

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2024

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

For the transition period from _____ to _____

FDIC Certificate Number: 19101

HARFORD BANK

(Exact 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.

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 ☒

Indicate the number of shares outstanding of each of the issuer's classes of common equity, as of the latest practicable date.
1,481,355 shares of common stock as of April 26, 2024.

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 Securities Exchange Act of 1934, as amended (the “Exchange Act”). All of the periodic and other reports filed by the Bank with the FDIC pursuant to the Exchange Act are available through the FDIC’s website at: <https://efr.fdic.gov/fcxweb/efr/index.html>, and are also 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, 2023.

The Bank is a Maryland-chartered bank with its principal office in Aberdeen, Harford County, Maryland. Through its nine branches, seven of which are located throughout Harford County and two of which are located 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, savings accounts, money market accounts and time deposits consisting of certificates of deposit of various types. In addition, the Bank offers Individual Retirement Accounts. All deposits are insured by the FDIC up to the maximum allowed by law. The Bank offers a full range of consumer and commercial loans, including fixed-rate consumer mortgage loans, variable rate home equity lines of credit, fixed rate home equity loans, and other consumer loans as well as 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, on-line banking with bill pay service, mobile banking, drive-through banking services, automated teller machine services, Visa check (debit) cards, as well as 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 credit 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 credit losses on loans represents management's estimate of probable expected loan losses inherent in the loan portfolio. Determining the amount of the allowance for credit losses on loans 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 individually evaluated loans, estimated losses on pools of homogeneous loans based on historical loss experience, consideration of current economic trends and conditions and reasonable and supportable forecasts, 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 credit losses on loans.

RESULTS OF OPERATIONS

Summary

For the three-month period ended March 31, 2024, the Bank reported net income of \$1,598,948, compared to \$1,573,914 for the same period of 2023, an increase of \$25,034, or 1.6%. The increase in net income was due primarily to a decrease in credit loss expense of \$183,287 and a decrease in income tax expense of \$22,514, partially offset by a decrease in net interest income of \$57,255, a decrease in noninterest income of \$15,741 and an increase in noninterest expense of \$107,771. The decrease in net interest income for the first quarter of 2024 was due primarily to the increase in yields paid on interest-bearing liabilities exceeding the increase in yields earned on interest-earning assets when compared to the same period of 2023. The increase in noninterest expense for the first quarter of 2024 was due primarily to an increase in salary and benefits and FDIC and state assessments when compared to the same period of 2023.

Basic net income per share of common stock for the three-month period ended March 31, 2024 was \$1.08, compared to \$1.07 for the same period in 2023. Diluted net income per share of common stock for the three-month period ended March 31, 2024 was \$1.07, compared to \$1.06 for the same period in 2023. Basic and diluted net income per share increased in the first quarter of 2024 when compared to the first quarter of 2023 due to an increase in net income earned partially offset by an increase in the weighted average number of common shares outstanding.

Annualized return on average assets was 0.95% for the three-month period ended March 31, 2024, compared to 1.08% for the same period in 2023. Annualized return on average stockholders' equity was 10.71% for the three-month period ended March 31, 2024, compared to 11.61% for the same period in 2023.

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. 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. 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-month periods ended March 31, 2024 and 2023 and related interest income, interest expense, and yields.

Average Balances, Interest, and Yields

	For the Three Months Ended March 31, 2024			For the Three Months Ended March 31, 2023		
	Average Balance	Interest	Yield	Average Balance	Interest	Yield
Assets						
Federal Reserve Bank interest-bearing deposits	\$ 41,837,967	\$ 473,571	4.55%	\$ 15,833,951	\$ 135,534	3.47%
Federal Home Loan Bank interest-bearing deposits	205,912	2,809	5.49%	36,611	441	4.89%
Federal funds sold	-	-	0.00%	-	-	0.00%
Time deposits in other banks	1,870,734	2,284	0.49%	2,542,547	2,905	0.46%
Other	2,667,364	52,523	7.92%	458,356	7,869	6.96%
Investment securities:						
U.S. Treasury securities	16,967,176	53,937	1.28%	20,559,251	58,766	1.16%
U.S. government agency securities	34,353,092	121,908	1.43%	36,762,132	129,380	1.43%
Mortgage-backed and CMO securities	40,224,084	232,814	2.33%	46,240,510	270,165	2.37%
SBA asset-backed securities	9,966,046	57,088	2.30%	11,657,555	46,422	1.61%
State and municipal securities	3,554,292	15,995	1.81%	3,569,261	16,722	1.90%
Total investment securities	105,064,690	481,742	1.84%	118,788,709	521,455	1.78%
Loans:						
Overdrafts	56,818	-	0.00%	44,925	-	0.00%
Consumer	32,371,944	434,625	5.40%	16,730,811	201,203	4.88%
Credit lines	11,796,217	238,920	8.15%	14,524,542	262,021	7.32%
Commercial	70,896,586	1,368,008	7.76%	48,900,608	822,266	6.82%
Real estate	391,769,231	4,956,488	5.09%	356,365,715	3,953,323	4.50%
Other loan fees	-	105,847		-	47,181	
Total loans *	506,890,796	7,103,888	5.64%	436,566,601	5,285,994	4.91%
Allowance for credit losses on loans	(5,705,740)			(4,767,637)		
Total loans, net of allowance for credit losses on loans *	501,185,056	7,103,888	5.70%	431,798,964	5,285,994	4.96%
Total interest-earning assets	652,831,723	8,116,817	5.00%	569,459,138	5,954,198	4.24%
Noninterest-bearing cash	3,427,821			3,454,040		
Bank premises and equipment, net	8,168,544			9,788,117		
Other assets	11,537,837			10,504,086		
Total assets	\$ 675,965,925			\$ 593,205,381		
Liabilities and Stockholders' Equity						
Interest-bearing deposits						
Interest-bearing demand deposits	\$ 130,121,008	44,635	0.14%	\$ 138,409,759	22,467	0.07%
Savings	53,052,277	28,924	0.22%	67,321,240	36,430	0.22%
Money market	93,535,032	494,158	2.12%	93,577,755	104,092	0.45%
Time deposits	147,698,388	1,506,605	4.10%	81,294,927	288,224	1.44%
Total interest-bearing deposits	424,406,705	2,074,322	1.97%	380,603,681	451,213	0.48%
Federal Home Loan Bank overnight borrowings	29,516,484	415,619	5.66%	3,466,667	42,339	4.95%
Federal Home Loan Bank term borrowings	17,000,000	202,408	4.79%	-	-	0.00%
Total borrowed funds	46,516,484	618,027	5.34%	3,466,667	42,339	4.95%
Total interest-bearing deposits and borrowed funds	470,923,189	2,692,349	2.30%	384,070,348	493,552	0.52%
Noninterest-bearing demand deposits	140,682,457			151,644,340		
Other liabilities	4,307,347			2,489,647		
Stockholders' equity	60,052,932			55,001,046		
Total liabilities and stockholders' equity	\$ 675,965,925			\$ 593,205,381		
Net interest spread			2.70%			3.72%
Net interest income		\$ 5,424,468			\$ 5,460,646	
Net margin on interest-earning assets			3.34%			3.89%

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

* Includes non-accrual loans.

Interest income, on a fully taxable equivalent basis, on total interest-earning assets for the three-month period ended March 31, 2024 was \$8,116,817, compared to \$5,954,198 for the same period in 2023, an increase of \$2,162,619, or 36.3%.

Interest income, on a fully taxable equivalent basis, on net loans for the three-month period ended March 31, 2024 was \$7,103,888, compared to \$5,285,994 for the same period in 2023, an increase of \$1,817,894, or 34.4%. The average balance of net loans for the three-month period ended March 31, 2024 was \$501,185,056, compared to \$431,798,964 for the same period in 2023, an increase of \$69,386,092, or 16.1%, primarily due to loan growth experienced in the final three quarters of 2023. The weighted average rate earned on net loans, on a fully taxable equivalent basis, for the three-month period ended March 31, 2024 was 5.70%, compared to 4.96% for the same period in 2023, an increase of 74 basis points, primarily due to increases in market interest rates since March 31, 2023.

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 for the three-month period ended March 31, 2024 was \$478,664, compared to \$138,880 for the same period in 2023, an increase of \$339,784, or 244.7%. The average balance of these instruments for the three-month period ended March 31, 2024 was \$43,914,613, compared to \$18,413,109 for the same period in 2023, an increase of \$25,501,504, or 138.5%. The weighted average rate earned on these holdings, on a fully taxable equivalent basis, for the three-month period ended March 31, 2024 was 4.38%, compared to 3.06% for the same period in 2023, an increase of 132 basis points.

Interest income, on a fully taxable equivalent basis, on investment securities for the three-month period ended March 31, 2024 was \$481,742, compared to \$521,455 for the same period in 2023, a decrease of \$39,713, or 7.6%. The average balance of investment securities for the three-month period ended March 31, 2024 was \$105,064,690, compared to \$118,788,709 for the same period in 2023, a decrease of \$13,724,019, or 11.6%. The weighted average rate earned on investment securities, on a fully taxable equivalent basis, for the three-month period ended March 31, 2024 was 1.84%, compared to 1.78% for the same period in 2023, an increase of six basis points.

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 March 31, 2024, the Bank recorded dividends received or accrued on stock issued by the FHLBA in the amount of \$52,523 on a fully taxable equivalent basis, compared to \$7,869 for the same period in 2023, an increase of \$44,654, or 567.5%. The average balance of FHLBA capital stock for the three-month period ended March 31, 2024 was \$2,667,364, compared to \$458,356 for the same period in 2023, an increase of \$2,209,008, or 481.9%. The weighted average rate earned on FHLBA capital stock, on a fully taxable equivalent basis, for the three-month period ended March 31, 2024 was 7.92%, compared to 6.96% for the same period in 2023, an increase of 96 basis points.

Interest expense on interest-bearing deposit liabilities for the three-month period ended March 31, 2024 was \$2,074,322, compared to \$451,213 for the same period in 2023, an increase of \$1,623,109, or 359.7%. The average balance of interest-bearing deposit liabilities for the three-month period ended March 31, 2024 was \$424,406,705, compared to \$380,603,681 for the same period in 2023, an increase of \$43,803,024, or 11.5%. The weighted-average rate paid on these deposit liabilities for the three-month period ended March 31, 2024 was 1.97%, compared to 0.48% for the same period in 2023, an increase of 149 basis points.

Interest expense on total borrowed funds for the three-month period ended March 31, 2024 was \$618,027, compared to \$42,339 for the same period in 2023, an increase of \$575,688, or 1359.7%. The average balance of total borrowed funds for the three-month period ended March 31, 2024 was \$46,516,484, compared to \$3,466,667 for the same period in 2023, an increase of \$43,049,817, or 1,241.8%. The weighted-average rate paid on total borrowed funds for the three-month period ended March 31, 2024 was 5.34%, compared to 4.95% for the same period in 2023, an increase of 39 basis points.

Net interest income, on a fully taxable equivalent basis, for the three-month period ended March 31, 2024 was \$5,424,468, compared to \$5,460,646 for the same period in 2023, a decrease of \$36,178, or 0.7%. 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, for the three-month period ended March 31, 2024 was 3.34%, compared to 3.89% for the same period in 2023, a decrease of 55 basis points. 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 Bank’s net interest spread, on a fully taxable equivalent basis, for the three-month period ended March 31, 2024 was 2.70%, compared to 3.72% for the same period in 2023, a decrease of 102 basis points.

Provision for Credit Losses on Loans

The provision for or recovery of credit losses on loans is determined by management as the amount to be added to or subtracted from, respectively, the allowance for credit losses on loans after net charge-offs (charge-offs less recoveries) have been deducted to bring the allowance for credit losses on loans to a level which, in management's best estimation, is necessary to absorb probable expected losses inherent in the existing loan portfolio. The Bank recorded provision for credit losses on loans expense for the three-month period ended March 31, 2024 of \$30,000, compared to provision expense of \$172,461 recorded for the same period of 2023. The difference in the amount of the provision for credit losses on loans between the 2024 and 2023 periods resulted from changes in the volume and mix of loans, management's assessment of the current and a reasonable and supportable forecast of market conditions, and management's analysis of the inherent risk within the loan portfolio.

Provision for Credit Losses on Off-Balance Sheet Items

The provision for or recovery of credit losses on off-balance sheet items is determined by management as the amount to be added to or subtracted from, respectively, the allowance for credit losses on off-balance sheet items to bring the allowance for credit losses on off-balance sheet items to a level which, in management's best estimation, is necessary to absorb probable expected losses inherent in off-balance sheet items. The Bank recorded recovery of credit losses on off-balance sheet items expense for the three-month period ended March 31, 2024 of \$72,501, compared to recovery of credit losses on off-balance sheet items expense of \$31,675 for the same period of 2023. The difference in the amount of the provision for or recovery of credit losses on off-balance sheet items between the 2024 and 2023 periods resulted from changes in the volume and mix of the components making up off-balance sheet items, management's assessment of the current and a reasonable and supportable forecast of market conditions, and management's analysis of the inherent risk within the components making up off-balance sheet items.

Noninterest Revenue

Noninterest revenue for the three-month period ended March 31, 2024 was \$479,621, compared to \$495,362 for the same period in 2023, a decrease of \$15,741, or 3.2%. The decrease was due to decreases of \$9,170 in service charges on deposit accounts and \$12,496 in other fees and commissions, partially offset by increases of \$4,396 in debit card income and \$1,529 in earnings on bank owned life insurance for the three-month period ended March 31, 2024 when compared to the same period in 2023.

Noninterest Expenses

Noninterest expenses for the three-month period ended March 31, 2024 were \$3,765,890, compared to \$3,658,119 for the same period in 2023, an increase of \$107,771, or 2.9%. The increase was due primarily to increases of \$79,510 in salaries and benefits expense, \$26,514 in professional fees and \$49,578 in FDIC and state assessments, partially offset by a decrease of \$48,806 in other operating expenses when comparing the three-month period ended March 31, 2024 to the same period in 2023.

Income Tax Expense

Income tax expense for the three-month period ended March 31, 2024 was \$516,332, compared to \$538,846 for the same period of 2023, a decrease of \$22,514 or 4.2%. The decrease was primarily due to a decline in the Bank's effective income tax rate for the three-month period ended March 31, 2024 to 24.41%, compared to 25.50% for the same period in 2023, with the decrease primarily due to a change in the mix of income tax components.

FINANCIAL CONDITION

Assets

Total assets were \$678,365,661 at March 31, 2024, compared to \$665,617,205 at December 31, 2023, an increase of \$12,748,456, or 1.9%.

The Bank invests excess cash balances in interest-bearing accounts at other banks and federal funds sold to correspondent banks. The balance on these instruments was \$47,289,987 at March 31, 2024, compared to \$30,427,507 at December 31, 2023, an increase of \$16,862,480, or 55.4%.

Investment securities were \$100,762,823 at March 31, 2024, compared to \$106,495,906 at December 31, 2023, a decrease of \$5,733,083, or 5.4%.

Loans

Loans, net of the allowance for credit losses on loans, were \$504,120,299 at March 31, 2024, compared to \$502,249,930 at December 31, 2023, an increase of \$1,870,369, or 0.4%. The average net loan portfolio represented 76.8% of average earning assets for the three-month period ended March 31, 2024, compared to 75.8% for the same period in 2023.

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

	March 31, 2024		December 31, 2023	
	Amount	% of Total	Amount	% of Total
Real estate				
Construction, development and other land	\$ 31,339,262	6.14%	\$ 31,970,782	6.29%
Secured by farmland	8,645,879	1.69%	8,778,243	1.73%
Commercial	253,212,530	49.64%	254,009,724	49.98%
Residential	135,127,371	26.49%	134,764,915	26.52%
Commercial and industrial	50,148,987	9.83%	46,110,314	9.07%
Other consumer	31,571,416	6.19%	32,515,311	6.40%
Overdrafts	52,541	0.02%	68,905	0.01%
Gross loans	510,097,986	100.00%	508,218,194	100.00%
Net deferred (fees) costs	(245,190)		(258,437)	
Allowance for credit losses on loans	(5,732,497)		(5,709,827)	
Net loans	<u>\$ 504,120,299</u>		<u>\$ 502,249,930</u>	
Allowance for credit losses on loans to gross loans	<u>1.12%</u>		<u>1.12%</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 credit losses on loans. Management believes the policies governing nonperforming loans and charge-offs are consistent with industry and regulatory standards. The amount of the allowance for credit losses on loans and the resulting provision for or recovery of credit losses on loans expense are reviewed and approved quarterly by the Board of Directors.

The following table provides a comprehensive view of the allowance for credit losses on loans activity including the periodic activity of charge-offs and recoveries allocated by loan class for the three-month periods ended March 31, 2024 and 2023.

Three months ended:		Construction, Development & Other Land	Commercial Real Estate & Farmland	Residential Real Estate	Commercial & Industrial	Other Consumer & Overdrafts	Total
March 31, 2024	Unallocated						
Allowance for credit losses on loans:							
Beginning balance	\$ 8,660	\$ 665,816	\$ 2,086,568	\$ 1,460,185	\$ 895,946	\$ 592,652	\$ 5,709,827
Charge-offs	-	-	-	-	-	(10,991)	(10,991)
Recoveries	-	-	-	2,000	-	1,661	3,661
Provision for (recovery of) credit losses on loans	2,248	18,125	(64,681)	1,862	82,640	(10,194)	30,000
Ending balance	<u>\$ 10,908</u>	<u>\$ 683,941</u>	<u>\$ 2,021,887</u>	<u>\$ 1,464,047</u>	<u>\$ 978,586</u>	<u>\$ 573,128</u>	<u>\$ 5,732,497</u>
March 31, 2023							
Allowance for credit losses on loans:							
Beginning balance	\$ 13,670	\$ 446,024	\$ 2,550,667	\$ 986,573	\$ 452,861	\$ 245,973	\$ 4,695,768
Impact of ASC 326 adoption	\$ (13,670)	\$ (112,669)	\$ 97,825	\$ 219,576	\$ (146,758)	\$ 162,017	\$ 206,321
Charge-offs	-	-	-	(766)	-	(4,765)	(5,531)
Recoveries	-	-	-	1,000	-	1,325	2,325
Provision for (recovery of) credit losses on loans	-	31,792	(118,417)	46,540	62,279	150,267	172,461
Ending balance	<u>\$ -</u>	<u>\$ 365,147</u>	<u>\$ 2,530,075</u>	<u>\$ 1,252,923</u>	<u>\$ 368,382</u>	<u>\$ 554,817</u>	<u>\$ 5,071,344</u>

The following table presents net (charge-offs) recoveries and the average balances of loans for the periods indicated.

Three months ended:	Periodic Net (Charge-Offs)	Annualized Net (Charge- Offs) Recoveries to Average Loans
March 31, 2024	Recoveries <u>\$ (7,330)</u>	Average Loans <u>\$ 501,185,056</u> <u>-0.01%</u>
March 31, 2023	Recoveries <u>\$ (3,206)</u>	Average Loans <u>\$ 431,798,964</u> <u>0.00%</u>

The following table presents the allocation of allowance for credit losses on loans and the balances of loans that were individually and collectively evaluated at March 31, 2024 and December 31, 2023.

		Construction, Development & Other Land	Commercial Real Estate & Farmland	Residential Real Estate	Commercial & Industrial	Other Consumer & Overdrafts	Total
March 31, 2024	Unallocated						
Allowance balance allocated to loans:							
Individually evaluated	\$ -	\$ -	\$ -	\$ -	\$ 2,565	\$ -	\$ 2,565
Collectively evaluated	10,908	683,941	2,021,887	1,464,047	976,021	573,128	5,729,932
	<u>\$ 10,908</u>	<u>\$ 683,941</u>	<u>\$ 2,021,887</u>	<u>\$ 1,464,047</u>	<u>\$ 978,586</u>	<u>\$ 573,128</u>	<u>\$ 5,732,497</u>
Loan balances:							
Individually evaluated		\$ -	\$ 6,797,192	\$ 154,058	\$ 130,607	\$ 1,071	\$ 7,082,928
Collectively evaluated		31,339,262	255,061,217	134,973,313	50,018,380	31,622,886	503,015,058
		<u>\$ 31,339,262</u>	<u>\$ 261,858,409</u>	<u>\$ 135,127,371</u>	<u>\$ 50,148,987</u>	<u>\$ 31,623,957</u>	<u>\$ 510,097,986</u>
December 31, 2023							
Allowance balance allocated to loans:							
Individually evaluated	\$ -	\$ -	\$ 56,000	\$ -	\$ 2,587	\$ -	\$ 58,587
Collectively evaluated	8,660	665,816	2,030,568	1,460,185	893,359	592,652	5,651,240
	<u>\$ 8,660</u>	<u>\$ 665,816</u>	<u>\$ 2,086,568</u>	<u>\$ 1,460,185</u>	<u>\$ 895,946</u>	<u>\$ 592,652</u>	<u>\$ 5,709,827</u>
Loan balances:							
Individually evaluated		\$ -	\$ 8,381,335	\$ 293,870	\$ 233,843	\$ 4,252	\$ 8,913,300
Collectively evaluated		31,970,782	254,406,632	134,471,045	45,876,471	32,579,964	499,304,894
		<u>\$ 31,970,782</u>	<u>\$ 262,787,967</u>	<u>\$ 134,764,915</u>	<u>\$ 46,110,314</u>	<u>\$ 32,584,216</u>	<u>\$ 508,218,194</u>

The allowance for credit losses on loans is increased by provisions for credit losses on loans charged to expense and recoveries of credit losses on loans previously charged-off. The allowance for credit losses on loans is decreased by loan charge-offs and recovery of provision for credit losses on loans expense. Provision for or recovery of provision for credit losses on loans are made to bring the allowance for credit losses on loans within the range of balances that are considered appropriate based upon the allowance methodology and to reflect expected losses inherent in the loan portfolio as of the balance sheet date. Accordingly, the methodology is based on historical loss experience by loan classification and on specific loss allocations, with adjustments for current and reasonable and supportable forecast events and conditions, or the “expected loss” approach. Management’s process for determining the appropriate level of the allowance for credit losses on loans is designed to account for credit losses over the expected life of loans. The provision for or recovery of provision for credit losses on loans 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, and adjustments for current and reasonable and supportable forecast events and conditions. The provision for or recovery of provision for credit losses on loans also reflect the totality of actions taken on all loans for a particular period. The amount of the provision for or recovery of provision for credit losses on loans reflects not only the necessary increases or decreases in the allowance for credit losses on loans 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 credit losses on loans was \$5,732,497 at March 31, 2024, compared to \$5,709,827 at December 31, 2023, an increase of \$22,670, or 0.4%. The increase in allowance for credit losses on loans was due to recoveries of amounts previously charged-off of \$3,661, and provision for credit losses on loans of \$30,000, partially offset by amounts charged-off of \$10,991. The “Allowance for Credit Losses on Loans to Gross Loans” ratio at March 31, 2024 was 1.12% compared to 1.12% at December 31, 2023. The allowance level reflects the results of management’s assessment of current and forecasted market conditions and analysis of expected inherent risk within the loan portfolio performed during the quarter.

The adequacy of the allowance for credit losses on loans is determined based upon management’s estimate of the expected 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 and reasonable and supportable forecast market conditions. Management believes that the allowance for credit losses on loans is adequate as of March 31, 2024; 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 the allowance for credit losses on loans by regulatory agencies, auditors and consultants engaged by the Bank may result in the need for additional provision for or recovery of provision for credit losses on loans 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 Past Due	60-89 Days Past Due	90 Days and Over Past Due	Total Past Due	Current	Total Loans	Loans over 90 Days and Accruing
March 31, 2024							
Construction, development & other land	\$ -	\$ -	\$ -	\$ -	\$ 31,339,262	\$ 31,339,262	\$ -
Commercial real estate & farmland	232,340	29,842	-	262,182	261,596,227	261,858,409	-
Residential real estate	-	32,576	-	32,576	135,094,795	135,127,371	-
Commercial & industrial	-	-	-	-	50,148,987	50,148,987	-
Other consumer & overdrafts	76,698	-	-	76,698	31,547,259	31,623,957	-
Total	<u>\$ 309,038</u>	<u>\$ 62,418</u>	<u>\$ -</u>	<u>\$ 371,456</u>	<u>\$ 509,726,530</u>	<u>\$ 510,097,986</u>	<u>\$ -</u>
December 31, 2023							
Construction, development & other land	\$ -	\$ -	\$ -	\$ -	\$ 31,970,782	\$ 31,970,782	\$ -
Commercial real estate & farmland	248,258	-	-	248,258	262,539,709	262,787,967	-
Residential real estate	35,286	-	-	35,286	134,729,629	134,764,915	-
Commercial & industrial	-	102,139	-	102,139	46,008,175	46,110,314	-
Other consumer & overdrafts	144,576	-	-	144,576	32,439,640	32,584,216	-
Total	<u>\$ 428,120</u>	<u>\$ 102,139</u>	<u>\$ -</u>	<u>\$ 530,259</u>	<u>\$ 507,687,935</u>	<u>\$ 508,218,194</u>	<u>\$ -</u>

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

Non-performing Assets	March 31, 2024	December 31, 2023
Non-performing loans by class		
Commercial real estate and farmland	\$ 6,206,095	\$ 6,362,441
Residential real estate	47,774	53,592
Commercial & industrial	-	102,139
Other consumer	1,071	4,252
Total non-performing loans	6,254,940	6,522,424
Foreclosed real estate	-	-
Reposessed assets	-	-
Total non-performing assets	<u>\$ 6,254,940</u>	<u>\$ 6,522,424</u>

Further information about the loan portfolio and the allowance for credit losses on loans 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, the amount undrawn on 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. As part of implementing the Financial Accounting Standards Board's Accounting Standards Update ("ASU") 2016-13 on January 1,

2023, the Bank created an allowance for credit losses on off-balance sheet items related to these financial instruments with off-balance sheet risk, which is reported as a liability on the consolidated statements of condition. The allowance for credit losses on off-balance sheet items was \$434,149 at March 31, 2024, compared to \$506,650 at December 31, 2023, a decrease of \$72,501, or 14.3%.

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 were \$571,104,984 at March 31, 2024, compared to \$554,308,636 at December 31, 2023, an increase of \$16,796,348, or 3.0%. Noninterest-bearing deposit liabilities were \$140,052,705 at March 31, 2024, compared to \$145,916,027 at December 31, 2023, a decrease of \$5,863,322, or 4.0%. Interest-bearing deposit liabilities were \$431,052,279 at March 31, 2024, compared to \$408,392,609 at December 31, 2023, an increase of \$22,659,670, or 5.5%. The Bank utilizes deposits primarily to fund its earning assets. During the three-month period ended March 31, 2024, average deposit liabilities provided funding for approximately 86.6% of average earning assets, compared to 93.5% for the comparable period of 2023.

Certificates of deposit greater than the FDIC deposit insurance limit of \$250,000 were \$53,239,911 at March 31, 2024, compared to \$42,875,315 at December 31, 2023.

Capital

Total stockholders' equity was \$60,290,614 at March 31, 2024, compared to \$58,962,668 at December 31, 2023, an increase of \$1,327,946, or 2.3%. The increase was due to earnings in the amount of \$1,598,948 and stock transactions netting \$68,937, partially offset by dividends declared and paid of \$339,939.

The federal banking agencies have provided community banking organizations the option to phase in the regulatory capital impact of the adoption of ASU 2016-13, which was effective for the Bank on January 1, 2023. Under this option, the initial impact of adoption of ASU 2016-13 may be phased into the regulatory capital calculations evenly over a three year period, starting with the first required regulatory report as of March 31, 2023. The Bank has not elected to phase in the impact of ASU 2016-13 on regulatory capital.

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 fully phased-in as of January 1, 2019, minimum requirements increased for both the quantity and quality of capital held by the Bank. The rules included a new minimum Common Equity Tier 1 capital ratio ("CET1 ratio") of 4.5% which, with the capital conservation buffer of 2.5% of risk-weighted assets added, effectively results in a minimum CET1 ratio of 7.0%. Basel III raised the minimum Tier 1 capital ratio from 4.0% to 6.0% which, with the capital conservation buffer of 2.5% of risk-weighted assets added, effectively results in a minimum Tier 1 capital ratio of 8.5%. Basel III maintained the minimum total capital ratio of 8.0%, which, with the capital conservation buffer of 2.5% of risk-weighted assets added, effectively results in a minimum Tier 1 capital ratio of 10.5%. Basel III maintained the minimum Tier 1 leverage capital ratio of 4.0%. Basel III also changed risk weights for certain assets and off-balance sheet exposures.

On September 17, 2019 the FDIC finalized a rule that introduced an optional simplified measure of capital adequacy for qualifying community banking organizations (i.e., the community bank leverage ratio framework, "CBLR framework"), as required by the Economic Growth, Regulatory Relief and Consumer Protection Act. The CBLR framework is designed to reduce burden by removing the requirements for calculating and reporting risk-based capital ratios for qualifying community banking organizations that opt into the framework. To qualify for the CBLR framework, a community banking organization must have a Tier 1 leverage ratio of at least 9 percent, less than \$10 billion in total consolidated assets, and limited amounts of off-balance-sheet exposures and trading assets and liabilities. A qualifying community banking organization that opts into the CBLR framework and meets all requirements under the framework will be considered to have met the well-capitalized ratio requirements under the Prompt Corrective Action regulations and will not be required to report or calculate risk-based capital. The Bank has elected not to opt into the CBLR framework at this time.

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 March 31, 2024. 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 March 31, 2024, the Bank's risk-based capital ratio was 13.35%.

The CET1 capital ratio 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 amount of the capital conservation buffer, with 6.50% being the regulatory minimum for well-capitalized banks. At March 31, 2024, the Bank's CET1 ratio was 12.11%.

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 amount of the capital conservation buffer, with 8.00% being the regulatory minimum for well-capitalized banks. At March 31, 2024, the Bank's Tier 1 capital ratio was 12.11%.

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 March 31, 2024, was 8.92%.

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 capital 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 a correspondent bank 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 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.

The Bank's FHLBA fixed-rate term borrowings are summarized as follows:

Maturity Date	Interest Rate	Interest Frequency	March 31, 2024	December 31, 2023
November 28, 2025	4.7800%	Quarterly	\$ 10,000,000	\$ 10,000,000
November 27, 2026	4.6105%	Quarterly	7,000,000	7,000,000
			<u>\$ 17,000,000</u>	<u>\$ 17,000,000</u>

In addition to the fixed-rate term borrowings, the Bank had \$25.25 million in FHLBA adjustable rate borrowings with no fixed maturity outstanding under the line of credit as of March 31, 2024, at an interest rate of 5.58%. The Bank had \$31.0 million in adjustable rate borrowings with no fixed maturity outstanding under the line of credit as of December 31, 2023, at an interest rate of 5.57%. Based on the value of available collateral as of March 31, 2024, the Bank could borrow an additional \$69,280,294 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 March 31, 2024, the Bank could borrow \$14,047,208 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 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 March 31, 2024, or \$67,836,566.

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 is a smaller reporting company and, as such, is not required to provide information called for by this item.

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 and procedures as of March 31, 2024 was carried out under the supervision and with the participation of the Bank's management, including the PEO and the PFO. Based in that evaluation, the Bank's management, including the PEO and the PFO, has concluded that the Bank's disclosure controls and procedures are, in fact, effective at the reasonable assurance level.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings

The Bank is at times, in the ordinary course of business, subject to other legal actions that are normally associated with a financial institution, none of which, in management's opinion, 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, 2023. 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 2004 Director Non-Qualified Stock Option Plan (the "2004 Director Plan"), the 2008 Key Employee Stock Option Plan (the "2008 Key Employee Plan"), the 2015 Director Stock Option Plan (the "2015 Director Plan") and the 2020 Employee Stock Purchase Plan (the "2020 ESPP"). The DRIP was 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 Director Plan expired in April 2014, and no further grants may be made under the plan, but options granted under the 2004 Director Plan remain outstanding and subject to exercise until April 2024. On April 9, 2015, the Bank's Board of Directors adopted the 2015 Director Plan so that the Bank may continue to incent non-employee directors through the grant of non-qualified stock options. The 2008 Key Employee Plan expired in April 2018 and no further grants may be made under the plan, but options granted under the 2008 Key Employee Plan remain outstanding and subject to exercise until April 2028. On May 20, 2020, the Bank's stockholders approved the 2020 ESPP that allows eligible employees to acquire in total up to 100,000 shares of the Bank's common stock at a discount through accumulated payroll deductions.

During the first quarter of 2024, a net total of 278 shares of common stock were sold pursuant to the DRIP at \$32.00 per share, a total of 2,142 shares of common stock were sold pursuant to the exercise of options at an average exercise price of \$19.77 per share, and a total of 580 shares of common stock were sold pursuant to the 2020 ESPP at a weighted-average price of \$30.56 per share.

Item 3. Defaults Upon Senior Securities

Not applicable.

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

During the quarter ended March 31, 2024, no director or officer of the Bank adopted or terminated (i) any contract, instruction or written plan for the purchase or sale of securities of the registrant intended to satisfy the affirmative defense conditions of Rule 10b5-1(c) promulgated under the Exchange Act or (ii) any “non-Rule 10b5-1 trading arrangement” as defined in Item 408(c) of the Securities and Exchange Commission’s Regulation S-K.

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: May 1, 2024

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

Date: May 1, 2024

/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:	March 31, 2024	December 31, 2023
	(Unaudited)	
ASSETS		
Cash and due from banks	\$ 4,946,244	\$ 3,833,802
Federal Reserve Bank deposit	45,464,584	27,864,800
Federal funds sold and Federal Home Loan Bank deposit	339,225	304,026
Total cash and cash equivalents	50,750,053	32,002,628
Time deposits in other banks	1,486,178	2,258,681
Investment securities held to maturity, at amortized cost (fair value of \$91,552,712 in 2024 and \$97,655,442 in 2023)	100,762,823	106,495,906
Federal Home Loan Bank stock, at cost	2,496,700	2,720,700
Total loans, including deferred fees net of costs	509,852,796	507,959,757
Less: Allowance for credit losses on loans	(5,732,497)	(5,709,827)
Net loans	504,120,299	502,249,930
Bank premises and equipment, net	8,115,035	8,194,907
Accrued interest receivable	1,752,712	1,825,679
Deferred income taxes	1,613,836	1,613,836
Bank owned life insurance	6,577,956	6,543,598
Other assets	690,069	1,711,340
Total assets	\$ 678,365,661	\$ 665,617,205
LIABILITIES AND STOCKHOLDERS' EQUITY		
Deposits		
Noninterest-bearing	\$ 140,052,705	\$ 145,916,027
Interest-bearing	431,052,279	408,392,609
Total deposits	571,104,984	554,308,636
Federal Home Loan Bank overnight borrowings	25,250,000	31,000,000
Federal Home Loan Bank term borrowings	17,000,000	17,000,000
Accrued interest payable	911,663	712,066
Income taxes payable	1,286,463	770,131
Allowance for credit losses on off-balance sheet items	434,149	506,650
SERP liability	1,126,105	1,133,875
Other liabilities	961,683	1,223,179
Total liabilities	618,075,047	606,654,537
Stockholders' equity		
Common stock, par value \$10 per share; authorized 5,000,000 shares; issued and outstanding 1,480,595 shares in 2024, and 1,477,595 shares in 2023	14,805,950	14,775,950
Surplus	17,903,679	17,864,742
Undivided profits	27,580,985	26,321,976
Total stockholders' equity	60,290,614	58,962,668
Total liabilities and stockholders' equity	\$ 678,365,661	\$ 665,617,205

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 March 31,	
	2024	2023
Interest revenue		
Loans, including fees	\$ 7,089,583	\$ 5,268,453
Investment securities held to maturity	465,098	504,028
Federal funds sold and Federal Home Loan Bank deposit	2,625	412
Federal Reserve Bank deposit	442,707	126,701
Time deposits in other banks	2,284	2,905
Other	49,100	7,356
Total interest revenue	<u>8,051,397</u>	<u>5,909,855</u>
Interest expense		
Deposits	2,074,322	451,213
Borrowed funds	618,027	42,339
Total interest expense	<u>2,692,349</u>	<u>493,552</u>
Net interest income	5,359,048	5,416,303
Credit loss expense		
Provision for (recovery of) credit losses on loans	30,000	172,461
Provision for (recovery of) credit losses on off-balance sheet items	(72,501)	(31,675)
Total provision for (recovery of) credit loss expense	<u>(42,501)</u>	<u>140,786</u>
Net interest income after provision for (recovery of) credit loss expense	<u>5,401,549</u>	<u>5,275,517</u>
Noninterest revenue		
Service charges on deposit accounts	183,666	192,836
Debit card income	131,814	127,418
Earnings on bank owned life insurance	34,358	32,829
Other fees and commissions	129,783	142,279
Total noninterest revenue	<u>479,621</u>	<u>495,362</u>
Noninterest expense		
Salaries and benefits	2,370,371	2,290,861
Occupancy	286,331	288,817
Furniture and equipment	232,009	222,675
Data processing expense	241,879	234,742
Professional fees	123,397	96,883
Director and committee fees	78,350	82,400
Stationery and supplies	16,554	19,500
FDIC and state assessments	137,976	88,398
Advertising	43,319	49,333
Other operating	235,704	284,510
Total noninterest expense	<u>3,765,890</u>	<u>3,658,119</u>
Income before income taxes	2,115,280	2,112,760
Income taxes	516,332	538,846
Net income	<u>\$ 1,598,948</u>	<u>\$ 1,573,914</u>
Basic net income per common share	\$ 1.08	\$ 1.07
Diluted net income per common share	\$ 1.07	\$ 1.06

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:					
March 31, 2023					
Balance at beginning of period	1,470,446	\$ 14,704,460	\$ 17,674,158	\$ 21,668,070	\$ 54,046,688
Transition adjustment pursuant to adoption of ASU 2016-13				(505,850)	(505,850)
Net income				1,573,914	1,573,914
Cash dividends, \$0.22 per share				(323,881)	(323,881)
Common stock issued:					
Shares issued under stock-based compensation plans and related tax effects	2,391	23,910	24,104	-	48,014
Stock sold and dividend reinvestment plan (DRIP)	2,568	25,680	58,216	-	83,896
Stock-based compensation expense			-	-	-
Stock acquired for DRIP administration	(585)	(5,850)	(13,262)	-	(19,112)
Balance, March 31, 2023	<u>1,474,820</u>	<u>\$ 14,748,200</u>	<u>\$ 17,743,216</u>	<u>\$ 22,412,253</u>	<u>\$ 54,903,669</u>
March 31, 2024					
Balance at beginning of period	1,477,595	\$ 14,775,950	\$ 17,864,742	\$ 26,321,976	\$ 58,962,668
Net income				1,598,948	1,598,948
Cash dividends, \$0.23 per share				(339,939)	(339,939)
Common stock issued:					
Shares issued under stock-based compensation plans and related tax effects	2,722	27,220	32,853	-	60,073
Stock sold and dividend reinvestment plan (DRIP)	2,409	24,090	52,966	-	77,056
Stock-based compensation expense			-	-	-
Stock acquired for DRIP administration	(2,131)	(21,310)	(46,882)	-	(68,192)
Balance, March 31, 2024	<u>1,480,595</u>	<u>\$ 14,805,950</u>	<u>\$ 17,903,679</u>	<u>\$ 27,580,985</u>	<u>\$ 60,290,614</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 Three Months Ended March 31,	2024	2023
Cash flows provided by (used in) operating activities		
Interest received	\$ 8,061,830	\$ 5,893,161
Fees and commissions received	598,340	658,196
Interest paid	(2,492,752)	(455,418)
Cash paid to suppliers and employees	(2,926,162)	(4,472,341)
Net cash provided by (used in) operating activities	<u>3,241,256</u>	<u>1,623,598</u>
Cash flows provided by (used in) investing activities		
Proceeds from maturities of time deposits in other banks	766,000	-
Proceeds from calls and maturities of investment securities	5,652,363	2,497,824
Redemption (purchase) of FHLB stock	224,000	(350,200)
Loans originated, net of principal repayments	(1,887,123)	(18,871,886)
Net (decrease) increase in deferred loan fees and costs	17,792	(82,136)
Purchases of bank premises and equipment	(42,209)	(51,267)
Net cash provided by (used in) investing activities	<u>4,730,823</u>	<u>(16,857,665)</u>
Cash flows provided by (used in) financing activities		
Net increase (decrease) in time deposits	24,967,491	5,702,839
Net increase (decrease) in other deposits	(8,171,143)	(6,682,571)
Proceeds from borrowed funds	-	9,000,000
Repayments of borrowed funds	(5,750,000)	-
Dividends paid	(339,939)	(323,881)
Dividends reinvested	77,056	83,896
Shares issued under stock-based compensation plans and related tax effects	60,073	48,014
Stock acquired for DRIP administration	(68,192)	(19,112)
Net cash provided by (used in) financing activities	<u>10,775,346</u>	<u>7,809,185</u>
Net increase (decrease) in cash and cash equivalents	<u>18,747,425</u>	<u>(7,424,882)</u>
Cash and cash equivalents at beginning of period	<u>32,002,628</u>	<u>28,444,396</u>
Cash and cash equivalents at end of period	<u><u>\$ 50,750,053</u></u>	<u><u>\$ 21,019,514</u></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 Three Months Ended March 31,	2024	2023
Reconciliation of net income to net cash provided by operating activities		
Net income	\$ 1,598,948	\$ 1,573,914
Adjustments to reconcile net income to net cash provided by operating activities		
Net amortization and accretion on loan fees and costs	(31,038)	(11,337)
Net amortization and accretion on time deposits in other banks	6,503	9,010
Net amortization and accretion on investment securities	80,720	116,622
Depreciation and amortization on fixed assets and software	122,847	136,926
Earnings on bank owned life insurance	(34,358)	(32,829)
Provision for (recovery of) credit losses on loans	30,000	172,461
Provision for (recovery of) credit losses on off-balance sheet items	(72,501)	(31,675)
Decrease (increase) in		
Accrued interest receivable	72,967	31,845
Income taxes refundable	-	146,070
Other assets	1,020,505	(267,518)
Increase (decrease) in		
Accrued interest payable	199,597	38,134
Income taxes payable	516,332	392,776
SERP liability	(7,770)	(10,125)
Other liabilities	(261,496)	(640,676)
	<u>\$ 3,241,256</u>	<u>\$ 1,623,598</u>
Non-Cash Transactions:		
Transition adjustment pursuant to adoption of ASU 2016-13	<u>\$ -</u>	<u>\$ 697,892</u>

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

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements

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. The estimates related to the allowance for credit losses, fair value of financial instruments and income taxes are particularly subject to change.

Current expected credit losses – Adoption of ASU 2016-13

Financial Accounting Standards Board (“FASB”) Accounting Standards Update (“ASU”) 2016-13, “Financial Instruments - Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments” affects financial assets with the contractual right to receive cash, including loans held for investment, held to maturity debt securities, and off-balance sheet credit exposures, unless specifically excluded from scope. Financial assets measured at an amortized cost basis are presented at the net amount expected to be collected. The allowance for credit losses (“ACL”) is a valuation account that is deducted from the amortized cost basis of the financial asset to present the net carrying value and the amount expected to be collected on the financial asset. The Bank has made the accounting policy election to exclude accrued interest receivable on financial assets from the estimate of credit losses.

The Bank adopted the Current Expected Credit Loss (“CECL”) Standard using the modified retrospective method for all financial assets measured at amortized cost and off-balance sheet credit exposures on January 1, 2023. Upon adoption, the Bank recognized an after-tax cumulative effect reduction to undivided profits totaling \$505,850, as detailed in the table below. Results for reporting periods beginning on January 1, 2023 are presented under the CECL standard while prior period amounts continue to be reported in accordance with previously applicable accounting guidance.

The adoption of ASU 2016-13 resulted in the following adjustments to the Bank’s consolidated financial statements as of January 1, 2023.

	Changes in Consolidated Statements of Condition	Income Tax Effect	Changes to Undivided Profits
At January 1, 2023			
Allowance for credit losses on loans	\$ 206,321	\$ 56,774	\$ 149,547
Allowance for credit losses on off-balance sheet items	491,571	135,268	356,303
	<u>\$ 697,892</u>	<u>\$ 192,042</u>	<u>\$ 505,850</u>

Reclassifications

Certain reclassifications have been made to the 2023 consolidated financial statement presentation to conform to the current year’s format. Total stockholders’ equity and net income are unchanged due to these reclassifications.

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements

1. Summary of Significant Accounting Policies - continued

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 typically 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. 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. An allowance for credit losses on held to maturity investments is recognized when lifetime credit losses are expected, for an amount that reflects the expected lifetime credit losses.

Restricted equity securities

As a member of the Federal Home Loan Bank of Atlanta ("FHLBA"), the Bank is required to hold FHLBA stock as a condition of membership as well as in relation to the Bank's use of products and services. FHLBA stock is not publicly-traded and is sold and redeemed by the FHLBA at par. The Bank views its investment in FHLBA stock as a long-term investment and as a restricted equity security, which is carried at cost and periodically evaluated for impairment based on the ultimate recoverability of the par value. The Bank does not consider this investment to be impaired as of March 31, 2024, and no impairment has been recognized.

Loans and allowance for credit losses on loans

Loans are stated at unpaid principal balance adjusted for any interest amounts applied to principal on nonaccrual loans, any amounts partially charged-off, the allowance for credit losses on loans, 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 ninety days past due and collateral is insufficient to discharge the debt in full. Non-accrual loans may be considered for return to accrual status after a minimum six-month period of on-time payment performance provided that no amount of the loan has been charged-off. Past due status is based on the contractual terms of the loan. If collection of principal is evaluated as doubtful, all payments are applied to principal.

Loans are individually evaluated when they do not share similar risk characteristics with other loans collectively evaluated (generally collateral dependent), and when, based on current information, management considers it unlikely that the collection of principal and interest payments on these loans will be made according to contractual terms. Generally, loans are reviewed for individual evaluation 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 modified due to a borrower experiencing financial difficulty.

The allowance for credit losses on loans is a valuation account that is deducted from the amortized cost basis of loans to present the net amount expected to be collected on the loans. Expected credit losses are estimated over the contractual term of the loans, adjusted for expected prepayments when appropriate. Credit losses on loans are charged against the allowance for credit losses on loans when management believes the uncollectability of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance for credit losses on loans.

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements

1. Summary of Significant Accounting Policies - continued

Management estimates the required allowance for credit losses on loans using relevant available information, from internal and external sources, relating to past events, current conditions, and reasonable and supportable forecasts. Historical credit loss experience (past events) provides the basis for the estimation of expected credit losses. Adjustments to historical loss information are made for differences in current conditions such as differences relating to underwriting standards, nature and volume of the loan portfolio, delinquency level and overall loan portfolio quality, or term as well as for changes in environmental conditions, such as changes in economic conditions that may affect the borrower's ability to pay, unemployment rates, property values, or other relevant factors. If the current economy or real estate market were to suffer a severe downturn, the provision for credit losses on loans would need to be increased.

The allowance for credit losses on loans is measured on a collective (pool) basis when similar risk characteristics exist. The Bank has identified portfolio segments based on collateral type and measures the allowance for credit losses on loans using Call Report-derived data. The Bank utilizes the discounted cash flow approach to calculate the expected loss for each loan within the pool. The Bank also considers qualitative adjustments to the historical loss rate for each loan portfolio segment, which are a combination of specific risk characteristics or current conditions at the reporting date that may differ from those in effect during the historical loss calculation period as well as forward looking projections for each pool based on a reasonable and supportable forecast based on objective economic data (primarily Federal Reserve Economic Data). The Bank uses a one-year forecast period, after which the loss factors revert to historical loss rates straight-line over four quarters. The total loss rate is the lifetime historical loss rate plus the total qualitative factor adjustments.

Some loans are not sufficiently similar in risk characteristics to other loans. These loans are evaluated on an individual basis. Loans evaluated individually are not included in the collective evaluation. Loans that are individually evaluated for which a potential for credit loss is determined to exist will have a specific reserve allocated to them and included in the allowance for credit losses on loans.

An unallocated component may be maintained to cover uncertainties that could affect management's estimate of probable expected losses. The unallocated component of the allowance for credit losses on loans reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating specific and general expected losses in the loan portfolio. Allocation of a portion of the allowance for credit losses on loans to one category of loans does not preclude its availability to absorb expected losses in other categories.

Allowance for credit losses on off-balance sheet items

The Bank estimates expected credit losses on off-balance sheet items, which consist of contractual obligations to extend credit, loans which the Bank has approved but have not been funded, and letters of credit, over the contractual period during which the Bank is exposed to credit risk, unless that obligation is unconditionally cancellable by the Bank. The allowance for credit losses on off-balance sheet items is recorded as a liability and is adjusted each reporting period through credit loss expense. The estimate includes consideration of the likelihood that funding will occur and an estimate of expected credit losses on off-balance sheet items expected to be funded over its estimated life. The loss rates used to determine the required allowance for credit losses on off-balance sheet items are essentially the same as those used on originated loans.

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 using the straight-line method over three years.

Other real estate owned and other repossessed assets

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

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements

1. Summary of Significant Accounting Policies - continued

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 consolidated 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.

Net income per common share

Basic net income 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 net income per common share is computed using the weighted-average number of common shares determined for the basic net income per common share computation plus the dilutive effect of common stock equivalents using the treasury stock method.

Stock-based compensation

The Bank accounts for 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 FASB Accounting Standards Codification ("ASC") Topic 718, *Stock Compensation*. This standard requires public companies to recognize compensation expense related to stock-based compensation awards in their statements of income 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 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.

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.

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements

3. Investment Securities Held to Maturity

The amortized cost and estimated fair value of the investment securities portfolio for the respective periods are shown below. The Bank owns residential mortgage-backed (“RMBS”), commercial mortgage-backed (“CMBS”) and collateralized mortgage obligation (“CMO”) investment securities which are 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 U.S. Small Business Administration (“SBA”).

	Amortized Cost	Gross Unrealized Gains	Losses	Fair Value
March 31, 2024				
U.S. Treasury securities	\$ 14,334,767	\$ -	\$ 684,977	\$ 13,649,790
U.S. government agency securities	33,595,942	-	2,402,596	31,193,346
Agency RMBS	34,157,136	-	3,978,000	30,179,136
Agency CMBS	4,191,342	-	193,265	3,998,077
Agency CMO securities	1,127,602	-	224,761	902,841
SBA asset-backed securities	9,804,223	-	1,120,787	8,683,436
State and municipal securities	3,551,811	-	605,725	2,946,086
	<u>\$ 100,762,823</u>	<u>\$ -</u>	<u>\$ 9,210,111</u>	<u>\$ 91,552,712</u>
December 31, 2023				
U.S. Treasury securities	\$ 17,344,342	\$ -	\$ 745,822	\$ 16,598,520
U.S. government agency securities	34,628,737	-	2,397,944	32,230,793
Agency RMBS	35,421,663	21,776	3,712,966	31,730,473
Agency CMBS	4,202,121	-	165,799	4,036,322
Agency CMO securities	1,154,204	-	215,050	939,154
SBA asset-backed securities	10,189,248	-	1,052,893	9,136,355
State and municipal securities	3,555,591	-	571,766	2,983,825
	<u>\$ 106,495,906</u>	<u>\$ 21,776</u>	<u>\$ 8,862,240</u>	<u>\$ 97,655,442</u>

Contractual maturities and the amount of pledged investment securities for the respective periods are shown below. Actual maturities might differ from contractual maturities because the issuers of the securities might 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.

	March 31, 2024		December 31, 2023	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Maturing in one year or less	\$ 21,631,172	\$ 21,065,134	\$ 16,651,013	\$ 16,305,486
Maturing over one to five years	20,149,035	18,494,143	29,175,581	27,169,485
Maturing over five to ten years	4,742,815	3,934,848	4,743,155	3,994,957
Maturing over ten years	4,959,498	4,295,097	4,958,921	4,343,210
Mortgage-backed, CMO and asset-backed securities	49,280,303	43,763,490	50,967,236	45,842,304
	<u>\$ 100,762,823</u>	<u>\$ 91,552,712</u>	<u>\$ 106,495,906</u>	<u>\$ 97,655,442</u>
Pledged securities	<u>\$ 75,675,562</u>	<u>\$ 68,032,817</u>	<u>\$ 79,710,044</u>	<u>\$ 72,118,271</u>

The following table displays the amortized cost of held to maturity state and municipal securities by credit rating provided by Moody’s at March 31, 2024 and December 31, 2023.

March 31, 2024	AAA	AA2	AA3	Below AA3	Total
State and municipal securities	<u>\$ 1,457,968</u>	<u>\$ 747,167</u>	<u>\$ 1,346,676</u>	<u>\$ -</u>	<u>\$ 3,551,811</u>
December 31, 2023	AAA	AA2	AA3	Below AA3	Total
State and municipal securities	<u>\$ 1,460,729</u>	<u>\$ 747,626</u>	<u>\$ 1,347,236</u>	<u>\$ -</u>	<u>\$ 3,555,591</u>

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements

3. Investment Securities Held to Maturity - continued

The following table presents unrealized losses and related fair values in the investment portfolio by investment classification, aggregated by the length of time that individual securities have been in a continuous unrealized loss position as of March 31, 2024 and December 31, 2023.

	Less than 12 Months		12 Months or Longer		Total	
	Fair	Gross	Fair	Gross	Fair	Gross
	Value	Unrealized	Value	Unrealized	Value	Unrealized
		Losses		Losses		Losses
March 31, 2024						
U.S. Treasury securities	\$ -	\$ -	\$ 13,649,790	\$ 684,977	\$ 13,649,790	\$ 684,977
U.S. government agency securities	-	-	31,193,346	2,402,596	31,193,346	2,402,596
Agency RMBS	2,911,650	13,751	27,267,486	3,964,249	30,179,136	3,978,000
Agency CMBS	-	-	3,998,077	193,265	3,998,077	193,265
Agency CMO securities	-	-	902,841	224,761	902,841	224,761
SBA asset-backed securities	-	-	8,683,436	1,120,787	8,683,436	1,120,787
State and municipal securities	-	-	2,946,086	605,725	2,946,086	605,725
	<u>\$ 2,911,650</u>	<u>\$ 13,751</u>	<u>\$ 88,641,062</u>	<u>\$ 9,196,360</u>	<u>\$ 91,552,712</u>	<u>\$ 9,210,111</u>
December 31, 2023						
U.S. Treasury securities	\$ -	\$ -	\$ 16,598,520	\$ 745,822	\$ 16,598,520	\$ 745,822
U.S. government agency securities	-	-	32,230,793	2,397,944	32,230,793	2,397,944
Agency RMBS	-	-	28,665,703	3,712,966	28,665,703	3,712,966
Agency CMBS	-	-	4,036,322	165,799	4,036,322	165,799
Agency CMO securities	-	-	939,154	215,050	939,154	215,050
SBA asset-backed securities	-	-	9,136,355	1,052,893	9,136,355	1,052,893
State and municipal securities	-	-	2,983,825	571,766	2,983,825	571,766
	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 94,590,672</u>	<u>\$ 8,862,240</u>	<u>\$ 94,590,672</u>	<u>\$ 8,862,240</u>

Based on its review of investment securities experiencing unrealized losses as of March 31, 2024 and December 31, 2023, the Bank concluded that it expected to recover the amortized cost basis of its investment. The Bank has the intent and ability to hold and does not believe it will be required to sell these investment securities until maturity. Unrealized losses are primarily due to increases in market interest rates over the yields available at the time the underlying investments were purchased, and the Bank does not believe that any of the securities are experiencing unrealized losses due to reasons of credit quality. 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. Treasury securities the Bank owns are backed by the full faith and credit of the U.S. government. 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 FHLB and the Federal Farm Credit system ("FFCB"), which are government-sponsored enterprises. The RMBS, CMBS and CMO 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.

As part of implementing ASU 2016-13 on January 1, 2023, the Bank determined that no allowance for credit losses was required on the Bank's investment portfolio. The securities owned by the Bank that are issued by the U.S. Treasury, the SBA, and U.S. government agencies, including agency MBS and CMO securities, are either explicitly or implicitly guaranteed by the U.S. government, are highly rated by major rating agencies and have a long history of no credit losses. The state and municipal securities owned by the Bank are general obligation bonds, highly rated by major rating agencies and have a long history of no credit losses. Based on management's assessment of the investment portfolio at March 31, 2024 and December 31, 2023, no allowance for credit losses was required on the Bank's investment portfolio.

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements

4. Loans

The Bank makes loans to customers located primarily in Harford and Cecil Counties and 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:

At:	March 31, 2024	December 31, 2023
Real estate		
Construction, development & other land	\$ 31,339,262	\$ 31,970,782
Secured by farmland	8,645,879	8,778,243
Commercial	253,212,530	254,009,724
Residential	135,127,371	134,764,915
Commercial & industrial	50,148,987	46,110,314
Other consumer	31,571,416	32,515,311
Overdrafts	52,541	68,905
Gross loans	510,097,986	508,218,194
Net deferred (fees) costs	(245,190)	(258,437)
Allowance for credit losses on loans	(5,732,497)	(5,709,827)
Net loans	<u>\$ 504,120,299</u>	<u>\$ 502,249,930</u>
Principal balance of pledged loans	<u>\$ 236,851,801</u>	<u>\$ 237,539,310</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 based on the property's value and debt service coverage ratios, and additional collateral may be required under certain circumstances. The Bank will generally obtain personal guarantees.

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.

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 10 to 30 years. Fixed-rate lending can expose the Bank to interest rate risk in a rising rate environment.

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

The Bank makes consumer installment loans secured by vehicles, boats, mobile homes and other collateral as well as unsecured loans with personal guarantees.

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.

Loan balances in the following tables are presented at recorded investment, which is unpaid principal balance adjusted for any interest amounts applied to principal on nonaccrual loans, and any amounts partially charged-off.

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements

4. Loans - continued

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

At:	March 31, 2024	December 31, 2023
<i>Maturing</i>		
In one year or less	\$ 58,787,796	\$ 47,019,846
After one year to five years	44,189,460	49,089,535
After five years to fifteen years	121,226,164	123,855,668
After fifteen years	285,894,566	288,253,145
Gross loans	<u>\$ 510,097,986</u>	<u>\$ 508,218,194</u>
Variable rate loans included above	<u>\$ 345,826,561</u>	<u>\$ 342,518,513</u>

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

	30-59 Days Past Due	60-89 Days Past Due	90 Days and Over Past Due	Total Past Due	Current	Total Loans	Loans over 90 Days and Accruing
March 31, 2024							
Construction, development & other land	\$ -	\$ -	\$ -	\$ -	\$ 31,339,262	\$ 31,339,262	\$ -
Commercial real estate & farmland	232,340	29,842	-	262,182	261,596,227	261,858,409	-
Residential real estate	-	32,576	-	32,576	135,094,795	135,127,371	-
Commercial & industrial	-	-	-	-	50,148,987	50,148,987	-
Other consumer & overdrafts	76,698	-	-	76,698	31,547,259	31,623,957	-
Total	<u>\$ 309,038</u>	<u>\$ 62,418</u>	<u>\$ -</u>	<u>\$ 371,456</u>	<u>\$ 509,726,530</u>	<u>\$ 510,097,986</u>	<u>\$ -</u>
December 31, 2023							
Construction, development & other land	\$ -	\$ -	\$ -	\$ -	\$ 31,970,782	\$ 31,970,782	\$ -
Commercial real estate & farmland	248,258	-	-	248,258	262,539,709	262,787,967	-
Residential real estate	35,286	-	-	35,286	134,729,629	134,764,915	-
Commercial & industrial	-	102,139	-	102,139	46,008,175	46,110,314	-
Other consumer & overdrafts	144,576	-	-	144,576	32,439,640	32,584,216	-
Total	<u>\$ 428,120</u>	<u>\$ 102,139</u>	<u>\$ -</u>	<u>\$ 530,259</u>	<u>\$ 507,687,935</u>	<u>\$ 508,218,194</u>	<u>\$ -</u>

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, 3 and 4 – These grades include “pass grade” loans to borrowers of acceptable credit quality and risk.

Grade 5 – This grade includes loans that are on management's “watch list” and are classified as “Pass Watch”. Loans with this grade are at the lower end of the acceptable quality range that exhibit weaknesses that require closer oversight and attention. 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 6 – 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 7 – 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.

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements

4. Loans - continued

Consumer loans will be assigned a loan grade of 7, substandard, when placed on non-accrual or when experiencing significant, protracted delinquency.

The following table presents loan grades applied at March 31, 2024 to the various loan classes by year of origination.

	Term Loans by Origination Year						Revolving	
	2024	2023	2022	2021	2020	Prior	Loans	Total
Construction, development & other land:								
Loan grades:								
Pass	\$ 1,356,902	\$ 2,572,350	\$ 3,856,317	\$ 1,814,452	\$ 2,439,715	\$ 1,170,779	\$ 8,471,852	\$ 21,682,367
Pass watch	-	-	6,585,409	-	-	143,976	2,927,510	9,656,895
Special mention	-	-	-	-	-	-	-	-
Substandard	-	-	-	-	-	-	-	-
	<u>\$ 1,356,902</u>	<u>\$ 2,572,350</u>	<u>\$ 10,441,726</u>	<u>\$ 1,814,452</u>	<u>\$ 2,439,715</u>	<u>\$ 1,314,755</u>	<u>\$ 11,399,362</u>	<u>\$ 31,339,262</u>
Commercial real estate & farmland:								
Loan grades:								
Pass	\$ 1,682,314	\$ 34,812,572	\$ 45,062,901	\$ 29,637,760	\$ 22,996,752	\$ 79,979,975	\$ 6,403,552	\$ 220,575,826
Pass watch	-	5,588,502	3,644,475	51,413	-	16,445,223	31,935	25,761,548
Special mention	-	1,941,430	4,471,917	-	-	644,029	837,000	7,894,376
Substandard	-	-	349,436	-	-	7,277,223	-	7,626,659
	<u>\$ 1,682,314</u>	<u>\$ 42,342,504</u>	<u>\$ 53,528,729</u>	<u>\$ 29,689,173</u>	<u>\$ 22,996,752</u>	<u>\$ 104,346,450</u>	<u>\$ 7,272,487</u>	<u>\$ 261,858,409</u>
Residential real estate:								
Loan grades:								
Pass	\$ 1,618,283	\$ 15,482,365	\$ 33,707,959	\$ 20,769,533	\$ 15,973,274	\$ 27,489,545	\$ 17,888,856	\$ 132,929,815
Pass watch	-	450,005	231,884	-	-	881,074	354,761	1,917,724
Special mention	-	-	-	-	-	-	-	-
Substandard	-	-	-	-	-	279,832	-	279,832
	<u>\$ 1,618,283</u>	<u>\$ 15,932,370</u>	<u>\$ 33,939,843</u>	<u>\$ 20,769,533</u>	<u>\$ 15,973,274</u>	<u>\$ 28,650,451</u>	<u>\$ 18,243,617</u>	<u>\$ 135,127,371</u>
Commercial & industrial:								
Loan grades:								
Pass	\$ 5,672,777	\$ 13,043,363	\$ 6,455,247	\$ 3,546,487	\$ 1,655,588	\$ 784,663	\$ 15,278,256	\$ 46,436,381
Pass watch	-	540,132	565,736	212,662	67,905	61,016	1,085,725	2,533,176
Special mention	-	918,823	-	-	-	-	130,000	1,048,823
Substandard	-	-	-	-	-	130,607	-	130,607
	<u>\$ 5,672,777</u>	<u>\$ 14,502,318</u>	<u>\$ 7,020,983</u>	<u>\$ 3,759,149</u>	<u>\$ 1,723,493</u>	<u>\$ 976,286</u>	<u>\$ 16,493,981</u>	<u>\$ 50,148,987</u>
Other consumer & overdrafts:								
Loan grades:								
Pass	\$ 287,329	\$ 18,747,022	\$ 9,583,598	\$ 820,262	\$ 323,954	\$ 1,812,361	\$ 25,853	\$ 31,600,379
Pass watch	-	-	-	22,506	-	-	-	22,506
Special mention	-	-	-	-	-	-	-	-
Substandard	-	-	-	-	-	1,072	-	1,072
	<u>\$ 287,329</u>	<u>\$ 18,747,022</u>	<u>\$ 9,583,598</u>	<u>\$ 842,768</u>	<u>\$ 323,954</u>	<u>\$ 1,813,433</u>	<u>\$ 25,853</u>	<u>\$ 31,623,957</u>
Total loans:								
Loan grades:								
Pass	\$ 10,617,605	\$ 84,657,672	\$ 98,666,022	\$ 56,588,494	\$ 43,389,283	\$ 111,237,323	\$ 48,068,369	\$ 453,224,768
Pass watch	-	6,578,639	11,027,504	286,581	67,905	17,531,289	4,399,931	39,891,849
Special mention	-	2,860,253	4,471,917	-	-	644,029	967,000	8,943,199
Substandard	-	-	349,436	-	-	7,688,734	-	8,038,170
	<u>\$ 10,617,605</u>	<u>\$ 94,096,564</u>	<u>\$ 114,514,879</u>	<u>\$ 56,875,075</u>	<u>\$ 43,457,188</u>	<u>\$ 137,101,375</u>	<u>\$ 53,435,300</u>	<u>\$ 510,097,986</u>

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements

4. Loans - continued

The following table presents loan grades applied at December 31, 2023 to the various loan classes by year of origination.

	Term Loans by Origination Year						Revolving	
	2023	2022	2021	2020	2019	Prior	Loans	Total
Construction, development & other land:								
Loan grades:								
Pass	\$ 2,781,372	\$ 10,537,184	\$ 1,824,608	\$ 2,439,715	\$ 2,654,533	\$ 1,188,019	\$ 7,913,718	\$ 29,339,149
Pass watch	-	-	-	-	144,936	-	2,486,697	2,631,633
Special mention	-	-	-	-	-	-	-	-
Substandard	-	-	-	-	-	-	-	-
	<u>\$ 2,781,372</u>	<u>\$ 10,537,184</u>	<u>\$ 1,824,608</u>	<u>\$ 2,439,715</u>	<u>\$ 2,799,469</u>	<u>\$ 1,188,019</u>	<u>\$ 10,400,415</u>	<u>\$ 31,970,782</u>
Commercial real estate & farmland:								
Loan grades:								
Pass	\$ 32,119,949	\$ 45,474,176	\$ 29,928,703	\$ 23,970,913	\$ 8,873,353	\$ 73,165,460	\$ 6,395,354	\$ 219,927,908
Pass watch	5,619,830	3,665,584	51,884	-	6,778,578	9,900,469	34,126	26,050,471
Special mention	1,481,191	4,486,747	-	-	-	796,354	826,866	7,591,158
Substandard	-	364,217	-	1,054,962	361,943	7,437,308	-	9,218,430
	<u>\$ 39,220,970</u>	<u>\$ 53,990,724</u>	<u>\$ 29,980,587</u>	<u>\$ 25,025,875</u>	<u>\$ 16,013,874</u>	<u>\$ 91,299,591</u>	<u>\$ 7,256,346</u>	<u>\$ 262,787,967</u>
Residential real estate:								
Loan grades:								
Pass	\$ 16,282,297	\$ 34,094,140	\$ 21,596,604	\$ 16,185,608	\$ 7,716,348	\$ 20,062,078	\$ 16,495,701	\$ 132,432,776
Pass watch	453,938	232,659	-	-	-	898,679	321,362	1,906,638
Special mention	-	-	-	-	-	-	-	-
Substandard	-	96,229	-	-	-	329,272	-	425,501
	<u>\$ 16,736,235</u>	<u>\$ 34,423,028</u>	<u>\$ 21,596,604</u>	<u>\$ 16,185,608</u>	<u>\$ 7,716,348</u>	<u>\$ 21,290,029</u>	<u>\$ 16,817,063</u>	<u>\$ 134,764,915</u>
Commercial & industrial:								
Loan grades:								
Pass	\$ 15,566,106	\$ 7,031,069	\$ 3,966,822	\$ 1,844,446	\$ 494,306	\$ 497,177	\$ 12,620,938	\$ 42,020,864
Pass watch	566,012	601,348	228,511	117,993	7,106	73,211	1,224,191	2,818,372
Special mention	927,235	-	-	-	-	-	110,000	1,037,235
Substandard	-	-	102,139	-	48,487	83,217	-	233,843
	<u>\$ 17,059,353</u>	<u>\$ 7,632,417</u>	<u>\$ 4,297,472</u>	<u>\$ 1,962,439</u>	<u>\$ 549,899</u>	<u>\$ 653,605</u>	<u>\$ 13,955,129</u>	<u>\$ 46,110,314</u>
Other consumer & overdrafts:								
Loan grades:								
Pass	\$ 19,028,578	\$ 10,145,493	\$ 972,908	\$ 389,502	\$ 256,772	\$ 1,732,235	\$ 29,664	\$ 32,555,152
Pass watch	-	-	24,812	-	-	-	-	24,812
Special mention	-	-	-	-	-	-	-	-
Substandard	-	-	-	-	-	4,252	-	4,252
	<u>\$ 19,028,578</u>	<u>\$ 10,145,493</u>	<u>\$ 997,720</u>	<u>\$ 389,502</u>	<u>\$ 256,772</u>	<u>\$ 1,736,487</u>	<u>\$ 29,664</u>	<u>\$ 32,584,216</u>
Total loans:								
Loan grades:								
Pass	\$ 85,778,302	\$ 107,282,062	\$ 58,289,645	\$ 44,830,184	\$ 19,995,312	\$ 96,644,969	\$ 43,455,375	\$ 456,275,849
Pass watch	6,639,780	4,499,591	305,207	117,993	6,930,620	10,872,359	4,066,376	33,431,926
Special mention	2,408,426	4,486,747	-	-	-	796,354	936,866	8,628,393
Substandard	-	460,446	102,139	1,054,962	410,430	7,854,049	-	9,882,026
	<u>\$ 94,826,508</u>	<u>\$ 116,728,846</u>	<u>\$ 58,696,991</u>	<u>\$ 46,003,139</u>	<u>\$ 27,336,362</u>	<u>\$ 116,167,731</u>	<u>\$ 48,458,617</u>	<u>\$ 508,218,194</u>

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements

4. Loans - continued

The following table presents gross charge-offs allocated by loan class by year of origination for the three-month periods ended March 31, 2024 and 2023. All charge-offs reported in overdrafts for the three-month periods ended March 31, 2024 and 2023 were related to deposit overdrafts.

	Three Months Ended March 31, 2024 by Year of Origination						
	2024	2023	2022	2021	2020	Prior	Total
Construction, development & other land	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Commercial real estate & farmland	-	-	-	-	-	-	-
Residential real estate	-	-	-	-	-	-	-
Commercial & industrial	-	-	-	-	-	-	-
Other consumer	-	-	-	-	-	-	-
Overdrafts	10,991	-	-	-	-	-	10,991
	<u>\$ 10,991</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 10,991</u>

	Three Months Ended March 31, 2023 by Year of Origination						
	2023	2022	2021	2020	2019	Prior	Total
Construction, development & other land	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Commercial real estate & farmland	-	-	-	-	-	-	-
Residential real estate	-	-	-	-	-	766	766
Commercial & industrial	-	-	-	-	-	-	-
Other consumer	-	-	-	-	-	-	-
Overdrafts	4,765	-	-	-	-	-	4,765
	<u>\$ 4,765</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 766</u>	<u>\$ 5,531</u>

The following table provides a comprehensive view of the allowance for credit losses on loans activity including the periodic activity of charge-offs and recoveries allocated by loan class for the three-month periods ended March 31, 2024 and 2023.

Three months ended:		Construction, Development & Other Land	Commercial Real Estate & Farmland	Residential Real Estate	Commercial & Industrial	Other Consumer & Overdrafts	Total
March 31, 2024	Unallocated						
Allowance for credit losses on loans:							
Beginning balance	\$ 8,660	\$ 665,816	\$ 2,086,568	\$ 1,460,185	\$ 895,946	\$ 592,652	\$ 5,709,827
Charge-offs	-	-	-	-	-	(10,991)	(10,991)
Recoveries	-	-	-	2,000	-	1,661	3,661
Provision for (recovery of) credit losses on loans	2,248	18,125	(64,681)	1,862	82,640	(10,194)	30,000
Ending balance	<u>\$ 10,908</u>	<u>\$ 683,941</u>	<u>\$ 2,021,887</u>	<u>\$ 1,464,047</u>	<u>\$ 978,586</u>	<u>\$ 573,128</u>	<u>\$ 5,732,497</u>
March 31, 2023							
Allowance for credit losses on loans:							
Beginning balance	\$ 13,670	\$ 446,024	\$ 2,550,667	\$ 986,573	\$ 452,861	\$ 245,973	\$ 4,695,768
Impact of ASC 326 adoption	(13,670)	(112,669)	97,825	219,576	(146,758)	162,017	206,321
Charge-offs	-	-	-	(766)	-	(4,765)	(5,531)
Recoveries	-	-	-	1,000	-	1,325	2,325
Provision for (recovery of) credit losses on loans	-	31,792	(118,417)	46,540	62,279	150,267	172,461
Ending balance	<u>\$ -</u>	<u>\$ 365,147</u>	<u>\$ 2,530,075</u>	<u>\$ 1,252,923</u>	<u>\$ 368,382</u>	<u>\$ 554,817</u>	<u>\$ 5,071,344</u>

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements

4. Loans - continued

The following table presents the allocation of allowance for credit losses on loans and the balances of loans that were individually and collectively evaluated for impairment at March 31, 2024 and December 31, 2023, and the loan balances by loan class for loans that were individually and collectively evaluated at March 31, 2024 and December 31, 2023.

		Construction, Development & Other Land	Commercial Real Estate & Farmland	Residential Real Estate	Commercial & Industrial	Other Consumer & Overdrafts	Total
March 31, 2024	Unallocated						
Allowance balance allocated to loans:							
Individually evaluated	\$ -	\$ -	\$ -	\$ -	\$ 2,565	\$ -	\$ 2,565
Collectively evaluated	10,908	683,941	2,021,887	1,464,047	976,021	573,128	5,729,932
	<u>\$ 10,908</u>	<u>\$ 683,941</u>	<u>\$ 2,021,887</u>	<u>\$ 1,464,047</u>	<u>\$ 978,586</u>	<u>\$ 573,128</u>	<u>\$ 5,732,497</u>
Loan balances:							
Individually evaluated		\$ -	\$ 6,797,192	\$ 154,058	\$ 130,607	\$ 1,071	\$ 7,082,928
Collectively evaluated		31,339,262	255,061,217	134,973,313	50,018,380	31,622,886	503,015,058
		<u>\$ 31,339,262</u>	<u>\$ 261,858,409</u>	<u>\$ 135,127,371</u>	<u>\$ 50,148,987</u>	<u>\$ 31,623,957</u>	<u>\$ 510,097,986</u>
December 31, 2023							
Allowance balance allocated to loans:							
Individually evaluated	\$ -	\$ -	\$ 56,000	\$ -	\$ 2,587	\$ -	\$ 58,587
Collectively evaluated	8,660	665,816	2,030,568	1,460,185	893,359	592,652	5,651,240
	<u>\$ 8,660</u>	<u>\$ 665,816</u>	<u>\$ 2,086,568</u>	<u>\$ 1,460,185</u>	<u>\$ 895,946</u>	<u>\$ 592,652</u>	<u>\$ 5,709,827</u>
Loan balances:							
Individually evaluated		\$ -	\$ 8,381,335	\$ 293,870	\$ 233,843	\$ 4,252	\$ 8,913,300
Collectively evaluated		31,970,782	254,406,632	134,471,045	45,876,471	32,579,964	499,304,894
		<u>\$ 31,970,782</u>	<u>\$ 262,787,967</u>	<u>\$ 134,764,915</u>	<u>\$ 46,110,314</u>	<u>\$ 32,584,216</u>	<u>\$ 508,218,194</u>

The following table presents the unpaid principal balance and the recorded investment of individually evaluated collateral dependent loans by class of loans for the periods indicated.

	Recorded Investment	Unpaid Principal Balance	Related Allowance
March 31, 2024			
Construction, development & other land	\$ -	\$ -	\$ -
Commercial real estate & farmland	6,797,192	7,943,172	-
Residential real estate	154,058	377,105	-
Commercial & industrial	-	-	-
Other consumer	1,071	33,024	-
	<u>\$ 6,952,321</u>	<u>\$ 8,353,301</u>	<u>\$ -</u>
December 31, 2023			
Construction, development & other land	\$ -	\$ -	\$ -
Commercial real estate & farmland	8,381,335	9,450,614	56,000
Residential real estate	293,870	513,973	-
Commercial & industrial	102,140	102,140	-
Other consumer	4,252	44,159	-
	<u>\$ 8,781,597</u>	<u>\$ 10,110,886</u>	<u>\$ 56,000</u>

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements

4. Loans - continued

From time to time, the Bank may modify certain loans to borrowers who are experiencing financial difficulty. In some cases, these modifications may result in new loans. Loan modifications to borrowers experiencing financial difficulty may be in the form of a term extension, an other-than-insignificant payment delay, an interest rate reduction, principal forgiveness, or a combination thereof, among other things.

Information as of or for the three-month periods ended March 31, 2024 and March 31, 2023, related to loans modified (by type of modification) for borrowers experiencing financial difficulty at the time of modification, is set forth in the following table.

	Term Extension	Payment Delay	Interest Rate Reduction	Principal Forgiveness	Combination Thereof	Total	Total Class of Loans
March 31, 2024							
Commercial real estate & farmland	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	-
March 31, 2023							
Commercial real estate & farmland	\$ -	\$ -	\$ -	\$ -	\$ 4,078,793	\$ 4,078,793	1.77%

There were no loans that the Bank modified in the 12 months preceding the three-month period ended March 31, 2024 for which there was a payment default during the 12-month period ended March 31, 2024. There were no loans that the Bank modified in the 12 months preceding the three-month period ended March 31, 2023 for which there was a payment default during the 12-month period ended March 31, 2023. Payment default is defined as any time the loan was more than 90 days past due or out of compliance with the modification agreement.

The following table summarizes non-accrual loans at March 31, 2024 and December 31, 2023.

	Non-accrual With No ACL Allocated	Non-accrual With ACL Allocated	Total Non-accrual	Loans Past Due Over 90 Days And Accruing	Total Non-performing Loans	ACL on Non-accrual Loans
March 31, 2024						
Commercial real estate & farmland	\$ 6,206,095	\$ -	\$ 6,206,095	\$ -	\$ 6,206,095	\$ -
Residential real estate	47,774	-	47,774	-	47,774	-
Commercial & industrial	-	-	-	-	-	-
Other consumer	1,071	-	1,071	-	1,071	-
Total	\$ 6,254,940	\$ -	\$ 6,254,940	\$ -	\$ 6,254,940	\$ -
December 31, 2023						
Commercial real estate & farmland	\$ 2,358,864	\$ 4,003,577	\$ 6,362,441	\$ -	\$ 6,362,441	\$ 56,000
Residential real estate	53,592	-	53,592	-	53,592	-
Commercial & industrial	102,139	-	102,139	-	102,139	-
Other consumer	4,252	-	4,252	-	4,252	-
Total	\$ 2,518,847	\$ 4,003,577	\$ 6,522,424	\$ -	\$ 6,522,424	\$ 56,000

The following table shows the amount of gross interest income that would have been recorded during the three-month periods ended March 31, 2024 and 2023 had the non-accrual loans been current and performing according to terms.

	March 31, 2024	March 31, 2023
Interest not accrued on non-accrual loans	\$ 79,804	\$ 32,698

There were no consumer mortgage loans secured by residential real estate that were in the process of foreclosure as of March 31, 2024.

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements

5. Credit Commitments

Loan commitments, unused lines of credit, and letters of credit outstanding at the respective dates are as follows:

At:	March 31, 2024	December 31, 2023
Commitments to extend credit		
Loan origination commitments	\$ 6,425,730	\$ 4,238,000
Unused consumer real estate construction	1,088,575	1,405,896
Unused home equity lines of credit	18,672,081	19,010,398
Unused overdraft lines of credit	7,256,224	7,186,613
Unused commercial lines of credit	51,772,687	64,760,928
	<u>\$ 85,215,297</u>	<u>\$ 96,601,835</u>
Letters of credit	<u>\$ 2,960,764</u>	<u>\$ 3,321,199</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.

As part of implementing ASU 2016-13 on January 1, 2023, the Bank created an allowance for credit losses on off-balance sheet items related to these financial instruments with off-balance sheet risk, which is reported as a liability on the consolidated statements of condition. The liability excludes commitments for which the Bank can, at any time and for any reason, cancel its commitment to lend as unconditionally cancellable commitments do not require an allowance. The allowance for credit losses on off-balance sheet items was \$434,149 as of March 31, 2024. The allowance for credit losses on off-balance sheet items was \$506,650 as of December 31, 2023.

The following table presents activity in the allowance for credit losses on off-balance sheet items for the three-month periods ended March 31, 2024 and 2023.

For the three months ended:	March 31, 2024	March 31, 2023
Beginning balance	\$ 506,650	\$ -
Impact of ASU 2016-13 adoption	-	491,571
Provision for (recovery of) allowance for credit losses on off-balance sheet items	<u>(72,501)</u>	<u>(31,675)</u>
Ending balance	<u>\$ 434,149</u>	<u>\$ 459,896</u>

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements

6. Related Party Transactions

In the normal course of business, the Bank's officers and directors enter into loan transactions with the Bank. A summary of related party loan activity follows:

Year to Date Through:	March 31, 2024	December 31, 2023
Beginning balance	\$ 15,256,507	\$ 17,275,810
Advances	119,558	1,425,725
Payments	<u>(356,107)</u>	<u>(3,445,028)</u>
Ending balance	<u>\$ 15,019,958</u>	<u>\$ 15,256,507</u>

In addition to the outstanding balances listed above, the Bank's executive officers and directors and their related parties had \$3,783,721 in unused loans committed but not funded as of March 31, 2024. As of December 31, 2023, the Bank's executive officers and directors and their related parties had \$3,781,653 in unused loans committed but not funded.

The Bank obtains goods and services from firms of which owners are also members of the Bank's Board of Directors. Amounts paid to these related parties totaled \$3,240 during the three months ended March 31, 2024. Amounts paid to these related parties totaled \$2,900 during the three months ended March 31, 2023.

The Bank has a wealth management referral relationship with the firm of a director. The Bank recognized \$3,985 of income from the referral relationship in the three months ended March 31, 2024. The Bank recognized \$2,815 of income from the referral relationship in the three months ended March 31, 2023.

Deposits of the Bank's executive officers and directors and their related parties totaled \$8,189,166 at March 31, 2024. Deposits of the Bank's executive officers and directors and their related parties totaled \$10,336,866 at December 31, 2023.

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements

7. Bank Premises and Equipment

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

	Useful Lives	March 31, 2024	December 31, 2023
Land		\$ 2,815,916	\$ 2,815,916
Building and improvements	15 - 39 years	7,878,703	7,878,703
Leasehold improvements	5 - 19 years	594,844	588,014
Furniture, fixtures, and equipment	3 - 10 years	<u>2,699,326</u>	<u>2,682,934</u>
		13,988,789	13,965,567
Accumulated depreciation		<u>5,873,754</u>	<u>5,770,660</u>
Net bank premises and equipment		<u>\$ 8,115,035</u>	<u>\$ 8,194,907</u>

For the Three Months Ended:

	March 31, 2024	March 31, 2023
Depreciation expense	<u>\$ 122,081</u>	<u>\$ 135,364</u>

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

	Useful Life	March 31, 2024	December 31, 2023
Computer software	3 years	\$ 65,493	\$ 65,493
Accumulated amortization		<u>62,690</u>	<u>61,924</u>
Net computer software		<u>\$ 2,803</u>	<u>\$ 3,569</u>

For the Three Months Ended:

	March 31, 2024	March 31, 2023
Amortization expense	<u>\$ 766</u>	<u>\$ 1,562</u>

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements

8. Lease Commitments

The Bank leases certain banking facilities under operating leases expiring on various dates through 2026. At March 31, 2024, the Bank had lease liabilities totaling \$160,597 included in other liabilities and right-of-use lease assets totaling \$160,597 included in other assets related to these leases. At December 31, 2023, the Bank had lease liabilities totaling \$200,640 included in other liabilities and right-of-use lease assets totaling \$200,640 included in other assets related to these leases.

The weighted-average discount rate on operating lease balances outstanding at March 31, 2024 was 2.53%. The weighted-average discount rate on operating lease balances outstanding at December 31, 2023 was 2.39%. The weighted-average remaining lease term of operating leases outstanding at March 31, 2024 was 1.6 years. The weighted-average remaining lease term of operating leases outstanding at December 31, 2023 was 1.7 years.

Rent expense, consisting of lease payments plus common area maintenance and all other charges assessed by the lessor, for the three months ended March 31, 2024 was \$73,800. Rent expense, consisting of lease payments plus common area maintenance and all other charges assessed by the lessor, for the three months ended March 31, 2023 was \$55,686.

As of March 31, 2024, future minimum lease payments, by year and in the aggregate, of operating leases are as follows:

Year	Amount
2024	\$ 110,211
2025	47,339
2026	<u>27,614</u>
Total undiscounted lease payments	185,164
Discount on cash flows	<u>(24,567)</u>
Total lease liability	<u><u>\$ 160,597</u></u>

9. Borrowings and Available Lines of Credit

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 was required to purchase shares of capital stock in the FHLBA as a condition to obtaining the line of credit, and is required to hold stock based on borrowing activity.

FHLBA fixed-rate term borrowings are summarized as follows:

Maturity Date	Interest Rate	Interest Frequency	March 31, 2024	December 31, 2023
November 28, 2025	4.7800%	Quarterly	\$ 10,000,000	\$ 10,000,000
November 27, 2026	4.6105%	Quarterly	<u>7,000,000</u>	<u>7,000,000</u>
			<u><u>\$ 17,000,000</u></u>	<u><u>\$ 17,000,000</u></u>

FHLBA fixed-rate term borrowings as of March 31, 2024 will require principal repayments as follows:

Year	Principal Reduction
2025	\$ 10,000,000
2026	<u>7,000,000</u>
	<u><u>\$ 17,000,000</u></u>

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Notes to Consolidated Financial Statements

9. Borrowings and Available Lines of Credit - continued

In addition to the fixed-rate term borrowings, the Bank had \$25.25 million in FHLBA adjustable rate borrowings with no fixed maturity outstanding under the line of credit as of March 31, 2024, at an interest rate of 5.58%. The Bank had \$31.0 million in adjustable rate borrowings with no fixed maturity outstanding under the line of credit as of December 31, 2023, at an interest rate of 5.57%. Based on the value of available collateral remaining as of March 31, 2024, the Bank could borrow an additional \$69,280,294 from the FHLBA.

The Bank is eligible to borrow from the Federal Reserve Bank Discount Window. This credit line is secured by the Bank's consumer loan portfolio. Based on the value of available collateral as of March 31, 2024, the Bank could borrow \$14,047,208 from the Federal Reserve Bank 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 March 31, 2024, or \$67,836,566.

The Bank has a secured credit line and an unsecured credit line with a correspondent bank, which are subject to periodic review. Based on the most recent review performed by the correspondent bank, the amount available under the secured line is \$5,000,000 and the amount available under the unsecured line is \$3,000,000.

10. Retirement Plan

The Bank has a tax-qualified 401(k) and Profit Sharing Plan (the "401(k) Plan") which is available to employees who have reached the age of 20, have completed at least 90 days of service, and meet certain other eligibility requirements as defined by the Plan. The Bank makes matching contributions of 100% on the first 3% of compensation deferred, plus 50% on the next 2% of compensation deferred. Participants are immediately vested in the matching contributions made by the Bank, and discretionary profit sharing contributions, if any, will vest ratably over a six-year period beginning in year two.

For the three months ended March 31, 2024, the Bank recognized \$78,632 of expense associated with the 401(k) Plan. For the three months ended March 31, 2023, the Bank recognized \$76,564 of expense associated with the 401(k) Plan.

In 2006, and in the second quarter of 2017, the Bank entered into agreements under its Supplemental Executive Retirement Plans ("SERP") to certain executive officers providing 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 recorded a liability of \$1,126,105 related to these benefits at March 31, 2024. The Bank recorded a liability of \$1,133,875 related to these benefits at December 31, 2023. SERP expense for the three months ended March 31, 2024 was \$12,576. SERP expense for the three months ended March 31, 2023 was \$10,221.

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11. Interest-Bearing Deposits

Major classifications of interest-bearing deposits at:	March 31, 2024	December 31, 2023
Interest-bearing checking and Money Market	\$ 219,872,034	\$ 221,173,233
Savings	52,256,775	53,263,397
Certificates of deposit	158,923,470	133,955,979
	<u>\$ 431,052,279</u>	<u>\$ 408,392,609</u>
 Maturities of certificates of deposit at:	 March 31, 2024	 December 31, 2023
Maturing within twelve months	\$ 141,935,732	\$ 110,447,806
Maturing after one year to three years	14,000,300	20,406,817
Maturing after three years to five years	2,987,438	3,101,356
	<u>\$ 158,923,470</u>	<u>\$ 133,955,979</u>
 Certificates of deposit in excess of \$250,000 included above:	 <u>\$ 53,239,911</u>	 <u>\$ 42,875,315</u>
 Interest expense for the three months ended:	 March 31, 2024	 March 31, 2023
Interest-bearing checking and Money Market	\$ 538,793	\$ 126,559
Savings	28,924	36,430
Certificates of deposit	1,506,605	288,224
	<u>\$ 2,074,322</u>	<u>\$ 451,213</u>

12. Income Taxes

The components of income tax expense are as follows:

Year to date through:	March 31, 2024	March 31, 2023
Federal	\$ 406,945	\$ 400,126
State	109,387	138,720
	<u>\$ 516,332</u>	<u>\$ 538,846</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:	March 31, 2024	March 31, 2023
Statutory federal income tax rate	21.00 %	21.00 %
Increase (decrease) resulting from		
State income taxes, net of federal income tax benefit	4.09	5.19
Tax-exempt income	(0.82)	(0.84)
Nondeductible expenses	0.14	0.15
	<u>24.41 %</u>	<u>25.50 %</u>

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements

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 and have a 10-year exercise period. On April 9, 2015, a new director stock option plan with 80,000 shares authorized was approved by the Board of Directors to replace the director stock option plan which expired in 2014. 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. All remaining options in the officer plan are fully vested.

The total number of shares originally authorized for active director stock option plans and inactive director and officer plans with outstanding options was 249,890. At March 31, 2024, a total of 18,702 shares remain available for grant under the active director option plan.

A summary of stock option activity for the three months ended March 31, 2024 is presented in the following table.

Options	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value
Outstanding at January 1, 2024	62,993	\$ 27.39		
Options granted	-	-		
Options exercised	(2,142)	19.77		
Options forfeited or expired	-	-		
Outstanding at March 31, 2024	<u>60,851</u>	<u>\$ 27.66</u>	<u>5.50 years</u>	<u>\$ 281,457</u>
Exercisable at March 31, 2024	<u>60,851</u>	<u>\$ 27.66</u>	<u>5.50 years</u>	<u>\$ 281,457</u>

The intrinsic value of options exercised during the three months ended March 31, 2024 was \$26,948. The intrinsic value of options exercised during the three months ended March 31, 2023 was \$27,502.

For the three months ended March 31, 2024, the Bank recorded stock-based compensation expense of \$0. For the three months ended March 31, 2023, the Bank recorded stock-based compensation expense of \$0. As of March 31, 2024, there was no unrecognized stock-based compensation expense to be recognized in future periods.

At the annual meeting of stockholders held on May 20, 2020, the Bank's stockholders approved the Harford Bank 2020 Employee Stock Purchase Plan (the "2020 ESPP") that allows eligible employees to acquire up to 100,000 shares of the Bank's common stock at a discount through accumulated payroll deductions. The 2020 ESPP commenced on July 1, 2020.

A total of 580 shares of stock were sold at a weighted average price of \$30.56 pursuant to the 2020 ESPP for the three months ended March 31, 2024. A total of 647 shares of stock were sold at a weighted average price of \$30.54 pursuant to the 2020 ESPP for the three months ended March 31, 2023. At March 31, 2024, a total of 91,852 shares remain available for grant under the 2020 ESPP.

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Notes to Consolidated Financial Statements

14. Capital Standards

The Board of Governors of the Federal Reserve System (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 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 fully phased-in as of January 1, 2019, minimum requirements increased for both the quantity and quality of capital held by the Bank.

The rules included a new minimum Common Equity Tier 1 capital ratio (“CET1 ratio”) of 4.5% which, with the capital conservation buffer of 2.5% of risk-weighted assets added, effectively results in a minimum CET1 ratio of 7.0%. Basel III raised the minimum Tier 1 capital ratio from 4.0% to 6.0% which, with the capital conservation buffer of 2.5% of risk-weighted assets added, effectively results in a minimum Tier 1 capital ratio of 8.5%. Basel III maintained the minimum total capital ratio of 8.0%, which, with the capital conservation buffer of 2.5% of risk-weighted assets added, effectively results in a minimum Tier 1 capital ratio of 10.5%. Basel III maintained the minimum Tier 1 leverage capital ratio of 4.0%. Basel III also changed risk weights for certain assets and off-balance sheet exposures.

The capital conservation buffer is designed to absorb losses during periods of economic stress and, as detailed above, effectively increases the minimum required risk-weighted capital ratios. Banking institutions with a ratio of Common Equity Tier 1 capital to risk-weighted assets below the effective minimum (4.5% plus the capital conservation buffer) will face constraints on dividends, equity repurchases and compensation based on the amount of the shortfall and the institution's “eligible retained income” (that is, four quarter trailing net income, net of distributions and tax effects not reflected in net income).

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 credit losses on loans and the allowance for credit losses on off-balance sheet items. 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.

On September 17, 2019 the FDIC finalized a rule that introduced an optional simplified measure of capital adequacy for qualifying community banking organizations (i.e., the community bank leverage ratio framework, “CBLR framework”), as required by the Economic Growth, Regulatory Relief and Consumer Protection Act. The CBLR framework is designed to reduce burden by removing the requirements for calculating and reporting risk-based capital ratios for qualifying community banking organizations that opt into the framework. To qualify for the CBLR framework, a community banking organization must have a Tier 1 leverage ratio of at least 9 percent, less than \$10 billion in total consolidated assets, and limited amounts of off-balance-sheet exposures and trading assets and liabilities. A qualifying community banking organization that opts into the CBLR framework and meets all requirements under the framework will be considered to have met the well-capitalized ratio requirements under the Prompt Corrective Action regulations and will not be required to report or calculate risk-based capital. The Bank has elected not to opt into the CBLR framework at this time.

The federal banking agencies have provided community banking organizations the option to phase in the impact on regulatory capital of the adoption of ASU 2016-13, which was effective for the Bank on January 1, 2023. The Bank did not select the option to phase in the impact of ASU 2016-13 on regulatory capital.

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements

14. Capital Standards - continued

The Bank's actual capital ratios, the required regulatory capital ratios to be considered well capitalized, the regulatory minimum capital ratios, and the regulatory minimum capital ratios with the 2.5% capital conservation buffer added based on the Basel III Capital Rules are as follows for the periods indicated:

(\$ in thousands) March 31, 2024	Actual		Required to be Well Capitalized		Minimum Capital		Minimum Capital With Capital Conservation Buffer	
	Amount	Ratio	Amount	Ratio	Amount	Ratio	Amount	Ratio
Total capital	\$ 66,458	13.35%	\$ 49,797	10.00%	\$ 39,837	8.00%	\$ 52,287	10.50%
Tier 1 capital	60,291	12.11%	39,837	8.00%	29,878	6.00%	42,327	8.50%
Common equity Tier 1 capital	60,291	12.11%	32,368	6.50%	22,409	4.50%	34,858	7.00%
Tier 1 leverage capital	60,291	8.92%	33,798	5.00%	27,039	4.00%	27,039	4.00%

December 31, 2023	Actual		Required to be Well Capitalized		Minimum Capital		Minimum Capital With Capital Conservation Buffer	
	Amount	Ratio	Amount	Ratio	Amount	Ratio	Amount	Ratio
Total capital	\$ 65,179	13.11%	\$ 49,736	10.00%	\$ 39,789	8.00%	\$ 52,222	10.50%
Tier 1 capital	58,963	11.86%	39,789	8.00%	29,841	6.00%	42,275	8.50%
Common equity Tier 1 capital	58,963	11.86%	32,328	6.50%	22,381	4.50%	34,815	7.00%
Tier 1 leverage capital	58,963	8.96%	32,901	5.00%	26,321	4.00%	26,321	4.00%

At March 31, 2024 and December 31, 2023, 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 the Bank's 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.

15. Net Income per Common Share

The calculation of basic and diluted net income per common share is presented below for the periods indicated:

For the three months ended March 31:	2024	2023
Basic net income per common share :		
Net income	\$ 1,598,948	\$ 1,573,914
Weighted-average common shares outstanding	1,478,047	1,471,560
Basic net income per common share	<u>\$ 1.08</u>	<u>\$ 1.07</u>
Diluted net income per common share :		
Net income	\$ 1,598,948	\$ 1,573,914
Weighted-average common shares outstanding	1,478,047	1,471,560
Dilutive common stock equivalents	9,415	14,204
Dilutive shares	<u>1,487,462</u>	<u>1,485,764</u>
Diluted net income per common share	<u>\$ 1.07</u>	<u>\$ 1.06</u>
Anti-dilutive shares	<u>9,300</u>	<u>-</u>

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Notes to Consolidated Financial Statements

16. Fair Value Measurements

FASB ASC Topic 820 defines fair value as the price that would be received for an asset or paid to transfer a liability, in the principal or most advantageous market for the asset or liability, in an orderly transaction between market participants on the measurement date under current market conditions (an exit price) and 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.

During the periods ended March 31, 2024 and December 31, 2023, the Bank did not measure any assets or liabilities at fair value on a recurring basis.

The Bank does not record loans held for investment at fair value on a recurring basis. However, there were instances when a loan was individually evaluated and an allowance for credit losses on loans was established. The Bank measures impairment either based on the fair value of the collateral if the loan is collateral dependent or uses the present value of expected future cash flows discounted at the loan's effective interest rate, which was not a fair value measurement. The Bank maintains a valuation allowance to the extent that this measure of the individually evaluated loan was less than the recorded investment in the loan. When an individually evaluated loan is measured at fair value based solely on observable market prices or a current appraisal without further adjustment for unobservable inputs, the Bank records the individually evaluated loan as a nonrecurring fair value measurement classified as Level 2. However, if based on management's review, additional discounts to observed market prices or appraisals are required or if observable inputs are not available, the Bank records the individually evaluated loan as a nonrecurring fair value measurement classified as Level 3.

Individually evaluated loans that were measured based on expected future cash flows discounted at the loan's effective interest rate rather than the market rate of interest, were not recorded at fair value and are therefore excluded from fair value disclosure requirements.

The following table presents individually evaluated collateral dependent loans measured at fair value on a nonrecurring basis where the outstanding investment in the loan exceeded fair value resulting in an allowance being allocated to the loan at March 31, 2024 and December 31, 2023.

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
March 31, 2024				
Collateral dependent loans with ACL	\$ -	\$ -	\$ -	\$ -
December 31, 2023				
Collateral dependent loans with ACL	\$ -	\$ -	\$ 3,947,577	\$ 3,947,577

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Notes to Consolidated Financial Statements

16. Fair Value Measurements - continued

The fair value of the individually evaluated collateral dependent loans is measured based on the fair value of the collateral (less estimated selling costs). Appraised values may be discounted based on management's historical experience, changes in market conditions from the time of valuation, and/or management's expertise and knowledge of the client and client's business. Individually evaluated collateral dependent loans are reviewed and evaluated on a quarterly basis for individual reserve and adjusted accordingly, based on the factors identified above.

The following table presents qualitative information about Level 3 fair value measurements for individually evaluated collateral dependent loans where the recorded investment in the loans exceeded fair value resulting in an allowance being allocated to the loans at March 31, 2024 and December 31, 2023.

	Fair Value Estimate	Valuation Techniques	Unobservable Inputs	Discount
March 31, 2024				
Collateral dependent loans with ACL	<u>\$ -</u>	Appraisal (1)	Selling cost	0%
			Discount for lack of marketability	0%
December 31, 2023				
Collateral dependent loans with ACL	<u>\$ 3,947,577</u>	Appraisal (1)	Selling cost	7%
			Discount for lack of marketability	10%

- (1) Fair value is generally determined through independent appraisal of underlying collateral, which generally includes various level 3 inputs which are not observable.

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Notes to Consolidated Financial Statements

16. Fair Value Measurements - continued

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)
March 31, 2024					
Financial assets:					
Cash and cash equivalents	\$ 50,750,053	\$ 50,750,053	\$ 50,750,053	\$ -	\$ -
Time deposits in other banks	1,486,178	1,466,872	-	1,466,872	-
Investment securities held to maturity:					
U.S. Treasury securities	14,334,767	13,649,790	13,649,790	-	-
Other investment securities	86,428,056	77,902,922	-	77,902,922	-
Loans, net	504,120,299	488,249,243	-	-	488,249,243
Accrued interest receivable	1,752,712	1,752,712	-	1,752,712	-
Bank owned life insurance	6,577,956	6,577,956	-	6,577,956	-
Financial liabilities:					
Noninterest-bearing deposits	140,052,705	140,052,705	-	140,052,705	-
Interest-bearing deposits	431,052,279	429,989,433	-	-	429,989,433
FHLBA overnight borrowings	25,250,000	25,250,000	-	25,250,000	-
FHLBA term borrowings	17,000,000	16,941,440	-	16,941,440	-
Accrued interest payable	911,663	911,663	-	911,663	-
December 31, 2023					
Financial assets:					
Cash and cash equivalents	\$ 32,002,628	\$ 32,002,628	\$ 32,002,628	\$ -	\$ -
Time deposits in other banks	2,258,681	2,218,604	-	2,218,604	-
Investment securities held to maturity:					
U.S. Treasury securities	17,344,342	16,598,520	16,598,520	-	-
Other investment securities	89,151,564	81,056,922	-	81,056,922	-
Loans, net	502,249,930	487,148,887	-	-	487,148,887
Accrued interest receivable	1,825,679	1,825,679	-	1,825,679	-
Bank owned life insurance	6,543,598	6,543,598	-	6,543,598	-
Financial liabilities:					
Noninterest-bearing deposits	145,916,027	145,916,027	-	145,916,027	-
Interest-bearing deposits	408,392,609	407,330,105	-	-	407,330,105
FHLBA overnight borrowings	31,000,000	31,000,000	-	31,000,000	-
FHLBA term borrowings	17,000,000	17,132,048	-	17,132,048	-
Accrued interest payable	712,066	712,066	-	712,066	-

Harford Bank and Subsidiary

Notes to Consolidated Financial Statements

17. Legal Proceedings

The Bank is at times, in the ordinary course of business, subject to other legal actions that are normally associated with a financial institution. In management's opinion, the effect of these other actions will not be material to the financial condition or results of operations of the Bank.

18. Accounting Standard Updates

ASU 2023-06, *"Disclosure Improvements, Codification Amendments in Response to the SEC's Disclosure Update and Simplification Initiative."* The amendments in ASU 2023-06 incorporate certain U.S. Securities and Exchange Commission ("SEC") disclosure requirements into the FASB Accounting Standards Codification. The amendments in the ASU are expected to clarify or improve disclosure and presentation requirements of a variety of Codification Topics, allow users to more easily compare entities subject to the SEC's existing disclosures with those entities that were not previously subject to the requirements, and align the requirements in the Codification with the SEC's regulations. For entities subject to the SEC's existing disclosure requirements and for entities required to file or furnish financial statements with or to the SEC in preparation for the sale of or for purposes of issuing securities that are not subject to contractual restrictions on transfer, the effective date for each amendment will be the date on which the SEC removes that related disclosure from its rules. For all other entities, the amendments will be effective two years later. However, if by June 30, 2027, the SEC has not removed the related disclosure from its regulations, the amendments will be removed from the Codification and not become effective for any entity. The adoption of ASU 2023-06 is not expected to have a material impact on the Bank's financial statements.

ASU 2023-07, *"Segment Reporting (Topic 280), Improvements to Reportable Segment Disclosures."* The amendments in ASU 2023-07 are intended to improve reportable segment disclosure requirements primarily through enhanced disclosures about significant segment expenses. This ASU requires disclosure of significant segment expenses that are regularly provided to the chief operating decision maker ("CODM"), an amount for other segment items by reportable segment and a description of its composition, all annual disclosures required by FASB ASU Topic 280 in interim periods as well, and the title and position of the CODM and how the CODM uses the reported measures. Additionally, this ASU requires that at least one of the reported segment profit and loss measures should be the measure that is most consistent with the measurement principles used in an entity's consolidated financial statements. Lastly, this ASU requires public business entities with a single reportable segment to provide all disclosures required by these amendments in this ASU and all existing segment disclosures in Topic 280. This ASU is effective for fiscal years beginning after December 15, 2023, and interim periods within fiscal years beginning after December 15, 2024. Early adoption is permitted. The amendments should be applied retrospectively. The adoption of ASU 2023-07 is not expected to have a material impact on the Bank's financial statements.

ASU 2023-09, *"Income Taxes (Topic 740), Improvement to Income Tax Disclosures."* The amendments in ASU 2023-09 require an entity to disclose specific categories in the rate reconciliation and provide additional information for reconciling items that meet a quantitative threshold, which is greater than five percent of the amount computed by multiplying pretax income by the entity's applicable statutory rate, on an annual basis. Additionally, the amendments in this ASU require an entity to disclose the amount of income taxes paid (net of refunds received) disaggregated by federal, state, and foreign taxes and the amount of income taxes paid (net of refunds received) disaggregated by individual jurisdictions that are equal to or greater than five percent of total income taxes paid (net of refunds received). Lastly, the amendments in this ASU require an entity to disclose income (or loss) from continuing operations before income tax expense (or benefit) disaggregated between domestic and foreign and income tax expense (or benefit) from continuing operations disaggregated by federal, state, and foreign. This ASU is effective for annual periods beginning after December 15, 2024. Early adoption is permitted. The amendments should be applied on a prospective basis; however, retrospective application is permitted. The adoption of ASU 2023-09 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: May 1, 2024

/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: May 1, 2024

/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 March 31, 2024, 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: May 1, 2024

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

Date: May 1, 2024

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