balances on loans increased by \$3,900,769, or 1.4%, for the nine-month period ended September 30, 2019 when compared to the same period in 2018. The weighted average rate earned on loans, on a fully taxable equivalent basis, increased by 11 basis points to 5.06% for the nine-month period ended September 30, 2019 when compared to the same period in 2018.

Interest income, on a fully taxable equivalent basis, on interest-bearing deposits in the Federal Reserve Bank ("FRB") and the Federal Home Loan Bank of Atlanta ("FHLBA"), federal funds sold, and time deposits in other banks increased by \$107,540, or 125.0%, for

the three-month period ended September 30, 2019 when compared to the same period in 2018. Average balances for these instruments increased by \$16,998,641, or 116.0%, for the three-month period ended September 30, 2019 when compared to the same period in 2018. The weighted average rate earned on these holdings, on a fully taxable equivalent basis, increased by 10 basis points to 2.43% for the three-month period ended September 30, 2019 when compared to the same period in 2018. Interest income, on a fully taxable equivalent basis, for interest-bearing deposits in the FRB and the FHLBA, federal funds sold, and time deposits in other banks increased by \$220,368, or 79.1%, for the nine-month period ended September 30, 2019 when compared to the same period in 2018. Average balances for these instruments increased by \$7,778,981, or 41.3%, for the nine-month period ended September 30, 2019 when compared to the same period in 2018. The weighted average rate earned on these holdings, on a fully taxable equivalent basis, increased by 11 basis points to 2.51% for the nine-month period ended September 30, 2019 when compared to the same period in 2018.

Interest income, on a fully taxable equivalent basis, on investment securities for the three-month period ended September 30, 2019 increased by \$61,464, or 34.4%, when compared to the same period in 2018. Average balances of investment securities for the three-month period ended September 30, 2019 increased by \$5,905,747, or 17.6%, when compared to the same period in 2018. The weighted average rate earned on investment securities, on a fully taxable equivalent basis, increased by 30 basis points to 2.42% for the three-month period ended September 30, 2019 when compared to the same period in 2018. Interest income, on a fully taxable equivalent basis, on investment securities for the nine-month period ended September 30, 2019 increased by \$178,121, or 35.8%, when compared to the same period in 2018. Average balances of investment securities for the nine-month period ended September 30, 2019 increased by \$3,782,903, or 11.5%, when compared to the same period in 2018. The weighted average rate earned on investment securities, on a fully taxable equivalent basis, increased by 44 basis points to 2.46% for the nine-month period ended September 30, 2019 when compared to the same period in 2018.

The Bank is a member of the FHLBA and is required to purchase capital stock of the FHLBA as a condition to obtaining a line of credit. Dividends on FHLBA capital stock may be paid to member banks subject to the discretion of the Board of Directors of the FHLBA. For the three-month period ended September 30, 2019, the Bank recorded dividends received or accrued on stock issued by the FHLBA in the amount of \$22,614 on a fully taxable equivalent basis, compared to \$27,112 for the same period in 2018, a decrease of \$4,498, or 16.6%. The average balance of FHLBA capital stock for the three-month period ended September 30, 2019 decreased by \$286,500, or 18.0%, when compared to the same period in 2018. The weighted average rate earned on FHLBA capital stock, on a fully taxable equivalent basis, increased by 11 basis points to 6.87% for the three-month period ended September 30, 2019 when compared to the same period in 2018. For the nine-month period ended September 30, 2019, the Bank recorded dividends received or accrued on stock issued by the FHLBA in the amount of \$74,492 on a fully taxable equivalent basis, compared to \$78,970 for the same period in 2018, a decrease of \$4,478. The average balance of FHLBA capital stock for the nine-month period ended September 30, 2019 decreased by \$285,184, or 17.1% when compared to the same period in 2018. The weighted average rate earned on FHLBA capital stock, on a fully taxable equivalent basis, increased by 88 basis points to 7.21% for the nine-month period ended September 30, 2019 when compared to the same period in 2018.

Interest expense on interest-bearing deposit liabilities increased by \$196,712, or 82.4%, for the three-month period ended September 30, 2019 when compared to the same period in 2018. The average balance of interest-bearing deposit liabilities increased by \$17,372,972, or 8.2%, to \$229,554,431 for the three-month period ended September 30, 2019 when compared to the same period in 2018. The weighted-average rate paid on these deposits increased by 30 basis points to 0.75% for the three-month period ended September 30, 2019 when compared to the same period of 2018. Interest expense on interest-bearing deposit liabilities increased by \$510,083, or 80.1%, for the nine-month period ended September 30, 2019 when compared to the same period in 2018. The average balance of interest-bearing deposit liabilities increased by \$12,624,132, or 6.0%, to \$224,654,476 for the nine-month period ended September 30, 2019 when compared to the same period in 2018. The weighted-average rate paid on these deposits increased by 28 basis points to 0.68% for the nine-month period ended September 30, 2019 when compared to the same period of 2018.

Interest expense on total borrowed funds decreased by \$39,326, or 21.9%, for the three-month period ended September 30, 2019 when compared to the same period in 2018. The average balance of total borrowed funds decreased by \$7,000,338, or 23.3%, to \$23,000,011 for the three-month period ended September 30, 2019 when compared to the same period in 2018. The weighted-average rate paid on total borrowed funds increased by four basis points to 2.41% for the three-month period ended September 30, 2019 when compared to the same period of 2018. Interest expense on total borrowed funds decreased by \$158,003, or 26.2%, for the nine-month period ended September 30, 2019 when compared to the same period in 2018. The average balance of total borrowed funds decreased by \$6,366,414, or 20.6%, to \$24,578,759 for the nine-month period ended September 30, 2019 when compared to the same period in 2018. The weighted-average rate paid on total borrowed funds decreased by 18 basis points to 2.42% for the nine-month period ended September 30, 2019 when compared to the same period of 2018.

Net interest income, on a fully taxable equivalent basis, for the three-month period ended September 30, 2019 was \$3,431,472, an increase of \$68,543, or 2.0%, when compared to the same period in 2018. Net interest income, on a fully taxable equivalent basis, for the nine-month period ended September 30, 2019 was \$10,251,653, an increase of \$410,969, or 4.2% when compared to the same period in 2018. The key performance measure for net interest income is the “net margin on interest-earning assets,” or annualized net interest income divided by average interest-earning assets. The Bank’s net interest margin, on a fully taxable equivalent basis, decreased by 19

basis points to 3.86% for the three-month period ended September 30, 2019 when compared to the same period in 2018. The Bank's net interest margin, on a fully taxable equivalent basis, decreased by two basis points to 3.97% for the nine-month period ended September 30, 2019 when compared to the same period in 2018. The net interest margin may be adversely affected by increases in competition, volatile interest rates, decreases in loan demand, changes in the mix of earning assets, the Bank's cost of funds where it outpaces the return on the Bank's loans and investment securities, and other unpredictable changes in the marketplace. The "net interest spread" is the rate earned on interest-earning assets less the rate paid on interest-bearing liabilities. The net interest spread decreased by 26 basis points to 3.61% for the three-month period ended September 30, 2019 when compared to the same period in 2018. The net interest spread decreased by seven basis points to 3.74% for the nine-month period ended September 30, 2019 when compared to the same period in 2018.

Provision for Loan Losses

The provision for or recovery of loan losses is determined by management as the amount to be added to or subtracted from, respectively, the allowance for loan losses after net charge-offs (charge-offs less recoveries) have been deducted to bring the allowance for loan losses to a level which, in management's best estimation, is necessary to absorb probable losses inherent in the existing loan portfolio. The Bank recorded provision expense for the three-month period ended September 30, 2019 of \$60,000, compared to provision expense of \$97,500 recorded for the same period of 2018, a decrease of \$37,500. The Bank recorded provision expense of \$90,000 for the nine-month period ended September 30, 2019, compared to provision expense of \$247,500 for the same period of 2018, a decrease of \$157,500. The difference in the amount of the provision for loan losses between the 2019 and 2018 periods resulted from changes in the levels of charge-offs and recoveries, changes in loan volume and mix, management's assessment of the current market conditions and analysis of inherent risk within the loan portfolio.

Noninterest Revenue

Noninterest revenue for the three-month period ended September 30, 2019 was \$384,680, compared to \$305,985 for the same period in 2018, an increase of \$78,695, or 25.7%. The increase was due to increases of \$63,314 in service charges on deposit accounts and \$16,097 in other fees and commissions, partially offset by the decrease of \$716 in earnings on bank owned life insurance for the three-month period ended September 30, 2019 when compared to the same period in 2018. Noninterest revenue for the nine-month period ended September 30, 2019 was \$1,046,787, compared to \$926,931 for the same period in 2018, an increase of \$119,856, or 12.9%. The increase was due to increases of \$68,502 in service charges on deposit accounts and \$52,147 in other fees and commissions, partially offset by the decrease of \$793 in earnings on bank owned life insurance for the nine-month period ended September 30, 2019 when compared to the same period in 2018.

Noninterest Expenses

Noninterest expenses for the three-month period ended September 30, 2019 were \$2,575,322, compared to \$2,471,447 for the same period in 2018, an increase of \$103,875, or 4.2%. The increase in noninterest expenses was mainly attributable to increases in salaries and benefits expense of \$63,933, furniture and equipment expense of \$23,268, director and committee fees of \$19,483, and other operating expenses of \$26,973, partially offset by decreases in FDIC and state assessments of \$25,230 and net expenses, losses and write-downs on repossessed assets and foreclosed real estate of \$25,817 for the three-month period ended September 30, 2019 when compared to the same period in 2018. Noninterest expenses for the nine-month period ended September 30, 2019 were \$7,774,141, compared to \$7,467,912 for the same period in 2018, representing an increase of \$306,229, or 4.1%. The increase in noninterest expenses was mainly attributable to increases in salaries and benefits expense of \$226,363, furniture and equipment expense of \$69,467, professional fees of \$32,825, and other operating expenses of \$88,572, partially offset by decreases in data processing expense of \$28,171, FDIC and state assessments of \$39,835 and other than temporary impairment of restricted stock expense of \$67,500 for the nine-month period ended September 30, 2019 when compared to the same period in 2018.

Income Tax Expense

Income tax expense for the three-month period ended September 30, 2019 was \$299,055, compared to \$292,898 for the same period of 2018, an increase of \$6,157, or 2.1%. The increase was due to higher income before income taxes earned for the three-month period ended September 30, 2019 when compared to the same period of 2018. Income tax expense for the nine-month period ended September 30, 2019 was \$871,957, compared to \$794,581 for the same period of 2018, an increase of \$77,376, or 9.7%. The increase was due to higher income before income taxes earned for the nine-month period ended September 30, 2019 when compared to the same period of 2018. The Bank's effective income tax rate was 25.1% for the nine-month period ended September 30, 2019, compared to 25.5% for the same period in 2018.

FINANCIAL CONDITION

Assets

Total assets at September 30, 2019 increased by \$25,158,029, or 6.9%, to \$389,728,693, from \$364,570,664 at December 31, 2018.

The Bank invests excess cash balances in interest-bearing accounts at other banks and federal funds sold to correspondent banks. These balances increased by \$13,832,717, or 68.8%, to \$33,949,226 at September 30, 2019, from \$20,116,509 at December 31, 2018.

The balance of investment securities at September 30, 2019 was \$41,323,908, an increase of \$6,744,433, or 19.5%, when compared to investment securities balances at December 31, 2018.

Loans

Loans, net of the allowance for loan losses, increased by \$5,016,276, or 1.8%, to \$286,967,312 at September 30, 2019, from \$281,951,036 at December 31, 2018. The average net loan portfolio represented 81.2% of average earning assets for the nine-month period ended September 30, 2019, compared to 83.8% for the same period in 2018.

The following table sets forth the major classifications of the Bank's loan portfolio.

	September 30, 2019		December 31, 2018	
	Amount	% of Total	Amount	% of Total
Real estate				
Construction, development and other land	\$ 9,317,451	3.21%	\$ 9,213,018	3.23%
Secured by farmland	6,000,648	2.07%	5,518,635	1.94%
Commercial	172,264,878	59.35%	171,540,843	60.16%
Residential	77,999,467	26.87%	75,051,252	26.32%
Commercial	15,685,916	5.40%	14,498,855	5.09%
Mobile home	4,808,373	1.66%	5,207,992	1.83%
Other consumer	4,081,939	1.41%	3,988,087	1.40%
Overdrafts	84,999	0.03%	105,169	0.03%
Gross loans	290,243,671	100.00%	285,123,851	100.00%
Net deferred (fees) costs	(126,067)		(118,053)	
Allowance for loan losses	(3,150,292)		(3,054,762)	
Net loans	<u>\$ 286,967,312</u>		<u>\$ 281,951,036</u>	
Allowance for loan losses to gross loans	<u>1.09%</u>		<u>1.07%</u>	

Loan Credit Risk Management

The Bank's loan portfolio is subject to varying degrees of credit risk. The Bank seeks to mitigate credit risk through portfolio diversification, limiting exposure to any single industry or customer, collateral protection and strong underwriting criteria. The following discussion provides information and statistics on the overall quality of the Bank's loan portfolio. Notes 1 and 4 to the consolidated financial statements included elsewhere in this report describe the accounting policies related to nonperforming loans and charge-offs, and foreclosed and repossessed assets, and describes the methodologies used to develop the allowance for loan losses. Management believes the policies governing nonperforming loans and charge-offs are consistent with industry and regulatory standards. The amount of the allowance for loan losses and the resulting provision for loan losses are reviewed and approved quarterly by the Board of Directors.

The following table provides a comprehensive view of the allowance for loan losses activity, including the periodic activity of charge-offs and recoveries, allocated by loan class for the nine- and 12-month periods ended September 30, 2019 and December 31, 2018, respectively, and the allocation of allowance for loan losses and the balances of loans that were individually and collectively evaluated for impairment at September 30, 2019 and December 31, 2018.

September 30, 2019	Unallocated	Construction, Development & Other Land	Commercial Real Estate & Farmland	Residential Real Estate	Commercial	Mobile Home	Other Consumer	Overdrafts	Total
Allowance for loan losses:									
Beginning balance	\$ 150,049	\$ 187,984	\$ 1,554,315	\$ 674,601	\$ 232,097	\$ 214,548	\$ 29,675	\$ 11,493	\$ 3,054,762
Charge-offs	-	-	-	(16,118)	-	(30,526)	(4,705)	(11,862)	(63,211)
Recoveries	-	51,458	-	9,000	4,800	1,600	-	1,883	68,741
Provision or (recovery of provision)	11,768	(49,152)	95,662	(8,107)	10,601	9,800	6,254	13,174	90,000
Ending balance	<u>\$ 161,817</u>	<u>\$ 190,290</u>	<u>\$ 1,649,977</u>	<u>\$ 659,376</u>	<u>\$ 247,498</u>	<u>\$ 195,422</u>	<u>\$ 31,224</u>	<u>\$ 14,688</u>	<u>\$ 3,150,292</u>
Allowance balance allocated to loans:									
Individually evaluated									
for impairment	\$ -	\$ -	\$ -	\$ 15,000	\$ 3,746	\$ 6,000	\$ -	\$ -	\$ 24,746
Collectively evaluated									
for impairment	<u>161,817</u>	<u>190,290</u>	<u>1,649,977</u>	<u>644,376</u>	<u>243,752</u>	<u>189,422</u>	<u>31,224</u>	<u>14,688</u>	<u>3,125,546</u>
	<u>\$ 161,817</u>	<u>\$ 190,290</u>	<u>\$ 1,649,977</u>	<u>\$ 659,376</u>	<u>\$ 247,498</u>	<u>\$ 195,422</u>	<u>\$ 31,224</u>	<u>\$ 14,688</u>	<u>\$ 3,150,292</u>
Loan balances:									
Individually evaluated									
for impairment		<u>\$ 256,038</u>	<u>\$ 10,644,303</u>	<u>\$ 1,239,011</u>	<u>\$ 234,148</u>	<u>\$ 72,822</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 12,446,322</u>
Collectively evaluated									
for impairment		<u>\$ 9,061,413</u>	<u>\$ 167,621,223</u>	<u>\$76,760,456</u>	<u>\$ 15,451,768</u>	<u>\$ 4,735,551</u>	<u>\$4,081,939</u>	<u>\$ 84,999</u>	<u>\$ 277,797,349</u>
December 31, 2018									
Allowance for loan losses:									
Beginning balance	\$ 17,238	\$ 145,099	\$ 1,521,854	\$ 541,599	\$ 241,287	\$ 254,547	\$ 12,240	\$ 7,440	\$ 2,741,304
Charge-offs	-	-	-	(62,429)	-	(2,986)	(1,000)	(10,195)	(76,610)
Recoveries	-	104,250	-	12,000	6,700	6,451	2,173	994	132,568
Provision or (recovery of provision)	132,811	(61,365)	32,461	183,431	(15,890)	(43,464)	16,262	13,254	257,500
Ending balance	<u>\$ 150,049</u>	<u>\$ 187,984</u>	<u>\$ 1,554,315</u>	<u>\$ 674,601</u>	<u>\$ 232,097</u>	<u>\$ 214,548</u>	<u>\$ 29,675</u>	<u>\$ 11,493</u>	<u>\$ 3,054,762</u>
Allowance balance allocated to loans:									
Individually evaluated									
for impairment	\$ -	\$ -	\$ 62,705	\$ 40,192	\$ 4,610	\$ 10,000	\$ -	\$ -	\$ 117,507
Collectively evaluated									
for impairment	<u>150,049</u>	<u>187,984</u>	<u>1,491,610</u>	<u>634,409</u>	<u>227,487</u>	<u>204,548</u>	<u>29,675</u>	<u>11,493</u>	<u>2,937,255</u>
	<u>\$ 150,049</u>	<u>\$ 187,984</u>	<u>\$ 1,554,315</u>	<u>\$ 674,601</u>	<u>\$ 232,097</u>	<u>\$ 214,548</u>	<u>\$ 29,675</u>	<u>\$ 11,493</u>	<u>\$ 3,054,762</u>
Loan balances:									
Individually evaluated									
for impairment		<u>\$ 261,379</u>	<u>\$ 9,219,711</u>	<u>\$ 1,545,460</u>	<u>\$ 60,226</u>	<u>\$ 94,289</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 11,181,065</u>
Collectively evaluated									
for impairment		<u>\$ 8,951,639</u>	<u>\$ 167,839,767</u>	<u>\$73,505,792</u>	<u>\$ 14,438,629</u>	<u>\$ 5,113,703</u>	<u>\$3,988,087</u>	<u>\$105,169</u>	<u>\$ 273,942,786</u>

The allowance for loan losses is increased by provisions for loan losses charged to expense and recoveries of loans previously charged-off. The allowance for loan losses is decreased by loan charge-offs and recovery of provision for loan losses expense. Recovery of or provisions for loan losses are made to bring the allowance for loan losses within the range of balances that are considered appropriate based upon the allowance methodology and to reflect losses inherent in the loan portfolio as of the balance sheet date. The allowance for loan losses methodology includes allowance allocations calculated in accordance with Financial Accounting Standards Board Accounting Standards Codification (“ASC”) Topic 310, “Receivables” and allowance allocations calculated in accordance with ASC Topic 450, “Contingencies.” Accordingly, the methodology is based on historical loss experience by loan classification and on specific loss allocations, with adjustments for current events and conditions. Management’s process for determining the appropriate level of the allowance for loan losses is designed to account for credit deterioration as it occurs. The recovery of or provision for loan losses reflects loan quality trends, including the levels of and trends related to non-accrual loans, past due loans, potential problem loans, and net charge-offs or recoveries, among other factors. The recovery of or provision for loan losses also reflect the totality of actions taken on all loans for a particular period. The amount of the recovery of or provision for loan losses reflects not only the necessary decreases or

increases in the allowance for loan losses related to newly identified rated loans, but it also reflects actions taken related to other loans including, among other things, any necessary increases or decreases in required allowances for specific loans or loan pools.

The allowance for loan losses was \$3,150,292 at September 30, 2019, compared to \$3,054,762 at December 31, 2018, an increase of \$95,530, or 3.1%. The increase was due to the provision for loan losses of \$90,000 plus recoveries of amounts previously charged-off of \$68,741, partially offset by amounts charged-off of \$63,211. The ratio of the allowance for loan losses to gross loans at September 30, 2019 was 1.09%, an increase of two basis points when compared to the ratio at December 31, 2018. The allowance level reflects the results of management's assessment of the current market conditions and analysis of inherent risk within the loan portfolio performed during the quarter.

The adequacy of the allowance for loan losses is determined based upon management's estimate of the inherent risks associated with lending activities, estimated fair value of collateral, past experience and present indicators such as loan delinquency trends, nonaccrual loans and current market conditions. Management believes that the allowance is adequate as of September 30, 2019; however, future changes in the composition of the loan portfolio and financial condition of borrowers may result in additions to or subtractions from the allowance. Examination of the loan portfolio and allowance for loan losses by regulatory agencies, auditors and consultants engaged by the Bank may result in the need for additional provisions or reversals of provision based upon information available at the time of examination.

Risk Elements of Loan Portfolio

The following table analyzes the status of loans by loan classification at the dates indicated.

	30-59 Days	60-89 Days	90 Days and Over	Total		Total	Loans over 90 Days and
September 30, 2019	Past Due	Past Due	Past Due	Past Due	Current	Loans	Accruing
Construction, development and other land	\$ -	\$ -	\$ -	\$ -	\$ 9,317,451	\$ 9,317,451	\$ -
Commercial real estate and farmland	-	-	84,177	84,177	178,181,349	178,265,526	-
Residential real estate	48,199	73,933	614,419	736,551	77,262,916	77,999,467	15,689
Commercial	-	-	-	-	15,685,916	15,685,916	-
Mobile homes	194,592	10,739	-	205,331	4,603,042	4,808,373	-
Other consumer and overdrafts	12,602	-	-	12,602	4,154,336	4,166,938	-
Total	<u>\$ 255,393</u>	<u>\$ 84,672</u>	<u>\$ 698,596</u>	<u>\$ 1,038,661</u>	<u>\$ 289,205,010</u>	<u>\$ 290,243,671</u>	<u>\$ 15,689</u>
December 31, 2018							
Construction, development and other land	\$ -	\$ -	\$ -	\$ -	\$ 9,213,018	\$ 9,213,018	\$ -
Commercial real estate and farmland	752,236	-	-	752,236	176,307,242	177,059,478	-
Residential real estate	287,479	23,426	130,975	441,880	74,609,372	75,051,252	-
Commercial	-	-	-	-	14,498,855	14,498,855	-
Mobile homes	280,974	3,712	-	284,686	4,923,306	5,207,992	-
Other consumer and overdrafts	8,087	-	-	8,087	4,085,169	4,093,256	-
Total	<u>\$ 1,328,776</u>	<u>\$ 27,138</u>	<u>\$ 130,975</u>	<u>\$ 1,486,889</u>	<u>\$ 283,636,962</u>	<u>\$ 285,123,851</u>	<u>\$ -</u>

The following table summarizes nonaccrual loans and other non-performing assets for the dates indicated.

Non-performing Assets	September 30, 2019	December 31, 2018
Non-accrual loans by class		
Real estate		
Commercial real estate and farmland	\$ 4,783,333	\$ 4,982,468
Residential real estate	672,662	333,731
Mobile home	62,084	76,556
Total non-accrual loans	5,518,079	5,392,755
Foreclosed real estate	-	-
Repossessed assets	-	62,562
Total non-performing assets	\$ 5,518,079	\$ 5,455,317

The significant balances in non-accrual commercial real estate and farmland loans at September 30, 2019 and December 31, 2018 relate primarily to one commercial real estate loan relationship which has demonstrated weakness in its recent operating results. Management conservatively decided to move this credit to non-accrual status in the first quarter of 2018. Payments are being made as agreed and, in management's opinion, the loan relationship is well-collateralized and no specific reserve was needed as of September 30, 2019.

The table below shows troubled debt restructured loans by loan classification at the dates indicated.

	September 30, 2019		December 31, 2018	
	Number of Contracts	Outstanding Loan Balance	Number of Contracts	Outstanding Loan Balance
Commercial real estate	5	\$ 4,608,072	6	\$ 5,481,147
Residential real estate	1	127,617	2	469,480
Commercial	-	-	1	60,226
	6	\$ 4,735,689	9	\$ 6,010,853

Further information about the loan portfolio is provided in Note 4 to the consolidated financial statements included elsewhere in this report.

Off-Balance Sheet Arrangements

In the normal course of business, to meet the financing needs of its customers, the Bank is a party to financial instruments with off-balance sheet risk. These financial instruments include commitments to extend credit, lines of credit, and standby letters of credit. The Bank's exposure to credit loss in the event of nonperformance by the other party to these financial instruments is represented by the contractual amount of the instruments. The Bank uses the same credit policies in making commitments and conditional obligations as it does for on-balance sheet instruments. The Bank generally requires collateral or other security to support the financial instruments with credit risk. The amount of collateral or other security is determined based on management's credit evaluation of the counterparty. The Bank evaluates each customer's creditworthiness on a case-by-case basis.

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Letters of credit are conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. Letters of credit and other commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Because many of the letters of credit and commitments are expected to expire without being drawn upon, the total commitment amount does not necessarily represent future cash requirements.

Management does not believe that any of the foregoing arrangements are reasonably likely to have an impact on the Bank's financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources that is material to investors.

Further information about these arrangements is provided in Note 5 to the consolidated financial statements included elsewhere in this report.

Deposit Liabilities

Total deposit liabilities at September 30, 2019 were \$322,190,594, an increase of \$25,450,134, or 8.6%, when compared to total deposit liabilities at December 31, 2018. Interest-bearing deposit liabilities at September 30, 2019 were \$236,030,578, an increase of \$10,028,882, or 4.4%, when compared to December 31, 2018. The Bank utilizes core deposits primarily to fund its earning assets.

During the nine-month period ended September 30, 2019, average deposit liabilities provided funding for approximately 87.5% of average earning assets, compared to 85.8% for the comparable period of 2018.

Certificates of deposit greater than the FDIC deposit insurance limit of \$250,000 at September 30, 2019 were \$22,802,096, compared to \$19,026,274 at December 31, 2018.

Borrowings

The Bank may borrow up to 25% of its reported total assets from the FHLBA through any combination of notes or line of credit advances. The line of credit interest rate is a variable rate set daily by the FHLBA. The notes payable and the line of credit are secured by a floating lien on all of the Bank's eligible residential first mortgage loans, home equity loans and commercial real estate loans.

The following table summarizes the Bank's fixed rate FHLBA advances.

Maturity Date	Interest Rate	Interest Frequency	September 30, 2019	December 31, 2018
March 19, 2019	2.4800%	Monthly	\$ -	\$ 1,000,000
June 20, 2019	2.4020%	Monthly	-	2,000,000
October 31, 2019	1.8200%	Monthly	3,000,000	3,000,000
December 27, 2019	2.1000%	Monthly	1,000,000	1,000,000
March 20, 2020	2.8500%	Quarterly	1,500,000	1,500,000
June 29, 2020	1.7100%	Monthly	2,500,000	2,500,000
September 21, 2020	2.9385%	Quarterly	1,500,000	1,500,000
December 29, 2020	2.2500%	Monthly	1,000,000	1,000,000
March 22, 2021	3.0195%	Quarterly	1,500,000	1,500,000
June 21, 2021	3.0535%	Quarterly	1,500,000	1,500,000
October 29, 2021	2.1300%	Monthly	3,000,000	3,000,000
December 29, 2021	2.3800%	Monthly	1,000,000	1,000,000
March 21, 2022	3.1155%	Quarterly	3,000,000	3,000,000
June 28, 2022	2.0600%	Monthly	2,500,000	2,500,000
			<u>\$ 23,000,000</u>	<u>\$ 26,000,000</u>

Further information about these advances is provided in Note 9 to the consolidated financial statements included elsewhere in this report.

Capital

Total stockholders' equity was \$42,060,504 at September 30, 2019, an increase of \$2,463,025, or 6.2%, when compared to total stockholders' equity at December 31, 2018. The increase was due to earnings in the amount of \$2,591,318 and stock transactions netting \$353,606, partially offset by quarterly dividends declared on outstanding shares of common stock of \$481,899.

On July 2, 2013, the Board of Governors of the Federal Reserve System, along with the FDIC and the Office of the Comptroller of the Currency, approved final rules to implement the Basel III regulatory capital reforms, among other changes required by the Dodd-Frank Wall Street Reform and Consumer Protection Act. The framework requires banking organizations to hold more and higher quality capital, which acts as a financial cushion to absorb losses, taking into account the impact of risk. The approved rules include a new minimum ratio of common equity Tier 1 (CET1) capital to risk-weighted assets of 4.50%. The rule will phase in a common equity Tier 1 capital conservation buffer starting in 2016 which will reach 2.50% of risk-weighted assets when fully implemented as of January 1, 2019. The Bank's ability to pay dividends may be limited depending on the Bank's level of Tier 1 capital conservation buffer. The rules also raise the minimum ratio of Tier 1 capital to risk-weighted assets from 4.00% to 6.00% and include a minimum leverage ratio of 4.00% for all banking institutions. For the largest, most internationally active banking organizations, the rules include a new minimum supplementary leverage ratio that takes into account off-balance sheet exposures. In terms of quality of capital, the final rules emphasize common equity Tier 1 capital and implement strict eligibility criteria for regulatory capital instruments. The rules also improve the methodology for calculating risk-weighted assets to enhance risk sensitivity. The phase-in period for smaller banking organizations including the Bank began in January 2015, and was fully phased-in on January 1, 2019.

The Bank continues to maintain capital at levels in excess of the minimum risk-based capital requirements adopted by the federal banking agencies and was considered to be "well capitalized" as of September 30, 2019. One measure of capital adequacy is the risk-based capital ratio, or the ratio of total capital to risk adjusted assets. Total capital is composed of both core capital (Tier 1) and supplemental capital (Tier 2). Total assets are adjusted for off-balance sheet items, such as letters of credit, and the different degrees of risk among various assets. Regulators require a minimum risk-based capital ratio of 10.50% including the fully phased-in amount of

the capital conservation buffer, with 10.00% being the regulatory minimum for well-capitalized banks. At September 30, 2019, the Bank's risk-based capital ratio was 15.57%.

The CET1 capital ratio, which became effective for the Bank January 1, 2015, is the ratio of CET1 to risk adjusted assets. CET1 capital consists of common stock, surplus and undivided profits. Regulators require a minimum CET1 ratio of 7.00% including the fully phased-in amount of the capital conservation buffer, with 6.50% being the regulatory minimum for well-capitalized banks. At September 30, 2019, the Bank's CET1 ratio was 14.49%.

Tier 1 capital consists of CET1 capital plus certain additional Tier 1 capital instruments. The Tier 1 capital ratio is the ratio of Tier 1 capital to risk adjusted assets. The Bank had no additional Tier 1 capital instruments. Regulators require a minimum Tier 1 capital ratio of 8.50% including the fully phased-in amount of the capital conservation buffer, with 8.00% being the regulatory minimum for well-capitalized banks. At September 30, 2019, the Bank's Tier 1 capital ratio was 14.49%.

Another measure of capital adequacy is the leverage capital ratio, which is calculated by dividing average total assets for the most recent quarter into Tier 1 capital outstanding at the end of the quarter. The regulatory minimum for this ratio is 4.00%, with 5.00% being the regulatory minimum for well-capitalized banks. The Bank's leverage capital ratio as of September 30, 2019 was 11.15%.

Management is not aware of any trends, favorable or unfavorable, that are likely to have a material effect on our financial condition or on our earnings. Further information about these capital standards is provided in Note 14 to the consolidated financial statements included elsewhere in this report.

Liquidity

Liquidity describes the ability of the Bank to meet financial obligations that arise during the normal course of business. Liquidity is primarily needed to meet the borrowing and deposit withdrawal requirements of customers and to fund current and planned expenditures. Liquidity is derived through increased customer deposits, maturities in the investment portfolio, loan repayments and income from earning assets. To the extent that deposits are not adequate to fund customer loan demand, liquidity needs can be met in short-term funds markets. The Bank has arrangements with correspondent banks whereby it has \$3,000,000 available in unsecured federal funds lines of credit, and \$5,000,000 available through a secured credit facility.

The Bank is also a member of the FHLBA, which provides another source of liquidity. The Bank may borrow up to 25% of its reported total assets from the FHLBA through any combination of notes or line of credit advances. The line of credit interest rate is a variable rate set daily by the lender. The notes payable and the line of credit are secured by a floating lien on all of the Bank's eligible residential first mortgage loans, home equity loans and commercial real estate loans. The Bank is required to purchase shares of capital stock in the FHLBA as a condition to obtaining the line of credit. Based on the value of available collateral as of September 30, 2019, the Bank could borrow an additional \$49,471,603 from the FHLBA.

The Bank is eligible to borrow from the FRB Discount Window. This credit line is secured by the Bank's eligible consumer loan portfolio. Based on the value of available collateral as of September 30, 2019, the Bank could borrow \$5,013,822 from the FRB Discount Window.

The Certificate of Deposit Account Registry Service ("CDARS") network is a form of brokered deposit program in which the Bank has been a participant in since June 2005. In addition to providing Bank clients enhanced FDIC insurance coverage, being a participant in CDARS allows the Bank to fund its balance sheet through the One-Way Buy program. This program uses a competitive bid process to allocate funding. Management believes that this arrangement would be a viable source of funding provided that the Bank maintains its well-capitalized status. The Bank may borrow up to 10% of its reported total assets as of September 30, 2019, or \$38,972,869.

Further information about borrowings and available lines of credit is provided in Note 9 to the consolidated financial statements included elsewhere in this report.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

The Bank's principal market risk is the fluctuation of interest rates and the impact such fluctuation would have on the Bank's lending, investing and deposit activities. Management has adopted procedures to evaluate and mitigate this risk. This risk and management's procedures are discussed in detail in Item 7 of Part II of the Bank's Annual Report on Form 10-K for the year ended December 31, 2018 under the caption "Market Risk Management". Management believes that there have been no material changes in the Bank's market risks, or the procedures used to evaluate and mitigate these risks since December 31, 2018. At September 30, 2019, the model simulations projected the following percentage changes in net interest income from the base case (no change in rates) over the next 12 months for the various interest rate change scenarios listed in the table below. Given prevailing interest rates at September 30, 2019, the likelihood that interest rates will decrease by more than 200 basis points in the foreseeable future is considered remote.

	+300	+200	+100	-100	-200	-300
Change in interest rates:	Basis points	Basis points	Basis points	Basis points	Basis points	Basis points
Projected change in net interest income	1.72%	1.57%	0.96%	-3.35%	-4.61%	N/A

Item 4. Controls and Procedures.

The Bank maintains disclosure controls and procedures that are designed to ensure that information required to be disclosed in the Bank's reports filed under the Securities Exchange Act of 1934 with the FDIC, such as this Quarterly Report, is recorded, processed, summarized and reported within the time periods specified in those rules and forms, and that such information is accumulated and communicated to the Bank's management, including its principal executive officer ("PEO") and its principal financial officer ("PFO"), as appropriate, to allow for timely decisions regarding required disclosure. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the control. The design of any system of controls also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions; over time, controls may become inadequate because of changes in conditions, or the degree of compliance with the policies or procedures may deteriorate.

An evaluation of the effectiveness of these disclosure controls as of September 30, 2019 was carried out under the supervision and with the participation of the Bank's management, including the PEO and PFO. Based on that evaluation, the Bank's management, including the PEO and PFO, has concluded that the Bank's disclosure controls and procedures are, in fact, effective at the reasonable assurance level.

During the quarter ended September 30, 2019, there was no change in the Bank's internal control over financial reporting that has materially affected, or is reasonably likely to materially affect, the Bank's internal control over financial reporting.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings

The Bank is party to various legal actions normally associated with a financial institution. In management's opinion, none of these actions is likely to have a material effect on the Bank's financial condition or future results of operations.

Item 1A. Risk Factors.

The risks and uncertainties to which the Bank's financial condition and operations are subject are discussed in detail in Item 1A of Part I of the Bank's Annual Report on Form 10-K for the year ended December 31, 2018. Management does not believe that any material changes in the Bank's risk factors have occurred since these risks were last discussed.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

Section 3(a)(2) of the Securities Act of 1933, as amended (the "Securities Act"), exempts from the definition of "security" any securities issued by a bank, and the FDIC, as the Bank's primary federal regulator, does not require the registration of the Bank's securities prior to offer or sale. From time to time, the Bank sells shares of its common stock pursuant to its dividend reinvestment plan ("DRIP") and upon exercise of options granted under its Director Stock Purchase Plan, Incentive Stock Option Plan, 2004 Director Non-Qualified Stock Option Plan (the "2004 Plan"), 2008 Employee Stock Purchase Plan (the "2008 Employee Plan") and the 2008 Key Employee

Stock Option Plan (the 2008 “Key Employee Plan”). The DRIP and all equity compensation plans other than the 2004 Director Plan, 2008 Employee Plan and the 2008 Key Employee Plan were adopted before the Bank converted from a national banking association into a state chartered bank, and the Office of the Comptroller of the Currency required that the shares issuable under such plans be registered under the Securities Act prior to their offer and sale. The 2004 Plan expired in April 2014, and, on April 9, 2015, the Bank’s Board of Directors adopted the Harford Bank 2015 Director Stock Option Plan (the “2015 Plan”) so that the Bank may continue to incent non-employee directors through the grant of non-qualified stock options. The 2008 Employee Plan and the 2008 Key Employee Plan expired in April 2018, and no further grants may be made under those plans. Granted options remain outstanding and subject to exercise until July 2020 under the 2008 Employee Plan. Granted options remain outstanding and subject to exercise until April 2028 under the 2008 Key Employee Plan.

During the first quarter of 2019, a net total of 3,111 shares of common stock were sold pursuant to the DRIP at \$27.40 per share. During the first quarter of 2019, a total of 997 shares of common stock were issued pursuant to the exercise of options at an average exercise price of \$22.55 per share.

During the second quarter of 2019, a net total of 3,083 shares of common stock were sold pursuant to the DRIP at \$28.10 per share. During the second quarter of 2019, a total of 350 shares of common stock were issued pursuant to the exercise of options at an average exercise price of \$12.16 per share.

During the third quarter of 2019, a net total of 2,647 shares of common stock were sold pursuant to the DRIP at \$28.07 per share. During the third quarter of 2019, a total of 2,005 shares of common stock were issued pursuant to the exercise of options at an average exercise price of \$16.66 per share.

Item 3. Defaults Upon Senior Securities

Not applicable.

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

None.

Item 6. Exhibits

The exhibits filed or furnished herewith are listed in the following Exhibit Index:

<u>Exhibit No.</u>	<u>Description</u>
Exhibit 31.1	Certifications of the Principal Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).
Exhibit 31.2	Certifications of the Principal Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).
Exhibit 32.1	Certification of the Periodic Report pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (furnished herewith).

SIGNATURES

Pursuant to the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

HARFORD BANK

Date: November 6, 2019

/s/ Michael F. Allen
Michael F. Allen
President
(Principal Executive Officer)

Date: November 6, 2019

/s/ Neil L. Christ, CPA
Neil L. Christ, CPA
Senior Vice President and Chief Financial Officer
(Principal Financial Officer & Principal Accounting Officer)

HARFORD BANK AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CONDITION

At:	September 30, 2019	December 31, 2018
ASSETS	(Unaudited)	
Cash and due from banks	\$ 7,823,972	\$ 9,175,306
Federal Reserve Bank deposit	32,594,538	19,952,251
Federal funds sold and Federal Home Loan Bank deposit	<u>104,688</u>	<u>164,258</u>
Cash and cash equivalents	40,523,198	29,291,815
Time deposits in other banks	1,250,000	-
Investment securities held to maturity at amortized cost (fair value of \$41,564,063 in 2019 and \$34,238,563 in 2018)	41,323,908	34,579,475
Federal Home Loan Bank stock, at cost	1,305,700	1,422,200
Total loans, including deferred fees net of costs	290,117,604	285,005,798
Less: Allowance for loan losses	<u>(3,150,292)</u>	<u>(3,054,762)</u>
Net loans	286,967,312	281,951,036
Bank premises and equipment, net	8,755,728	8,384,835
Income taxes refundable	-	59,558
Accrued interest receivable	918,371	848,717
Deferred income taxes	663,417	663,417
Bank owned life insurance	6,456,335	6,344,418
Other assets	<u>1,564,724</u>	<u>1,025,193</u>
Total assets	<u>\$ 389,728,693</u>	<u>\$ 364,570,664</u>

LIABILITIES AND STOCKHOLDERS' EQUITY

Deposits		
Noninterest-bearing	\$ 86,160,016	\$ 70,738,764
Interest-bearing	<u>236,030,578</u>	<u>226,001,696</u>
Total deposits	322,190,594	296,740,460
Federal Home Loan Bank advances	23,000,000	26,000,000
Accrued interest payable	209,782	134,746
Income taxes payable	11,899	-
Dividend payable	-	239,763
Other liabilities	<u>2,255,914</u>	<u>1,858,216</u>
Total liabilities	<u>347,668,189</u>	<u>324,973,185</u>
Stockholders' equity		
Common stock, par value \$10 per share; authorized 5,000,000 shares; issued and outstanding 1,422,564 shares in 2019, and 1,410,371 shares in 2018	14,225,640	14,103,710
Surplus	16,951,343	16,719,667
Undivided profits	<u>10,883,521</u>	<u>8,774,102</u>
Total stockholders' equity	<u>42,060,504</u>	<u>39,597,479</u>
Total liabilities and stockholders' equity	<u>\$ 389,728,693</u>	<u>\$ 364,570,664</u>

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

HARFORD BANK AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF INCOME (Unaudited)

	For the three months ended September 30,		For the nine months ended September 30,	
	2019	2018	2019	2018
Interest revenue				
Loans, including fees	\$ 3,592,410	\$ 3,547,346	\$ 10,689,171	\$ 10,337,896
Investment securities held to maturity	230,197	171,349	645,551	476,299
Federal funds sold and Federal Home Loan Bank deposit	2,889	483	6,813	2,354
Federal Reserve Bank deposit	172,779	79,613	452,715	253,352
Time deposits in other banks	5,765	335	7,779	5,248
Other	21,141	25,344	69,637	73,822
Total interest revenue	<u>4,025,181</u>	<u>3,824,470</u>	<u>11,871,666</u>	<u>11,148,971</u>
Interest expense				
Deposits	435,492	238,780	1,146,750	636,667
Borrowed funds	139,943	179,269	444,287	602,290
Total interest expense	<u>575,435</u>	<u>418,049</u>	<u>1,591,037</u>	<u>1,238,957</u>
Net interest income	<u>3,449,746</u>	<u>3,406,421</u>	<u>10,280,629</u>	<u>9,910,014</u>
Provision for loan losses	<u>60,000</u>	<u>97,500</u>	<u>90,000</u>	<u>247,500</u>
Net interest income after provision for loan losses	<u>3,389,746</u>	<u>3,308,921</u>	<u>10,190,629</u>	<u>9,662,514</u>
Noninterest revenue				
Service charges on deposit accounts	199,507	136,193	498,333	429,831
Earnings on bank owned life insurance	37,676	38,392	111,917	112,710
Other fees and commissions	147,497	131,400	436,537	384,390
Total noninterest revenue	<u>384,680</u>	<u>305,985</u>	<u>1,046,787</u>	<u>926,931</u>
Noninterest expense				
Salaries and benefits	1,518,635	1,454,702	4,538,445	4,312,082
Occupancy	195,897	178,144	594,648	573,615
Furniture and equipment	129,332	106,064	374,285	304,818
Data processing expense	221,051	226,714	619,314	647,485
Professional fees	57,780	54,236	227,648	194,823
Director and committee fees	74,183	54,700	190,385	188,903
Stationery and supplies	39,821	35,249	134,517	126,514
FDIC and state assessments	10,864	36,094	68,717	108,552
Advertising	46,136	45,077	137,140	138,894
Net expenses, losses and write-downs on repossessed assets and foreclosed real estate	(26,017)	(200)	(4,646)	(390)
Other-than-temporary impairment of restricted stock	-	-	-	67,500
Other operating	307,640	280,667	893,688	805,116
Total noninterest expense	<u>2,575,322</u>	<u>2,471,447</u>	<u>7,774,141</u>	<u>7,467,912</u>
Income before income taxes	<u>1,199,104</u>	<u>1,143,459</u>	<u>3,463,275</u>	<u>3,121,533</u>
Income taxes	<u>299,055</u>	<u>292,898</u>	<u>871,957</u>	<u>794,581</u>
Net income	<u>\$ 900,049</u>	<u>\$ 850,561</u>	<u>\$ 2,591,318</u>	<u>\$ 2,326,952</u>
Basic net income per share	\$ 0.63	\$ 0.60	\$ 1.83	\$ 1.66
Diluted net income per share	\$ 0.63	\$ 0.60	\$ 1.81	\$ 1.64

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

HARFORD BANK AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY (Unaudited)

	Common stock			Undivided	Total
	<u>Shares</u>	<u>Par value</u>	<u>Surplus</u>	<u>profits</u>	<u>Stockholders' Equity</u>
Three months ended:					
September 30, 2019					
Balance at beginning of period	1,417,912	\$ 14,179,120	\$ 16,858,501	\$ 10,224,852	\$ 41,262,473
Net income				900,049	900,049
Cash dividends, \$0.17 per share				(241,380)	(241,380)
Common stock issued:					
Shares issued under stock-based compensation plans and related tax effects	2,005	20,050	13,353	-	33,403
Stock sold and dividend reinvestment plan (DRIP)	2,647	26,470	47,836	-	74,306
Stock-based compensation expense	-	-	31,653	-	31,653
Stock acquired for DRIP administration	-	-	-	-	-
Balance at end of period	<u>1,422,564</u>	<u>\$ 14,225,640</u>	<u>\$ 16,951,343</u>	<u>\$ 10,883,521</u>	<u>\$ 42,060,504</u>
September 30, 2018					
Balance at beginning of period	1,403,879	\$ 14,038,790	\$ 16,590,262	\$ 7,539,454	\$ 38,168,506
Net income				850,561	850,561
Cash dividends, \$0.17 per share				(239,256)	(239,256)
Common stock issued:					
Shares issued under stock-based compensation plans and related tax effects	233	2,330	2,674	-	5,004
Stock sold and dividend reinvestment plan (DRIP)	3,276	32,760	54,545	-	87,305
Stock-based compensation expense	-	-	11,896	-	11,896
Stock acquired for DRIP administration	-	-	-	-	-
Balance at end of period	<u>1,407,388</u>	<u>\$ 14,073,880</u>	<u>\$ 16,659,377</u>	<u>\$ 8,150,759</u>	<u>\$ 38,884,016</u>
Nine months ended:					
September 30, 2019					
Balance at beginning of period	1,410,371	\$ 14,103,710	\$ 16,719,667	\$ 8,774,102	\$ 39,597,479
Net income				2,591,318	2,591,318
Cash dividends, \$0.34 per share				(481,899)	(481,899)
Common stock issued:					
Shares issued under stock-based compensation plans and related tax effects	3,352	33,520	24,349	-	57,869
Stock sold and dividend reinvestment plan (DRIP)	8,841	88,410	157,769	-	246,179
Stock-based compensation expense	-	-	49,558	-	49,558
Stock acquired for DRIP administration	-	-	-	-	-
Balance at end of period	<u>1,422,564</u>	<u>\$ 14,225,640</u>	<u>\$ 16,951,343</u>	<u>\$ 10,883,521</u>	<u>\$ 42,060,504</u>
September 30, 2018					
Balance at beginning of period	1,395,256	\$ 13,952,560	\$ 16,425,257	\$ 6,511,740	\$ 36,889,557
Net income				2,326,952	2,326,952
Cash dividends, \$0.49 per share				(687,933)	(687,933)
Common stock issued:					
Shares issued under stock-based compensation plans and related tax effects	2,473	24,730	13,987	-	38,717
Stock sold and dividend reinvestment plan (DRIP)	9,659	96,590	157,621	-	254,211
Stock-based compensation expense	-	-	62,512	-	62,512
Stock acquired for DRIP administration	-	-	-	-	-
Balance at end of period	<u>1,407,388</u>	<u>\$ 14,073,880</u>	<u>\$ 16,659,377</u>	<u>\$ 8,150,759</u>	<u>\$ 38,884,016</u>

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

HARFORD BANK AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)

For the nine months ended September 30,	2019	2018
Cash flows from operating activities		
Interest received	\$ 11,731,479	\$ 11,150,260
Fees and commissions received	1,177,142	1,077,248
Interest paid	(1,516,001)	(1,211,787)
Cash paid to suppliers and employees	(7,657,329)	(7,046,661)
Income taxes paid	<u>(800,500)</u>	<u>(959,584)</u>
Net cash provided by (used in) operating activities	<u>2,934,791</u>	<u>3,009,476</u>
Cash flows from investing activities		
Proceeds from maturities of time deposits in other banks	-	750,000
Purchases of time deposits in other banks	(1,250,000)	-
Proceeds from maturities of investment securities	18,082,163	9,389,980
Purchases of investment securities	(24,878,404)	(10,420,657)
Redemption (purchase) of FHLB stock	116,500	112,200
Loans originated, net of principal repayments	(5,114,290)	(10,556,263)
Purchases of bank premises and equipment	<u>(691,897)</u>	<u>(637,154)</u>
Net cash provided by (used in) investing activities	<u>(13,735,928)</u>	<u>(11,361,894)</u>
Cash flows from financing activities		
Net (decrease) increase in time deposits	12,497,247	1,154,657
Net (decrease) increase in other deposits	12,952,887	5,638,935
Net (decrease) increase in borrowed funds	(3,000,000)	(1,989,297)
Dividends paid	(721,662)	(671,918)
Dividends reinvested	246,179	254,211
Shares issued under stock-based compensation plans and related tax effects	<u>57,869</u>	<u>38,717</u>
Net cash provided by (used in) financing activities	<u>22,032,520</u>	<u>4,425,305</u>
Net increase (decrease) in cash and cash equivalents	11,231,383	(3,927,113)
Cash and cash equivalents at beginning of period	<u>29,291,815</u>	<u>26,849,569</u>
Cash and cash equivalents at end of period	<u>\$ 40,523,198</u>	<u>\$ 22,922,456</u>

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

HARFORD BANK AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited - continued)

For the nine months ended September 30,	2019	2018
Reconciliation of net income to net cash provided by operating activities		
Net income	\$ 2,591,318	\$ 2,326,952
Adjustments to reconcile net income to net cash provided by operating activities		
Depreciation and amortization	326,036	257,525
Provision for loan losses	90,000	247,500
Amortization of premiums and accretion of discounts, net	51,808	134,383
Loss (gain) on disposition of bank premises and equipment	423	-
Other-than-temporary impairment on restricted stock	-	67,500
Stock-based compensation expense	49,558	62,512
Decrease (increase) in:		
Deferred loan fees and costs	8,014	84,484
Cash surrender value of BOLI	(111,917)	(112,710)
Accrued interest receivable	(69,654)	(67,261)
Income taxes receivable	59,558	(5,169)
Other assets	(544,986)	(54,042)
Increase (decrease) in:		
Accrued interest payable	75,036	27,170
Income taxes payable	11,899	(159,834)
Other liabilities	397,698	200,466
Net cash provided by (used in) operating activities	<u>\$ 2,934,791</u>	<u>\$ 3,009,476</u>

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

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements (Unaudited)

1. Summary of Significant Accounting Policies

Nature of operations

Harford Bank (the “Bank”) provides a full range of banking services to customers located in Harford and Cecil Counties and surrounding areas of northeastern Maryland.

Basis of presentation

The accounting and reporting policies reflected in the consolidated financial statements conform to accounting principles generally accepted in the United States of America and to general practices within the banking industry, and, in the opinion of management, the consolidated financial statements reflect all adjustments necessary for a fair presentation of the Bank's financial position and results of operations. Management has evaluated subsequent events for potential recognition and/or disclosure through the date of issuance of the consolidated financial statements.

Principles of consolidation

The consolidated financial statements include the accounts of Harford Bank and its subsidiary, HB Trust, a Maryland statutory trust. Intercompany accounts and entries have been eliminated in the consolidated financial statements.

Use of estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements. These estimates and assumptions may affect the reported amounts of revenue and expenses during the reporting period. Actual results could differ from these estimates.

Reclassifications

Certain reclassifications have been made to the 2018 consolidated financial statement presentation to conform to the current year's format. Total equity and net income are unchanged due to these reclassifications.

Cash and cash equivalents

For purposes of reporting cash flows, cash and cash equivalents include cash on hand, amounts due from banks, deposits with other financial institutions that have an initial maturity of less than 90 days when acquired, and federal funds sold. Generally, federal funds are purchased and sold for one-day periods.

Time deposits in other banks

Negotiable time deposits in other banks are carried at cost and are placed in amounts of \$250,000 or less to qualify for Federal Deposit Insurance Corporation (“FDIC”) deposit insurance coverage. Non-negotiable time deposits placed with correspondent banks may exceed the \$250,000 limit.

Investment securities

Management has classified all investment securities as held to maturity. Management has the intent and ability to hold all investment securities to maturity. These investment securities are recorded at amortized cost which is cost adjusted for amortization of premiums and accretion of discounts to maturity. Premiums and discounts are recognized in interest revenue using the interest method over the term of the securities, except that premiums on callable securities are amortized to the call price at the first call date.

Credit declines in the fair value of individual held to maturity investment securities below their amortized cost that are determined to be other than temporary result in write-downs of the individual securities to their fair value. The related write downs are included in earnings as realized losses. Factors that management considers in determining if other than temporary impairment has been incurred include the length of time and the extent to which the fair value has been less than amortized cost, the financial condition and prospects of the issuer, and the intent and ability of the Bank to hold the investment securities for a period of time sufficient to allow for recovery in fair value.

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements (Unaudited)

1. Summary of Significant Accounting Policies - continued

Restricted equity securities

As a member of the Federal Home Loan Bank of Atlanta ("FHLB"), the Bank is required to hold FHLB stock as a condition of membership as well as in relation to the Bank's use of products and services. FHLB stock is not publicly-traded and is sold and redeemed by the FHLB at par. The Bank views its investment in FHLB stock as a long-term investment and as a restricted equity security, which is carried at cost, because there is a minimal market for the stock. Therefore, when evaluating FHLB stock for impairment, its value is based on the ultimate recoverability of the par value rather than by recognizing temporary declines in value. The Bank does not consider this investment to be other-than-temporarily impaired at September 30, 2019, and no impairment has been recognized.

The Bank owns stock in an area banker's bank. This stock is not publicly-traded and there is a minimal market for the stock. The Bank views this stock as a long-term investment and as a restricted equity security, which is carried at cost adjusted for other-than-temporary impairment, and grouped with other assets. As a result of impairment assessments conducted in previous years, the carrying value of the restricted stock was reduced to \$0 as of June 30, 2018.

Loans and allowance for loan losses

Loans are stated at unpaid principal balance adjusted for any amounts partially charged-off, the allowance for loan losses, and deferred origination fees and costs.

Interest on loans is accrued based on the principal amounts outstanding. Origination fees and costs are recognized as an adjustment to the related loan yield using an approximate interest method. The accrual of interest is discontinued when any portion of the principal or interest is 90 days past due and collateral is insufficient to discharge the debt in full. Past due status is based on the contractual terms of the loan. If collection of loan principal is evaluated as doubtful, all payments are applied to principal.

Loans are considered impaired when, based on current information, management considers it unlikely that the collection of principal and interest payments will be made according to contractual terms. Generally, loans are reviewed for impairment when rated 4, Special Mention, or 5, Substandard, when 60 or more days past due, when the accrual of interest has been discontinued, and when the loan has been restructured in a troubled debt restructuring (a "TDR"). A TDR is the restructuring of a loan in which a concession is granted to a borrower experiencing financial difficulty.

The allowance for loan losses represents an amount which, in management's judgment, will be adequate to absorb losses inherent in the loan portfolio. Management's judgment in determining the adequacy of the allowance is based on evaluations of the collectability of loans. These evaluations take into consideration such factors as changes in the nature and volume of the loan portfolio, current economic conditions that may affect the borrower's ability to pay, overall portfolio quality, and review of specific problem areas. If the economy or real estate market were to suffer a severe downturn, then the estimate for uncollectible accounts would need to be increased. Loan losses are charged against the allowance when management believes the uncollectability of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance.

The allowance consists of specific, general and unallocated components. The specific component relates to loans that are individually evaluated for impairment and for which impairment is determined to exist. The general component covers the remaining loan portfolio and is based on historical loss experience adjusted for qualitative factors. An unallocated component may be maintained to cover uncertainties that could affect management's estimate of probable losses. The unallocated component of the allowance reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating specific and general losses in the portfolio. Allocation of a portion of the allowance to one category of loans does not preclude its availability to absorb losses in other categories.

Bank premises and equipment

Land is carried at cost. Buildings and improvements, and furniture and equipment are recorded at cost, less accumulated depreciation computed principally by the straight-line method over the estimated useful lives of the assets. Leasehold improvements are generally depreciated over the lesser of the term of the respective leases or the estimated useful lives of the improvements. Software is recorded in other assets at cost and amortized by the straight-line method over three years.

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements (Unaudited)

1. Summary of Significant Accounting Policies - continued

Leases

The Bank leases certain branch facilities under operating leases. The Bank recognizes a liability to make lease payments during the lease term as a lease liability recorded in other liabilities, and the asset representing the right to use the underlying asset during the lease term as a right-of-use lease asset recorded in other assets. The lease liability is measured at the present value of the remaining lease payments, discounted at the Bank's incremental borrowing rate. The right-to-use lease asset is recorded at amount of the lease liability adjusted for any lease incentives. The right-to-use lease asset is amortized and the lease liability is accreted over the remaining lease term.

Other real estate owned

Real estate acquired through foreclosure or by deed in lieu of foreclosure is recorded on the date acquired at the lower of cost or fair value less estimated costs to sell. Losses incurred at the time of acquisition of the property are charged to the allowance for loan losses. Subsequent reductions in the estimated value of the property are included in noninterest expense.

Other repossessed assets

Loan collateral other than real estate acquired through or in lieu of foreclosure is recorded in other assets on the date acquired at the lower of cost or fair value less estimated costs to sell. Losses incurred at the time of acquisition of the collateral are charged to the allowance for loan losses. Subsequent reductions in the estimated value of the collateral are included in noninterest expense.

Income taxes

The provision for income taxes includes taxes payable for the current year and deferred income taxes. Deferred tax assets and liabilities are determined based on the difference between the financial statement and tax bases of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to reverse. Interest and penalties incurred related to income taxes are included in income tax expense.

Management considers the likelihood of changes by taxing authorities in its filed income tax returns and recognizes a liability for or discloses potential changes that management believes are more likely than not to occur upon examination by tax authorities. Management has not identified any uncertain tax positions in filed income tax returns that require recognition or disclosure in the accompanying financial statements. The Bank's income tax returns for the past three years are subject to examination by tax authorities and may change upon examination.

Advertising costs

Advertising costs are expensed as incurred.

Earnings per common share

Basic earnings per common share is determined by dividing net income by the weighted-average number of shares of common stock outstanding after giving retroactive effect to stock dividends for all periods presented. Diluted earnings per common share is computed using the weighted-average number of common shares determined for the basic earnings per common share computation plus the dilutive effect of common stock equivalents using the treasury stock method.

Stock-based compensation

The Bank accounts for employee and director stock options under the fair value method of accounting using a Black-Scholes valuation model to measure stock based compensation at the date of grant. The Bank accounts for stock-based compensation in accordance with Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") Topic 718, *Stock Compensation* under the modified prospective method. This standard requires public companies to recognize compensation expense related to stock based compensation awards in their income statements over the period during which an individual is required to provide service in exchange for such award.

Segment reporting

FASB ASC Topic 280, *Segment Reporting*, requires reporting of selected information about operating segments in its financial reports issued to stockholders. Management has performed an analysis and determined that the Bank has only one operating segment, which is commercial banking. The Bank's chief operating decision makers use combined results to make operating and strategic decisions and therefore the Bank is not required to disclose any additional segment information.

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements (Unaudited)

2. Cash and Cash Equivalents

The Bank normally carries balances with other banks that exceed the federally insured limit.

Banks are required to carry noninterest-bearing cash reserves at specified percentages of deposit balances. The Bank's normal amount of cash on hand and on deposit with other banks is sufficient to satisfy the reserve requirements.

3. Investment Securities Held to Maturity

The amortized cost and estimated fair value of the investment securities portfolio are shown below. The Bank's mortgage-backed investment security holdings are residential and issued and guaranteed by the Government National Mortgage Association ("GNMA"), the Federal National Mortgage Association ("FNMA"), and the Federal Home Loan Mortgage Corporation ("FHLMC"). The asset-backed investment security holdings are issued and guaranteed by the Small Business Administration ("SBA").

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
September 30, 2019				
U.S. Treasury securities	\$ 3,989,584	\$ 14,292	\$ 1,896	\$ 4,001,980
U.S. government agency securities	15,968,922	57,499	5,868	16,020,553
Mortgage-backed securities	15,846,093	79,245	19,684	15,905,654
Asset-backed securities	4,597,366	113,647	3,385	4,707,628
State and municipal securities	921,943	7,149	844	928,248
	<u>\$ 41,323,908</u>	<u>\$ 271,832</u>	<u>\$ 31,677</u>	<u>\$ 41,564,063</u>
December 31, 2018				
U.S. Treasury securities	\$ 3,937,267	\$ 3,853	\$ -	\$ 3,941,120
U.S. government agency securities	14,855,416	9,571	96,431	14,768,556
Mortgage-backed securities	11,042,717	1,344	252,216	10,791,845
Asset-backed securities	3,501,041	13,313	12,514	3,501,840
State and municipal securities	1,243,034	-	7,832	1,235,202
	<u>\$ 34,579,475</u>	<u>\$ 28,081</u>	<u>\$ 368,993</u>	<u>\$ 34,238,563</u>

Contractual maturities and the amount of pledged investment securities for the respective periods are shown below. Actual maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties. Investment securities are pledged to secure deposits of federal and local governments.

	September 30, 2019		December 31, 2018	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Maturing				
In one year or less	\$ 6,914,443	\$ 6,922,932	\$ 5,594,163	\$ 5,574,609
Over one to five years	13,649,758	13,704,909	14,441,554	14,370,269
Greater than five years	316,248	322,940	-	-
Mortgage-backed and asset-backed securities	<u>20,443,459</u>	<u>20,613,282</u>	<u>14,543,758</u>	<u>14,293,685</u>
	<u>\$ 41,323,908</u>	<u>\$ 41,564,063</u>	<u>\$ 34,579,475</u>	<u>\$ 34,238,563</u>
 Pledged securities	 <u>\$ 19,066,362</u>	 <u>\$ 19,177,022</u>	 <u>\$ 21,698,314</u>	 <u>\$ 21,482,138</u>

Harford Bank and Subsidiary
Notes to Consolidated Financial Statements (Unaudited)

3. Investment Securities Held to Maturity - continued

Investment securities with unrealized losses as of the respective periods are shown below.

	Less than 12 Months		12 Months or Longer		Total	
	Gross		Gross		Gross	
	Fair	Unrealized	Fair	Unrealized	Fair	Unrealized
	Value	Losses	Value	Losses	Value	Losses
September 30, 2019						
U.S. Treasury securities	\$ 1,008,910	\$ 1,896	\$ -	\$ -	\$ 1,008,910	\$ 1,896
U.S. government agency securities	1,993,850	4,578	1,498,565	1,290	3,492,415	5,868
Mortgage-backed securities	3,635,422	9,793	1,554,294	9,891	5,189,716	19,684
Asset-backed securities	507,780	3,385	-	-	507,780	3,385
State and municipal securities	-	-	403,004	844	403,004	844
	<u>\$ 7,145,962</u>	<u>\$ 19,652</u>	<u>\$ 3,455,863</u>	<u>\$ 12,025</u>	<u>\$ 10,601,825</u>	<u>\$ 31,677</u>
December 31, 2018						
U.S. Treasury securities	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
U.S. government agency securities	3,483,910	8,268	6,408,030	88,163	9,891,940	96,431
Mortgage-backed securities	2,085,562	23,879	7,967,348	228,337	10,052,910	252,216
Asset-backed securities	429,064	5,804	1,360,998	6,710	1,790,062	12,514
State and municipal securities	337,710	1,195	897,493	6,637	1,235,203	7,832
	<u>\$ 6,336,246</u>	<u>\$ 39,146</u>	<u>\$ 16,633,869</u>	<u>\$ 329,847</u>	<u>\$ 22,970,115</u>	<u>\$ 368,993</u>

The investment securities experiencing unrealized losses as of September 30, 2019 are considered to be temporarily impaired. Management has the intent and ability to hold and does not believe they will be required to sell these investment securities until maturity. Unrealized losses are largely due to increases in market interest rates over the yields available at the time the underlying investments were purchased. The fair value is expected to recover as the securities approach their maturity date or if market interest rates for such securities decline. The U.S. government agency securities the Bank owns are issued by FNMA and FHLMC, which the U.S. government has affirmed its commitment to support, and by the Federal Home Loan Bank system and the Federal Farm Credit system, which are government-sponsored enterprises. The mortgage-backed securities owned by the Bank are issued by GNMA, which carry U.S. government guarantees, and FNMA and FHLMC, which the U.S. government has affirmed its commitment to support. The asset-backed securities owned by the Bank are issued by the SBA and carry U.S. government guarantees. The state and municipal securities owned by the Bank are all general obligation bonds, with unlimited and limited taxing authority. Management does not believe that any of the securities are experiencing unrealized losses due to reasons of credit quality, and concludes the unrealized losses detailed in the above table are temporary.

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements (Unaudited)

4. Loans

The Bank makes loans to customers located primarily in Harford and Cecil Counties in Maryland and in the surrounding areas. The performance of the loan portfolio will be influenced by the regional real estate market and economy.

Major classifications of loans are as follows for the periods indicated:

	September 30, 2019	December 31, 2018
Real estate		
Construction, development and other land	\$ 9,317,451	\$ 9,213,018
Secured by farmland	6,000,648	5,518,635
Commercial	172,264,878	171,540,843
Residential	77,999,467	75,051,252
Commercial	15,685,916	14,498,855
Mobile home	4,808,373	5,207,992
Other consumer	4,081,939	3,988,087
Overdrafts	84,999	105,169
Gross loans	290,243,671	285,123,851
Net deferred (fees) costs	(126,067)	(118,053)
Allowance for loan losses	(3,150,292)	(3,054,762)
Net loans	<u>\$ 286,967,312</u>	<u>\$ 281,951,036</u>
Principal balance of pledged loans	<u>\$ 104,639,610</u>	<u>\$ 100,293,409</u>

Substantial portions of the Bank's loans are secured by residential and commercial real estate. Loans secured by commercial real estate and farmland generally involve larger principal amounts and a higher degree of risk than loans secured by residential one- to four-family mortgages. Repayment of loans secured by commercial real estate and farmland is often dependent on the successful operation or management of the properties, making collectability of such loans subject to adverse economic or real estate market conditions. The Bank seeks to mitigate these risks through its underwriting standards which require that loans be qualified on the basis of the property's value and debt service coverage ratios, and additional collateral may be required under certain circumstances. The Bank generally obtains personal guarantees.

The Bank originates one- to four-family residential mortgage loans in amounts typically up to 80% of the lower of the appraised value or purchase price of the property securing the loan. The predominance of the Bank's residential mortgage portfolio consists of fixed rate mortgages with original maturities ranging from 15 to 30 years. Fixed rate lending can expose the Bank to interest rate risk in a rising rate environment.

Construction lending is generally considered to present a higher degree of credit risk than other types of real estate lending. Risks of loss include the accuracy of the borrower's estimate of construction costs, timing, and ultimate completion value, and the borrower's ability to complete the project in a workmanlike manner. These risks may result in a project whose value is insufficient to ensure full repayment.

Commercial loans are generally secured by inventories, equipment and other assets of the business. Personal guarantees of the borrowers are generally required.

The Bank makes mobile home loans in amounts up to 90% of the lower of the purchase price or the National Appraisal Guides value with original maturities of up to 20 years. To mitigate the risk of loss, the Bank makes loans only for mobile homes located in a mobile home park or sited on land owned by the borrower.

Eligible consumer installment loans are pledged to secure borrowing facilities at the Federal Reserve Discount Window. The Bank's eligible residential first mortgage loans, home equity loans and commercial real estate loans are pledged to secure borrowing facilities at the FHLBA.

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements (Unaudited)

4. Loans - continued

The maturity distribution of the loan portfolio is as follows for the periods indicated:

	September 30, 2019	December 31, 2018
<i>Maturing</i>		
In one year or less	\$ 14,456,999	\$ 9,911,221
Over one to three years	13,346,187	15,517,453
Over three to five years	18,344,352	21,107,523
Over five to fifteen years	97,917,364	91,457,678
Over fifteen years	146,178,769	147,129,976
Gross loans	<u>\$ 290,243,671</u>	<u>\$ 285,123,851</u>
Variable rate loans included above	<u>\$ 218,416,692</u>	<u>\$ 213,454,434</u>

The following table analyzes the status of loans for the periods indicated:

	30-59 Days	60-89 Days	90 Days and Over	Total		Gross	Loans over 90 Days and
September 30, 2019	Past Due	Past Due	Past Due	Past Due	Current	Loans	Accruing
Construction, development and other land	\$ -	\$ -	\$ -	\$ -	\$ 9,317,451	\$ 9,317,451	\$ -
Commercial real estate and farmland	-	-	84,177	84,177	178,181,349	178,265,526	-
Residential real estate	48,199	73,933	614,419	736,551	77,262,916	77,999,467	15,689
Commercial	-	-	-	-	15,685,916	15,685,916	-
Mobile homes	194,592	10,739	-	205,331	4,603,042	4,808,373	-
Other consumer and overdrafts	12,602	-	-	12,602	4,154,336	4,166,938	-
Total	<u>\$ 255,393</u>	<u>\$ 84,672</u>	<u>\$ 698,596</u>	<u>\$ 1,038,661</u>	<u>\$ 289,205,010</u>	<u>\$ 290,243,671</u>	<u>\$ 15,689</u>
December 31, 2018							
Construction, development and other land	\$ -	\$ -	\$ -	\$ -	\$ 9,213,018	\$ 9,213,018	\$ -
Commercial real estate and farmland	752,236	-	-	752,236	176,307,242	177,059,478	-
Residential real estate	287,479	23,426	130,975	441,880	74,609,372	75,051,252	-
Commercial	-	-	-	-	14,498,855	14,498,855	-
Mobile homes	280,974	3,712	-	284,686	4,923,306	5,207,992	-
Other consumer and overdrafts	8,087	-	-	8,087	4,085,169	4,093,256	-
Total	<u>\$ 1,328,776</u>	<u>\$ 27,138</u>	<u>\$ 130,975</u>	<u>\$ 1,486,889</u>	<u>\$ 283,636,962</u>	<u>\$ 285,123,851</u>	<u>\$ -</u>

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements (Unaudited)

4. Loans - continued

Credit Quality Indicators. As part of the on-going monitoring of the quality of the Bank's loan portfolio, management tracks certain credit quality indicators.

The Bank does not credit score new loans but does utilize a risk grading system for non-consumer loans. Loans are risk rated on the scale listed below:

Grade 1, 2 and 3A – These grades include “pass grade” loans to borrowers of acceptable credit quality and risk.

Grade 3W – This grade includes loans that are on management's “watch list” and are classified as “Pass Watch”. It is management's intent to utilize this rating on a temporary basis for pass grade borrowers where a significant risk-modifying action is anticipated in the near future.

Grade 4 – This grade is for “Other Assets Especially Mentioned” or “Special Mention” in accordance with regulatory guidelines. This grade is intended to be temporary and includes loans to borrowers whose credit quality has clearly deteriorated and are at risk of further decline unless active measures are taken to correct the situation. This grade may include loans not fully secured where a specific valuation allowance may be warranted.

Grade 5 – This grade includes “Substandard” loans, in accordance with regulatory guidelines, for which accrual of interest may have stopped. This grade includes loans that are past due or not fully secured where a specific valuation allowance may be warranted.

The following table illustrates classified loans for the periods indicated. Classified loans include loans in Risk Grades 3W, 4, and 5.

	Pass Watch Grade 3W	Special Mention Grade 4	Substandard Grade 5	Total
September 30, 2019				
Construction, development and other land	\$ 3,036,668	\$ -	\$ 256,038	\$ 3,292,706
Commercial real estate and farmland	25,774,678	3,786,791	10,635,387	40,196,856
Residential real estate	5,030,294	-	1,239,011	6,269,305
Commercial	1,065,858	83,437	233,168	1,382,463
Mobile home	32,202	-	72,823	105,025
Other consumer	62,116	-	-	62,116
	<u>\$ 35,001,816</u>	<u>\$ 3,870,228</u>	<u>\$ 12,436,427</u>	<u>\$ 51,308,471</u>
December 31, 2018				
Construction, development and other land	\$ 3,902,830	\$ -	\$ 261,379	\$ 4,164,209
Commercial real estate and farmland	21,581,675	3,681,381	9,763,184	35,026,240
Residential real estate	5,969,356	110,421	1,545,460	7,625,237
Commercial	1,216,277	-	60,227	1,276,504
Mobile home	33,497	-	94,289	127,786
Other consumer	271,912	-	-	271,912
	<u>\$ 32,975,547</u>	<u>\$ 3,791,802</u>	<u>\$ 11,724,539</u>	<u>\$ 48,491,888</u>

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements (Unaudited)

4. Loans - continued

The following table presents allowance for loan losses activity allocated by loan class for nine- and 12-month periods ended September 30, 2019 and December 31, 2018, respectively, and the allocation of allowance for loan losses for loans that were individually and collectively evaluated for impairment at September 30, 2019 and December 31, 2018, and the loan balances by loan class for loans that were individually and collectively evaluated for impairment at September 30, 2019 and December 31, 2018.

		Construction, Development & Other Land	Commercial Real Estate & Farmland	Residential Real Estate	Commercial	Mobile Home	Other Consumer	Overdrafts	Total
September 30, 2019	Unallocated								
Allowance for loan losses:									
Beginning balance	\$ 150,049	\$ 187,984	\$ 1,554,315	\$ 674,601	\$ 232,097	\$ 214,548	\$ 29,675	\$ 11,493	\$ 3,054,762
Charge-offs	-	-	-	(16,118)	-	(30,526)	(4,705)	(11,862)	(63,211)
Recoveries	-	51,458	-	9,000	4,800	1,600	-	1,883	68,741
Provision or (recovery of provision)	11,768	(49,152)	95,662	(8,107)	10,601	9,800	6,254	13,174	90,000
Ending balance	<u>\$ 161,817</u>	<u>\$ 190,290</u>	<u>\$ 1,649,977</u>	<u>\$ 659,376</u>	<u>\$ 247,498</u>	<u>\$ 195,422</u>	<u>\$ 31,224</u>	<u>\$ 14,688</u>	<u>\$ 3,150,292</u>
Allowance balance allocated to loans:									
Individually evaluated									
for impairment	\$ -	\$ -	\$ -	\$ 15,000	\$ 3,746	\$ 6,000	\$ -	\$ -	\$ 24,746
Collectively evaluated									
for impairment	<u>161,817</u>	<u>190,290</u>	<u>1,649,977</u>	<u>644,376</u>	<u>243,752</u>	<u>189,422</u>	<u>31,224</u>	<u>14,688</u>	<u>3,125,546</u>
	<u>\$ 161,817</u>	<u>\$ 190,290</u>	<u>\$ 1,649,977</u>	<u>\$ 659,376</u>	<u>\$ 247,498</u>	<u>\$ 195,422</u>	<u>\$ 31,224</u>	<u>\$ 14,688</u>	<u>\$ 3,150,292</u>
Loan balances:									
Individually evaluated									
for impairment		<u>\$ 256,038</u>	<u>\$ 10,644,303</u>	<u>\$ 1,239,011</u>	<u>\$ 234,148</u>	<u>\$ 72,822</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 12,446,322</u>
Collectively evaluated									
for impairment		<u>\$ 9,061,413</u>	<u>\$ 167,621,223</u>	<u>\$76,760,456</u>	<u>\$ 15,451,768</u>	<u>\$ 4,735,551</u>	<u>\$4,081,939</u>	<u>\$ 84,999</u>	<u>\$ 277,797,349</u>
December 31, 2018									
Allowance for loan losses:									
Beginning balance	\$ 17,238	\$ 145,099	\$ 1,521,854	\$ 541,599	\$ 241,287	\$ 254,547	\$ 12,240	\$ 7,440	\$ 2,741,304
Charge-offs	-	-	-	(62,429)	-	(2,986)	(1,000)	(10,195)	(76,610)
Recoveries	-	104,250	-	12,000	6,700	6,451	2,173	994	132,568
Provision or (recovery of provision)	132,811	(61,365)	32,461	183,431	(15,890)	(43,464)	16,262	13,254	257,500
Ending balance	<u>\$ 150,049</u>	<u>\$ 187,984</u>	<u>\$ 1,554,315</u>	<u>\$ 674,601</u>	<u>\$ 232,097</u>	<u>\$ 214,548</u>	<u>\$ 29,675</u>	<u>\$ 11,493</u>	<u>\$ 3,054,762</u>
Allowance balance allocated to loans:									
Individually evaluated									
for impairment	\$ -	\$ -	\$ 62,705	\$ 40,192	\$ 4,610	\$ 10,000	\$ -	\$ -	\$ 117,507
Collectively evaluated									
for impairment	<u>150,049</u>	<u>187,984</u>	<u>1,491,610</u>	<u>634,409</u>	<u>227,487</u>	<u>204,548</u>	<u>29,675</u>	<u>11,493</u>	<u>2,937,255</u>
	<u>\$ 150,049</u>	<u>\$ 187,984</u>	<u>\$ 1,554,315</u>	<u>\$ 674,601</u>	<u>\$ 232,097</u>	<u>\$ 214,548</u>	<u>\$ 29,675</u>	<u>\$ 11,493</u>	<u>\$ 3,054,762</u>
Loan balances:									
Individually evaluated									
for impairment		<u>\$ 261,379</u>	<u>\$ 9,219,711</u>	<u>\$ 1,545,460</u>	<u>\$ 60,226</u>	<u>\$ 94,289</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 11,181,065</u>
Collectively evaluated									
for impairment		<u>\$ 8,951,639</u>	<u>\$ 167,839,767</u>	<u>\$73,505,792</u>	<u>\$ 14,438,629</u>	<u>\$ 5,113,703</u>	<u>\$3,988,087</u>	<u>\$105,169</u>	<u>\$ 273,942,786</u>

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements (Unaudited)

4. Loans - continued

The following table presents the recorded investment, and the current balance of impaired loans segmented by those with and without a related allowance recorded at September 30, 2019 and December 31, 2018. The average recorded investment and interest income recognized is presented for the time during which the loans were impaired within the nine- and 12-month periods then ended.

	Unpaid Principal Balance	Recorded Investment	Related Allowance	Average Recorded Investment	Interest Income Recognized
September 30, 2019					
With no related allowance recorded:					
Construction, development and other land	\$ 256,038	\$ 256,038	\$ -	\$ 258,482	\$ 12,675
Commercial real estate and farmland	11,241,825	10,644,303	-	10,922,093	209,705
Residential real estate	1,216,744	1,014,470	-	989,847	12,193
Commercial	-	-	-	-	-
Mobile home	70,125	54,929	-	58,831	853
Other consumer	-	-	-	-	-
With an allowance recorded:					
Construction, development and other land	-	-	-	-	-
Commercial real estate and farmland	-	-	-	-	-
Residential real estate	224,541	224,541	15,000	232,597	8,818
Commercial	234,148	234,148	3,746	235,626	4,832
Mobile home	22,898	17,893	6,000	19,147	-
Other consumer	-	-	-	-	-
Total:					
Construction, development and other land	256,038	256,038	-	258,482	12,675
Commercial real estate and farmland	11,241,825	10,644,303	-	10,922,093	209,705
Residential real estate	1,441,285	1,239,011	15,000	1,222,444	21,011
Commercial	234,148	234,148	3,746	235,626	4,832
Mobile home	93,023	72,822	6,000	77,978	853
Other consumer	-	-	-	-	-
	<u>\$ 13,266,319</u>	<u>\$ 12,446,322</u>	<u>\$ 24,746</u>	<u>\$ 12,716,623</u>	<u>\$ 249,076</u>
December 31, 2018					
With no related allowance recorded:					
Construction, development and other land	\$ 261,379	\$ 261,379	\$ -	\$ 265,015	\$ 15,810
Commercial real estate and farmland	9,048,587	8,554,709	-	8,803,650	179,275
Residential real estate	1,139,334	966,184	-	939,242	19,545
Commercial	-	-	-	-	-
Mobile home	79,651	67,493	-	75,036	1,625
Other consumer	-	-	-	-	-
With an allowance recorded:					
Construction, development and other land	-	-	-	-	-
Commercial real estate and farmland	665,002	665,002	62,705	690,068	32,234
Residential real estate	579,276	579,276	40,192	599,149	29,621
Commercial	60,226	60,226	4,610	64,379	3,124
Mobile home	50,732	26,796	10,000	31,918	619
Other consumer	-	-	-	-	-
Total:					
Construction, development and other land	261,379	261,379	-	265,015	15,810
Commercial real estate and farmland	9,713,589	9,219,711	62,705	9,493,718	211,509
Residential real estate	1,718,610	1,545,460	40,192	1,538,391	49,166
Commercial	60,226	60,226	4,610	64,379	3,124
Mobile home	130,383	94,289	10,000	106,954	2,244
Other consumer	-	-	-	-	-
	<u>\$ 11,884,187</u>	<u>\$ 11,181,065</u>	<u>\$ 117,507</u>	<u>\$ 11,468,457</u>	<u>\$ 281,853</u>

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements (Unaudited)

4. Loans - continued

Under a TDR, the Bank has granted a concession that it would not otherwise make to a borrower who has experienced financial difficulty. At the time of the restructuring, the borrower is expected to pay the amounts due under the renegotiated terms.

The table below shows trouble debt restructured loans outstanding by classification included in impaired loans at the respective dates. The Bank is committed to lend additional funds under a line of credit arrangement to one borrower who has received a TDR.

	September 30, 2019		December 31, 2018	
	Number of Contracts	Outstanding Loan Balance	Number of Contracts	Outstanding Loan Balance
Commercial real estate	5	\$ 4,608,072	6	\$ 5,481,147
Residential real estate	1	127,617	2	469,480
Commercial	-	-	1	60,226
	<u>6</u>	<u>\$ 4,735,689</u>	<u>9</u>	<u>\$ 6,010,853</u>

The Bank did not modify or remodify any loans during the nine-month period ended September 30, 2019 or during the 12-month period ended December 31, 2018.

There were no loans that the Bank modified in the 12 months preceding the period ended September 30, 2019 for which there was a payment default during the nine-month period ended September 30, 2019. There were no loans that the Bank modified in the 12 months preceding the period ended December 31, 2018 for which there was a payment default during the 12-month period ended December 31, 2018. Payment default is defined as any time the loan was more than 60 days past due.

The following table summarizes nonaccrual loans and other non-performing assets at September 30, 2019 and December 31, 2018, and the amount of gross interest income that would have been recorded during the nine-month periods ended September 30, 2019 and 2018 had the nonaccrual loans been current and performing according to terms.

Non-performing Assets	September 30, 2019	December 31, 2018
Non-accrual loans by class		
Real estate		
Commercial real estate and farmland	\$ 4,783,333	\$ 4,982,468
Residential real estate	672,662	333,731
Mobile home	<u>62,084</u>	<u>76,556</u>
Total non-accrual loans	<u>5,518,079</u>	<u>5,392,755</u>
Foreclosed real estate	-	-
Reposessed assets	-	62,562
Total non-performing assets	<u>\$ 5,518,079</u>	<u>\$ 5,455,317</u>

Year to Date Through:

	September 30, 2019	September 30, 2018
Interest not accrued on non-accrual loans	<u>\$ 153,151</u>	<u>\$ 142,991</u>

There were three consumer mortgage loans secured by residential real estate with a recorded investment totaling \$306,567 that were in the process of foreclosure as of September 30, 2019.

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements (Unaudited)

5. Credit Commitments

The table below shows outstanding loan commitments, unused lines of credit, and letters of credit.

At:	September 30, 2019	December 31, 2018
Commitments to extend credit		
Loan origination commitments	\$ 24,068,100	\$ 7,227,700
Unused consumer real estate construction	36,000	229,237
Unused home equity lines of credit	11,039,500	10,540,769
Unused overdraft lines of credit	5,155,040	4,929,704
Unused commercial lines of credit	33,881,227	30,146,368
	<u>\$ 74,179,867</u>	<u>\$ 53,073,778</u>
Letters of credit	<u>\$ 3,430,602</u>	<u>\$ 2,200,485</u>

Loan commitments and lines of credit are agreements to lend to a customer as long as there is no violation of any condition to the contract. Loan commitments generally have variable interest rates, fixed expiration dates, and may require payment of a fee. Lines of credit generally have variable interest rates. Such lines do not represent future cash requirements because it is unlikely that all customers will draw upon their lines in full at any time. Letters of credit are commitments issued to guarantee the performance of a customer to a third party.

The Bank's exposure to credit loss in the event of nonperformance by the customer is the contractual amount of the commitment. Loan commitments, lines of credit, and letters of credit are made on the same terms, including collateral, as outstanding loans. Management is not aware of any accounting loss to be incurred by funding these commitments.

6. Related Party Transactions

In the normal course of business, the Bank's executive officers and directors enter into loan transactions with the Bank. Loans to these related parties are made on the same terms, including interest rates and collateral, as those prevailing at the time for comparable loans with borrowers who are not related to the Bank. The following table shows the activity in related party loans for the periods indicated.

Year to Date Through:	September 30, 2019	December 31, 2018
Beginning balance	\$ 16,425,113	\$ 16,461,100
Advances	4,417,184	6,169,206
Change in related party	(12,353)	(8,743)
Transfer to unrelated party	-	(804,918)
Payments	(3,730,650)	(5,391,532)
Ending balance	<u>\$ 17,099,294</u>	<u>\$ 16,425,113</u>

For 2019, the change in related party was due to the retirement of a related party that occurred in May 2019. For 2018, the change in related party was due to a resignation of a related party that occurred in July 2018 and the transfer to unrelated party relates to the sale of a related party's real estate interest that occurred in June 2018.

In addition to the outstanding balances listed above, the Bank's related parties had \$1,490,809 in unused loans committed but not funded as of September 30, 2019. As of December 31, 2018, the Bank's related parties had \$2,735,275 in unused loans committed but not funded.

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements (Unaudited)

6. Related Party Transactions (continued)

The Bank obtains goods and services from firms of which owners are also members of the Bank's Board of Directors. Prices paid for these goods and fees charged for these services are at rates for similar materials and work that are substantially similar to prices and fees charged by persons who are not related to the Bank. The Bank paid \$6,622 to these related parties during the nine months ended September 30, 2019. The Bank paid \$6,513 to these related parties during the nine months ended September 30, 2018.

Deposits of executive officers and directors of the Bank totaled \$3,300,316 at September 30, 2019. Deposits of executive officers and directors of the Bank totaled \$4,966,412 at December 31, 2018.

7. Bank Premises and Equipment

Bank premises and equipment and the related depreciation are as follows:

	Useful Lives	September 30, 2019	December 31, 2018
Land		\$ 3,174,756	\$ 3,174,756
Building and improvements	15 - 39 years	7,386,594	7,155,296
Leasehold improvements	10 - 19 years	518,660	518,660
Furniture, fixtures, and equipment	3 - 10 years	2,460,816	2,159,686
		<u>13,540,826</u>	<u>13,008,398</u>
Accumulated depreciation		<u>4,785,098</u>	<u>4,623,563</u>
Net bank premises and equipment		<u>\$ 8,755,728</u>	<u>\$ 8,384,835</u>

Year to Date Through:

	September 30, 2019	September 30, 2018
Depreciation expense	<u>\$ 320,581</u>	<u>\$ 256,110</u>

Computer software included in other assets and the related amortization are as follows:

	Useful Life	September 30, 2019	December 31, 2018
Computer software	3 years	\$ 280,195	\$ 280,195
Accumulated amortization		<u>266,032</u>	<u>260,577</u>
Net computer software		<u>\$ 14,163</u>	<u>\$ 19,618</u>

Year to Date Through:

	September 30, 2019	September 30, 2018
Amortization expense	<u>\$ 5,455</u>	<u>\$ 1,415</u>

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements (Unaudited)

8. Leases

The Bank leases certain banking facilities under operating leases expiring on various dates through 2026. At September 30, 2019, the Bank had lease liabilities totaling \$382,541 included in other liabilities and right-of-use lease assets totaling \$382,541 included in other assets related to these leases. The right-of-use asset is amortized and the operating lease liability is accreted over the applicable lease terms.

The weighted-average discount rate on operating lease balances outstanding at September 30, 2019 was 2.89%. The weighted-average remaining lease term of operating leases outstanding at September 30, 2019 was 5.5 years.

Rent expense, consisting of lease payments plus common area maintenance and all other charges assessed by the lessor, paid in cash for the nine months ended September 30, 2019 was \$102,357. Rent expense, consisting of lease payments plus common area maintenance and all other charges assessed by the lessor, paid in cash for the nine months ended September 30, 2018 was \$97,511.

As of September 30, 2019, future minimum payments, by year and in the aggregate, of operating leases are as follows:

Year	Amount
Remainder of 2019	\$ 25,404
2020	102,174
2021	88,704
2022	46,529
2023	47,333
2024 and thereafter	<u>125,117</u>
Total undiscounted lease payments	435,261
Discount on cash flows	<u>(52,720)</u>
Total lease liability	<u><u>\$ 382,541</u></u>

9. Borrowings and Available Lines of Credit

FHLBA fixed rate term advances are summarized as follows:

Maturity Date	Interest Rate	Interest Frequency	September 30, 2019	December 31, 2018
March 19, 2019	2.4800%	Monthly	\$ -	\$ 1,000,000
June 20, 2019	2.4020%	Monthly	-	2,000,000
October 31, 2019	1.8200%	Monthly	3,000,000	3,000,000
December 27, 2019	2.1000%	Monthly	1,000,000	1,000,000
March 20, 2020	2.8500%	Quarterly	1,500,000	1,500,000
June 29, 2020	1.7100%	Monthly	2,500,000	2,500,000
September 21, 2020	2.9385%	Quarterly	1,500,000	1,500,000
December 29, 2020	2.2500%	Monthly	1,000,000	1,000,000
March 22, 2021	3.0195%	Quarterly	1,500,000	1,500,000
June 21, 2021	3.0535%	Quarterly	1,500,000	1,500,000
October 29, 2021	2.1300%	Monthly	3,000,000	3,000,000
December 29, 2021	2.3800%	Monthly	1,000,000	1,000,000
March 21, 2022	3.1155%	Quarterly	3,000,000	3,000,000
June 28, 2022	2.0600%	Monthly	2,500,000	2,500,000
			<u>\$ 23,000,000</u>	<u>\$ 26,000,000</u>

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements (Unaudited)

9. Borrowings and Available Lines of Credit (continued)

FHLBA term advances as of September 30, 2019 will require principal repayments as follows:

Year	Principal Reduction
Remainder of 2019	\$ 4,000,000
2020	6,500,000
2021	7,000,000
2022	5,500,000
	<u>\$ 23,000,000</u>

The Bank may borrow up to 25% of its reported total assets from the FHLBA through any combination of notes or line of credit advances. The line of credit interest rate is a variable rate set daily by the lender. The notes payable and the line of credit are secured by a floating lien on all of the Bank's eligible residential first mortgage loans, home equity loans and commercial real estate loans. The Bank is required to purchase shares of capital stock in the FHLB as a condition to obtaining the line of credit. Based on the value of available collateral as of September 30, 2019, the Bank could borrow an additional \$49,471,603 from the FHLBA.

The Bank is eligible to borrow from the Federal Reserve Bank (the "FRB") Discount Window. This credit line is secured by the Bank's eligible consumer loan portfolio. Based on the value of available collateral as of September 30, 2019, the Bank could borrow \$5,013,822 from the FRB Discount Window.

The Certificate of Deposit Account Registry Service ("CDARS") is a form of brokered deposit program in which the Bank has been a participant since June 2005. In addition to offering depositors enhanced FDIC insurance coverage, being a participant in CDARS allows the Bank to fund its balance sheet through their One-Way Buy program. This program uses a competitive bid process to allocate funding. Management believes this arrangement would be a viable source of funding provided that the Bank maintains its well-capitalized status. The Bank may borrow up to 10% of reported total assets as of September 30, 2019, or \$38,972,869.

The Bank has secured and unsecured credit lines with correspondent banks, which are subject to periodic review. Based on the last review performed in the second quarter of 2019, the amount available under the secured line is \$5,000,000 and the amount available under the unsecured line is \$3,000,000.

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements (Unaudited)

10. Retirement Plan

The Bank has a profit sharing plan qualifying under section 401(k) of the Internal Revenue Code. The plan covers all full-time employees with one year of service who have reached 21 years of age. The Bank's discretionary contribution is determined annually by the Board of Directors.

In 2006, and in the second quarter of 2017, the Bank entered into agreements under its Supplemental Executive Retirement Plans ("SERP") with certain executive officers to provide for retirement income benefits. The Bank accrues the present value of these benefits over the remaining number of years to the executives' retirement dates. The Bank has recorded a liability of \$1,156,615 related to these benefits at September 30, 2019. SERP expense for the nine months ended September 30, 2019 was \$120,358. SERP expense for the nine months ended September 30, 2018 was \$113,472.

11. Interest-Bearing Deposits

Major classifications of interest-bearing deposits are as follows:

	September 30, 2019	December 31, 2018
Money market and NOW	\$ 111,641,882	\$ 113,784,049
Savings	39,250,311	39,576,510
Certificates of deposit	85,138,385	72,641,137
	<u>\$ 236,030,578</u>	<u>\$ 226,001,696</u>

Maturities of certificates of deposit are as follows:

	September 30, 2019	December 31, 2018
Maturing within twelve months	\$ 42,650,726	\$ 38,079,239
Maturing over one to three years	29,381,046	23,143,588
Maturing over three to five years	13,106,613	11,418,310
	<u>\$ 85,138,385</u>	<u>\$ 72,641,137</u>

Certificates of deposit over \$250,000 included above:	<u>\$ 22,802,096</u>	<u>\$ 19,026,274</u>
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Interest expense for interest-bearing deposits is as follows:

Year to date through:	September 30, 2019	September 30, 2018
Money market and NOW	\$ 125,970	\$ 96,868
Savings	40,771	26,604
Certificates of deposit	980,009	513,195
	<u>\$ 1,146,750</u>	<u>\$ 636,667</u>

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements (Unaudited)

12. Income Taxes

The components of income tax expense are as follows:

Year to date through:	September 30, 2019	September 30, 2018
Current		
Federal	\$ 669,023	\$ 592,596
State	202,934	201,985
	<u>\$ 871,957</u>	<u>\$ 794,581</u>

The differences between the statutory federal income tax rate in effect during the periods indicated and the effective tax rate for the Bank are reconciled as follows:

Year to date through:	September 30, 2019	September 30, 2018
Statutory federal income tax rate	21.0 %	21.0 %
Increase (decrease) resulting from		
State income taxes, net of federal income tax benefit	4.6	5.1
Tax-exempt income	(0.9)	(1.1)
Nondeductible expenses	0.4	0.5
	<u>25.1 %</u>	<u>25.5 %</u>

13. Stock Option and Stock Purchase Plans

The Bank has adopted stock option plans for directors and officers. Option exercise prices are equal to the fair market value of the stock on the date of grant. Options granted under the director plan fully vest at the time of grant. Options granted under the officer plan vest three years after their grant dates. On April 23, 2018, the officer plan expired, eliminating the Bank's ability to make future grants, although options granted remain outstanding and subject to exercise through April 2028.

The Bank has also adopted a qualified employee stock purchase plan that allows the Bank to grant options to eligible employees to acquire shares of common stock through direct payment or payroll deductions over a maximum 27-month period from the date of the grant. Options granted under the employee stock purchase plan fully vest at the time of grant. On April 23, 2018, the employee plan expired, eliminating the Bank's ability to make future grants, although options granted remain outstanding and subject to exercise through July 2020.

The total number of shares originally authorized for active stock option plans and plans with outstanding options was 276,610. At September 30, 2019, a total of 56,102 shares remain available for grant.

A summary of activity for stock option activity for the nine months ended September 30, 2019 is as follows:

Options	Number of Shares	Exercise Price	Remaining Contractual Term	Intrinsic Value
Outstanding at January 1, 2019	98,396	\$ 22.25		
Options granted	7,260	\$ 28.57		
Options exercised	(4,716)	\$ 20.81		
Options forfeited or expired	(11,882)	\$ 22.27		
Outstanding at September 30, 2019	<u>89,058</u>	<u>\$ 22.84</u>	<u>5.87 years</u>	<u>\$ 504,972</u>
Exercisable at September 30, 2019	<u>71,686</u>	<u>\$ 22.26</u>	<u>5.31 years</u>	<u>\$ 447,559</u>

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements (Unaudited)

13. Stock Option and Stock Purchase Plans - continued

A summary of activity for nonvested stock options for the nine months ended September 30, 2019 is as follows:

Nonvested Options	Number of Shares	Average Grant Date Fair Value
Outstanding at January 1, 2019	24,477	\$ 5.43
Options granted	-	\$ -
Options vested	(6,138)	\$ 6.43
Options forfeited or expired	(967)	\$ 5.69
Outstanding at September 30, 2019	<u>17,372</u>	\$ 5.07

Stock-based compensation expense is recognized ratably over the requisite service period for all awards. The service period generally matches the vesting period. At September 30, 2019, unrecognized stock-based compensation expense related to nonvested stock options will be recognized as follows, by year and in the aggregate:

Year	Stock-Based Compensation Expense
Remainder of 2019	\$ 6,969
2020	20,367
2021	5,001
	<u>\$ 32,337</u>

For the nine months ended September 30, 2019, the Bank recorded stock-based compensation expense of \$49,558. For the nine months ended September 30, 2018, the Bank recorded stock-based compensation expense of \$62,513.

The intrinsic value of options exercised during the nine months ended September 30, 2019 was \$36,730. The intrinsic value of options exercised during the nine months ended September 30, 2018 was \$27,944.

14. Capital Standards

The FRB and the FDIC have adopted risk-based capital standards for banking organizations. These standards require ratios of capital to assets for minimum capital adequacy and to be classified as well capitalized under prompt corrective action provisions.

In July 2013, the Board of Governors of the FRB and the FDIC approved the final rules implementing the Basel Committee on Banking Supervision's capital guidelines for U.S. banks ("Basel III"). Under the final rules, which became effective for the Bank on January 1, 2015 and are subject to a phase-in period through January 1, 2019, minimum requirements will increase for both the quantity and quality of capital held by the Bank. The rules include a new minimum Common Equity Tier 1 capital ratio ("CET1 ratio") of 4.5% and a capital conservation buffer of 2.5% of risk-weighted assets, which when fully phased-in, effectively results in a minimum CET1 ratio of 7.0%. Basel III raises the minimum Tier 1 capital ratio from 4.0% to 6.0% which, with the capital conservation buffer, effectively results in a minimum Tier 1 capital ratio of 8.5% when fully phased-in. Basel III maintains the minimum total capital ratio of 8.0%, which, with the capital conservation buffer, effectively results in a minimum Tier 1 capital ratio of 10.5% when fully phased-in. Basel III maintains the minimum Tier 1 leverage capital ratio of 4.0%, which, with the capital conservation buffer, effectively results in a minimum Tier 1 leverage capital ratio of 6.5% when fully phased-in. Basel III also makes changes to risk weights for certain assets and off-balance sheet exposures.

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements (Unaudited)

14. Capital Standards - continued

Under Basel III, Total capital consists of two tiers of capital, Tier 1 and Tier 2. Tier 1 capital is further composed of Common equity Tier 1 capital and additional Tier 1 capital. For the Bank, Common equity Tier 1 capital consists of common stock, surplus and undivided profits. The Bank has no additional Tier 1 capital items. The Bank's Tier 2 capital consists of a limited amount of the allowance for loan losses. The Bank's Total capital is the sum of Tier 1 capital plus Tier 2 capital.

The Total capital ratio, the Tier 1 capital ratio and the Common equity Tier 1 capital ratio are calculated using end of period risk-weighted assets. In calculating risk-weighted assets, specified risk percentages are applied to each category of asset and off-balance sheet items based on regulatory requirements. The Tier 1 leverage capital ratio is calculated using quarterly average assets.

The Bank's actual capital ratios and required regulatory minimum capital requirements in effect at the time for the periods indicated based on the phase-in provisions of the Basel III Capital Rules and the minimum required capital levels as of January 1, 2019 when the Basel III Capital Rules have been fully phased-in are as follows:

(\$ in thousands)	Actual		Minimum Capital Basel III Phase-In Schedule		Minimum Capital Basel III Fully Phased-In		Required To be Well Capitalized	
			Amount	Ratio	Amount	Ratio	Amount	Ratio
September 30, 2019	Amount	Ratio	Amount	Ratio	Amount	Ratio	Amount	Ratio
Total capital	\$ 45,211	15.57%	\$ 30,487	10.50%	\$ 30,487	10.50%	\$ 29,035	10.00%
Tier 1 capital	42,061	14.49%	24,680	8.50%	24,680	8.50%	23,228	8.00%
Common equity Tier 1 capital	42,061	14.49%	20,325	7.00%	20,325	7.00%	18,873	6.50%
Tier 1 leverage capital	42,061	11.15%	15,093	4.00%	15,093	4.00%	18,866	5.00%
December 31, 2018			Minimum Capital Basel III Phase-In Schedule		Minimum Capital Basel III Fully Phased-In		Required To be Well Capitalized	
			Amount	Ratio	Amount	Ratio	Amount	Ratio
Total capital	\$ 42,652	15.09%	\$ 27,903	9.875%	\$ 29,669	10.50%	\$ 28,256	10.00%
Tier 1 capital	39,597	14.01%	22,251	7.875%	24,017	8.50%	22,605	8.00%
Common equity Tier 1 capital	39,597	14.01%	18,013	6.375%	19,779	7.00%	18,366	6.50%
Tier 1 leverage capital	39,597	10.87%	14,568	4.000%	14,568	4.00%	18,210	5.00%

As of September 30, 2019, capital levels at the Bank exceed all capital adequacy requirements under the Basel III Capital Rules on a fully phased-in basis. Based on the ratios presented above, capital levels of the Bank exceed the minimum levels necessary to be considered well capitalized.

Failure to meet the capital requirements could affect the Bank's ability to pay dividends and accept deposits and may significantly affect the operations of the Bank.

In its most recent regulatory report the Bank was categorized as well capitalized under the prompt corrective action regulations. Management knows of no events or conditions that should change this classification.

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements (Unaudited)

15. Net Income per Common Share

The calculations of basic and diluted net income per common share are presented in the following table.

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2019	2018	2019	2018
Basic:				
Net income	\$ 900,049	\$ 850,561	\$2,591,318	\$2,326,952
Weighted-average common shares outstanding	1,418,822	1,406,288	1,415,516	1,402,407
Basic net income per common share	<u>\$ 0.63</u>	<u>\$ 0.60</u>	<u>\$ 1.83</u>	<u>\$ 1.66</u>
Diluted:				
Net income	\$ 900,049	\$ 850,561	\$2,591,318	\$2,326,952
Weighted-average common shares outstanding	1,418,822	1,406,288	1,415,516	1,402,407
Dilutive common stock equivalents	17,690	22,394	17,464	19,864
Dilutive EPS shares	<u>1,436,512</u>	<u>1,428,682</u>	<u>1,432,980</u>	<u>1,422,271</u>
Diluted net income per common share	<u>\$ 0.63</u>	<u>\$ 0.60</u>	<u>\$ 1.81</u>	<u>\$ 1.64</u>
Anti-dilutive shares	<u>7,260</u>	<u>-</u>	<u>7,260</u>	<u>13,766</u>

16. Fair Value Measurements

FASB ASC Topic 820 defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value. FASB ASC Topic 820 also establishes a hierarchy for determining fair value measurement. The hierarchy includes three levels and is based upon the valuation techniques used to measure assets and liabilities.

The fair value hierarchy is as follows:

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

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

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

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements (Unaudited)

16. Fair Value Measurements - continued

During the nine- and 12-month periods ended September 30, 2019 and December 31, 2018, respectively, the Bank did not measure any assets or liabilities at fair value on a recurring basis. Assets measured at fair value on a nonrecurring basis are as follows:

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
September 30, 2019				
Impaired loans (net of impairment)	\$ -	\$ 12,191,174	\$ 230,401	\$ 12,421,575
Other real estate owned	-	-	-	-
Reposessed assets	-	-	-	-
Total	<u>\$ -</u>	<u>\$ 12,191,174</u>	<u>\$ 230,401</u>	<u>\$ 12,421,575</u>
December 31, 2018				
Impaired loans (net of impairment)	\$ -	\$ 10,077,332	\$ 986,226	\$ 11,063,558
Other real estate owned	-	-	-	-
Reposessed assets	-	62,562	-	62,562
Total	<u>\$ -</u>	<u>\$ 10,139,894</u>	<u>\$ 986,226</u>	<u>\$ 11,126,120</u>

At September 30, 2019, impaired loans totaling \$12,446,322 had specific loan loss allowances of \$24,746 carried in the allowance for loan losses, resulting in a fair value of impaired loans (net of impairment) measured on a nonrecurring basis of \$12,421,575. At December 31, 2018, impaired loans totaling \$11,181,065 had specific loan loss allowances of \$117,507 carried in the allowance for loan losses, resulting in a fair value of impaired loans (net of impairment) measured on a nonrecurring basis of \$11,063,558.

Nonrecurring fair value adjustments to collateral dependent impaired loans through a specific valuation allowance or through charge-off reflect values that are based principally on the collateral's observable market price or current appraised value of the collateral less estimated selling costs. Fair value adjustments based principally on the appraised value of the collateral less costs to sell are classified as Level 2.

Nonrecurring fair value adjustments to non-collateral dependent impaired loans through a specific valuation allowance reflect values based on the present value of expected cash flows. Since present value calculation techniques do not utilize quoted prices in active markets or significant other observable market inputs in measuring fair value, non-collateral dependent loan fair values are classified as Level 3.

Nonrecurring fair value adjustments to foreclosed real estate owned reflect values that are based principally on the real estate's observable market price or current appraised value of the collateral. Fair value adjustments based principally on the observable market price or appraised value of the collateral less costs to sell are classified as Level 2.

Nonrecurring fair value adjustments to reposessed assets reflect values that are based principally on the collateral's observable market price or current National Appraisal Guides value of the collateral. Fair value adjustments based principally on the observable market price or appraised value of the collateral less costs to sell are classified as Level 2.

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements (Unaudited)

16. Fair Value Measurements - continued

The estimated fair value of the Bank's financial instruments equals the carrying value of the instruments except as follows. In estimating fair values, the Bank utilizes valuation techniques that are consistent with the market approach, the income approach and/or the cost approach. Such valuation techniques are consistently applied. Inputs to valuation techniques include the assumptions that market participants would use in pricing an asset or liability. Also, the calculation of estimated fair values is based on market conditions at a specific point in time and may not reflect current or future fair values.

	Carrying Amount	Estimated Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
September 30, 2019					
Financial assets:					
Time deposits in other banks	\$ 1,250,000	\$ 1,266,291	\$ -	\$ -	\$ 1,266,291
Investment securities held to maturity					
U.S. Treasury securities	3,989,584	4,001,980	-	4,001,980	-
U.S. government agencies	15,968,922	16,020,553	-	16,020,553	-
Mortgage-backed securities	15,846,093	15,905,654	-	15,905,654	-
Asset-backed securities	4,597,366	4,707,628	-	4,707,628	-
State and municipal securities	921,943	928,248	-	928,248	-
Loans, net	286,967,312	286,655,337	-	12,191,174	274,464,163
Bank owned life insurance	6,456,335	6,456,335	-	6,456,335	-
Financial liabilities:					
Interest-bearing deposits	236,030,578	236,952,529	-	-	236,952,529
FHLB advances	23,000,000	23,238,701	-	-	23,238,701
December 31, 2018					
Financial assets:					
Time deposits in other banks	\$ -	\$ -	\$ -	\$ -	\$ -
Investment securities held to maturity					
U.S. Treasury securities	3,937,267	3,941,120	-	3,941,120	-
U.S. government agencies	14,855,416	14,768,556	-	14,768,556	-
Mortgage-backed securities	11,042,717	10,791,845	-	10,791,845	-
Asset-backed securities	3,501,041	3,501,840	-	3,501,840	-
State and municipal securities	1,243,034	1,235,202	-	1,235,202	-
Loans, net	281,951,036	280,861,798	-	10,077,332	270,784,466
Bank owned life insurance	6,344,418	6,344,418	-	6,344,418	-
Financial liabilities:					
Interest-bearing deposits	226,001,696	225,229,568	-	-	225,229,568
FHLB advances	26,000,000	25,873,360	-	-	25,873,360

Time deposits in other banks

The fair value of non-negotiable time deposits in correspondent banks is estimated based on interest rates currently offered for deposits of similar remaining maturities, as there is no demonstrable market for non-negotiable time deposits.

Investment securities held to maturity

The fair value of investment securities held to maturity is estimated based on quoted market prices, when available. If quoted market prices are not available, fair values are measured utilizing independent valuation techniques of identical or similar securities for which significant assumptions are derived primarily from or corroborated by observable market data. Third party vendors compile prices from various sources and may determine the fair value of identical or similar securities by using pricing models that consider observable market data.

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements (Unaudited)

16. Fair Value Measurements - continued

Loans, net

The carrying value of loans is net of deferred fees and costs and the allowance for loan and lease losses. The fair value of loans is measured using an exit price notion.

Bank owned life insurance

The fair value of bank owned life insurance is estimated to equal the carrying amount, which is the cash surrender value.

Interest-bearing deposits

The fair value of interest-bearing checking, savings, and money market deposit accounts is estimated to equal the carrying amount. The fair value of fixed-maturity time deposits is estimated based on interest rates currently offered for deposits of similar remaining maturities.

FHLB advances

The fair value of FHLBA advances is obtained directly from the FHLBA where possible and represent mathematical approximations of exit values derived from its proprietary models when available.

Fed Funds Sold and Fed Funds Purchased

Due to the overnight nature of Fed Funds Sold and Fed Funds Purchased, the fair value of these instruments is estimated to equal the carrying amount.

Commitments to extend credit, lines of credit, and letters of credit

It is not practicable to estimate the fair value of outstanding loan commitments, unused lines of credit, and letters of credit.

17. Legal Proceedings

The Bank is party to various legal actions normally associated with a financial institution. In management's opinion, the effect of these actions will not be material to the financial condition of the Bank.

18. Accounting Standard Updates

Accounting Standards Update ("ASU") 2014-09, "Revenue from Contracts with Customers (Topic 606)." ASU 2014-09 implements a common revenue standard that clarifies the principles for recognizing revenue. The core principle of ASU 2014-09 is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. To achieve that core principle, an entity should apply the following steps: (i) identify the contract(s) with a customer, (ii) identify the performance obligations in the contract, (iii) determine the transaction price, (iv) allocate the transaction price to the performance obligations in the contract and (v) recognize revenue when (or as) the entity satisfies a performance obligation. ASU 2014-09 was originally going to be effective for the Bank on January 1, 2017; however, the FASB deferred the effective date by one year which would make ASU 2014-09 effective for the Bank on January 1, 2018. The Bank's revenue is comprised of net interest income on financial assets and financial liabilities, which is explicitly excluded from the scope of ASU 2014-09, and non-interest income. ASU 2014-09 became effective for the Bank on January 1, 2018 and did not have a material impact on the Bank's financial statements.

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements (Unaudited)

18. Accounting Standard Updates - continued

ASU 2016-01, “*Financial Instruments – Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities*.” ASU 2016-01, among other things, (i) requires equity investments, with certain exceptions, to be measured at fair value with changes in fair value recognized in net income, (ii) simplifies the impairment assessment of equity investments without readily determinable fair values by requiring a qualitative assessment to identify impairment, (iii) eliminates the requirement for public business entities to disclose the methods and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost on the balance sheet, (iv) requires public business entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes, (v) requires an entity to present separately in other comprehensive income the portion of the total change in the fair value of a liability resulting from a change in the instrument-specific credit risk when the entity has elected to measure the liability at fair value in accordance with the fair value option for financial instruments, (vi) requires separate presentation of financial assets and financial liabilities by measurement category and form of financial asset on the balance sheet or the accompanying notes to the financial statements and (vii) clarifies that an entity should evaluate the need for a valuation allowance on a deferred tax asset related to available-for-sale debt securities. ASU 2016-01 became effective for the Bank on January 1, 2018 and did not have a material impact on the Bank’s financial statements.

ASU 2016-02, “*Leases (Topic 842)*.” ASU 2016-02 requires that lessees and lessors recognize lease assets and lease liabilities on the balance sheet and disclose key information about leasing arrangements. ASU 2016-02 was effective for the Bank on January 1, 2019. ASU 2016-02 provides for a modified retrospective transition approach requiring lessees to recognize and measure leases on the balance sheet at the beginning of either the earliest period presented or as of the beginning of the period of adoption with the option to elect certain practical expedients. The Bank has elected to apply ASU 2016-02 as of the beginning of the period of adoption (January 1, 2019) and has not restated comparative periods. Of the optional practical expedients available under ASU 2016-02, all have been adopted except for the hindsight practical expedient. The Bank’s operating leases relate to bank branches. As a result of implementing ASU 2016-02, the Bank recognized an operating lease right-of-use asset of \$456,311 and an operating lease liability of \$456,311 on January 1, 2019, with no impact on the Bank’s consolidated statement of income or consolidated statement of cash flows compared to the prior lease accounting model. The operating lease right-of-use asset and operating lease liability are recorded in other assets and other liabilities, respectively, in the consolidated statements of condition.

ASU 2016-13, “*Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*.” ASU 2016-13 requires the measurement of all expected credit losses for financial assets held at the reporting date based on historical experience, current conditions, and reasonable and supportable forecasts and requires enhanced disclosures related to the significant estimates and judgments used in estimating credit losses, as well as the credit quality and underwriting standards of an organization’s portfolio. In addition, ASU 2016-13 amends the accounting for credit losses on available-for-sale debt securities and purchased financial assets with credit deterioration. The guidance is effective for fiscal years beginning after December 15, 2019 and interim periods within those fiscal years. Management has formed an implementation team led the CFO that also includes other functional areas of the Bank which is currently evaluating the potential impact of ASU 2016-13 on the Bank’s financial statements. While management is currently unable to reasonably estimate the impact of adopting ASU 2016-13, the Bank expects that the impact of adoption could be significantly influenced by the composition, characteristics and quality of the Bank’s loan portfolio as well as the prevailing economic conditions and forecasts as of the adoption date. As part of management’s evaluation process and implementation process, the Bank has focused on data capture and portfolio segmentation with continued progress toward model validation and testing. In July 2019, the FASB proposed changes to the effective date for smaller reporting companies, as defined by the SEC, and other non-SEC reporting entities. The proposal would delay the effective date to fiscal years beginning after December 15, 2022, including interim periods within those fiscal periods. As the Bank is a smaller reporting company for fiscal year 2020, the proposed delay would be applicable. On October 16, 2019, the FASB approved its proposal to delay the effective date for smaller reporting companies, as defined by the SEC, and other non-SEC reporting entities and plans to release a final ASU in mid-November.

ASU 2016-15, “*Statement of Cash Flows (Topic 230) - Classification of Certain Cash Receipts and Cash Payments*.” ASU 2016-15 provides guidance related to certain cash flow issues in order to reduce the current and potential future diversity in practice. ASU 2016-15 became effective for the Bank on January 1, 2018 and did not have a material impact on the Bank’s financial statements.

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements (Unaudited)

18. Accounting Standard Updates - continued

ASU 2016-18, *“Statement of Cash Flows (Topic 230) - Restricted Cash.”* ASU 2016-18 requires that a statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. Therefore, amounts generally described as restricted cash and restricted cash equivalents should be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows. ASU 2016-18 became effective for the Bank on January 1, 2018 and did not have a material impact on the Bank’s financial statements.

ASU 2017-05, *“Other Income - Gains and Losses from the Derecognition of Nonfinancial Assets (Subtopic 610-20) - Clarifying the Scope of Asset Derecognition Guidance and Accounting for Partial Sales of Nonfinancial Assets.”* ASU 2017-05 clarifies the scope of Subtopic 610-20 and adds guidance for partial sales of nonfinancial assets, including partial sales of real estate. Historically, U.S. GAAP contained several different accounting models to evaluate whether the transfer of certain assets qualified for sale treatment. ASU 2017-05 reduces the number of potential accounting models that might apply and clarifies which model does apply in various circumstances. ASU 2017-05 became effective for the Bank on January 1, 2018 and did not have a material impact on the Bank’s financial statements.

ASU 2017-09, *“Compensation - Stock Compensation (Topic 718) - Scope of Modification Accounting.”* ASU 2017-09 clarifies when changes to the terms or conditions of a share-based payment award must be accounted for as modifications. Under ASU 2017-09, an entity will not apply modification accounting to a share-based payment award if all of the following are the same immediately before and after the change: (i) the award's fair value, (ii) the award's vesting conditions and (iii) the award's classification as an equity or liability instrument. ASU 2017-09 became effective for the Bank on January 1, 2018 and did not have a material impact on the Bank’s financial statements.

ASU 2018-07, *“Compensation - Stock Compensation (Topic 718): Improvements to Nonemployee Share-Based Payment Accounting.”* ASU 2018-07 expands the scope of Topic 718, Compensation – Stock Compensation (which currently only includes share-based payments to employees) to include share-based payments issued to nonemployees for goods or services. Consequently, the accounting for share-based payments to nonemployees and employees will be substantially aligned. The ASU supersedes Subtopic 505-50, Equity – Equity-Based Payments to Non-Employees. ASU 2018-07 became effective for the Bank on January 1, 2019 and did not have a material impact on the Bank’s financial statements.

ASU 2018-13, *“Fair Value Measurement (Topic 820) - Disclosure Framework-Changes to the Disclosure Requirements for Fair Value Measurement.”* ASU 2018-13 modifies the disclosure requirements on fair value measurements in Topic 820. The amendments in this update remove disclosures that no longer are considered cost beneficial, modify/clarify the specific requirements of certain disclosures, and add disclosure requirements identified as relevant. ASU 2018-13 will be effective for the Bank on January 1, 2020, with early adoption permitted, and is not expected to have a material impact on the Bank’s financial statements.

CERTIFICATIONS OF THE PRINCIPAL EXECUTIVE OFFICER
Pursuant to Securities Exchange Act Rules 13a-1 and 15d-14
As adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, Michael F. Allen, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Harford Bank;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared; and
 - b Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles; and
 - c Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 6, 2019

/s/ Michael F. Allen
Michael F. Allen
President
(Principal Executive Officer)

CERTIFICATIONS OF THE PRINCIPAL FINANCIAL OFFICER
Pursuant to Securities Exchange Act Rules 13a-1 and 15d-14
As adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, Neil L. Christ, CPA, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Harford Bank;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared; and
 - b Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles; and
 - c Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 6, 2019

/s/ Neil L. Christ, CPA
Neil L. Christ, CPA
Senior Vice President and Chief Financial Officer
(Principal Financial Officer)

CERTIFICATION OF THE PERIODIC REPORT
Pursuant to 18 U.S.C. Section 1350
As adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

Pursuant to, and for purposes only of, 18 U.S.C. § 1350, each of the undersigned hereby certifies that (i) the Quarterly Report of Harford Bank on Form 10-Q for the quarter ended September 30, 2019, filed with the Federal Deposit Insurance Corporation (the “Report”) fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, and (ii) information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of Harford Bank.

Date: November 6, 2019

/s/ Michael F. Allen
Michael F. Allen
President
(Principal Executive Officer)

Date: November 6, 2019

/s/ Neil L. Christ, CPA
Neil L. Christ, CPA
Senior Vice President and Chief Financial Officer
(Principal Financial Officer)