HARBOR BANKSHARES CORPORATION

2020 Annual Report

HARBOR BANKSHARES
CORPORATION

BOARD OF DIRECTORS

James H. DeGraffenreidt, Jr.
Retired Chairman & CEO
WGL Holdings, Inc.

Joseph Haskins, Jr.
Chairman & CEO
Harbor Bankshares Corporation

Kevin M. Johnson
President
Commercial Group

Delores G. Kelley
Senator
Maryland State Senate

Erich W. March
Vice President
William C. March Funeral Home

James Scott, Jr.
Principal
Penan & Scott, P.C.

Stanley W. Tucker
President
Meridian Management Group, Inc.

George F. Vaeth, Jr.
Retired Architect

Yitzhak Zelmanovitch
President
Founders' Impact, Inc.
(f/k/a East Coast Capital Holdings, Ltd)

EXECUTIVE OFFICERS

Joseph Haskins, Jr.
Chairman & CEO
Corporation and Bank

John Lewis
President & Chief Operating Officer
Corporation and Bank

Kimberly J. Levine
Executive Vice President
Chief Financial Officer
Corporation and Bank

James H. DeGraffenreidt, Jr.
Chairman
Executive Committee
Corporation and Bank

George F. Vaeth, Jr.
Secretary
Corporation and Bank

EXECUTIVE COMMITTEE

James H. DeGraffenreidt, Jr., Chairman
Joseph Haskins, Jr.
Delores G. Kelley
Erich W. March
George F. Vaeth, Jr.

AUDIT COMMITTEE

George F. Vaeth, Jr., Chairman
Erich W. March
James Scott, Jr.
Stanley W. Tucker

HUMAN RESOURCES COMMITTEE

Delores G. Kelley, Chairwoman
James H. DeGraffenreidt, Jr.
Joseph Haskins, Jr.

INVESTMENT COMMITTEE

James H. DeGraffenreidt, Jr., Chairman
Joseph Haskins, Jr.
Kevin M. Johnson
Yitzhak Zelmanovitch

HARBOR BANKSHARES
C O R P O R A T I O N

March 25, 2021

Dear Shareholder:

This past year was like no other with the COVID-19 pandemic casting its shadow over almost everything. Harbor Bankshares Corporation (the Corporation), like most other businesses, had to adapt. With the temporary closure of our branches, we had to find new ways to meet customers' needs. For many, work became virtual. And while there were pandemic-driven expenses and some negative impact to income streams caused by so much of the world shutting down, previously developed plans to weather unanticipated crises served us well. The Corporation ended the year profitably, recording net income of $1.1 million.

While achieving profitability, leadership focused on new initiatives, including participation in the Federal Reserve Bank's Main Street Lending Program, the Small Business Administration's Paycheck Protection Program (PPP), and the transition to a new and improved core information technology platform. Recognizing that small businesses make up the lifeblood of the community, The Harbor Bank of Maryland (the Bank) originated over $41 million in PPP loans. These loans which are fully guaranteed by the SBA averaged $111,000, with amounts as low as $1,000, helping to reach some of the smallest and most vulnerable businesses that are often overlooked. In 2021 the Bank continues to meet the need, originating another $17.9 million in PPP loans.

The Corporation also entered into agreements with Google and JPMorgan Chase to collaborate on new product and service offerings. These partnerships will help expand the beneficial impact the Corporation will have in the community. As both a Minority Depository Institution (MDI) and a Certified Development Financial Institution (CDFI), the Corporation's mission has always been to improve the communities it serves.

As a CDFI, we have access to capital that supports lending to underserved communities at a much greater capacity than traditional lending alone. In 2020, we received a $50 million CDFI New Market Tax Credit award, bringing our total lifetime awards to $384 million. We deployed most of the new award expeditiously to create and save jobs and expand access to community services and quality healthcare for the most vulnerable populations.

Balancing objectives to serve the community and shareholders, in early 2021, the Corporation repurchased 4.3 million shares of stock held by the U.S. Treasury, an ownership interest that originated in 2009 under the Troubled Asset Relief Program (TARP). This repurchase not only increased the book value per share but also favorably positioned the Corporation for new capital raising opportunities, particularly those sparked by recent interest in racial equity.

We continue to forge ahead to make the Corporation and the Bank stronger and to better serve our customers, community, and shareholders.

We thank you for your continued support.

Sincerely,

HARBOR BANKSHARES CORPORATION

Joseph Haskins, Jr.
Chairman & CEO

Harbor Bankshares Corporation and Subsidiaries

Consolidated Financial Statements

Years Ended December 31, 2020 and 2019

Table of Contents

Consolidated Financial Statements:

INDEPENDENT AUDITOR'S REPORT

To the Stockholders and Board of Directors
Harbor Bankshares Corporation

Report on the Financial Statements
We have audited the accompanying consolidated financial statements of Harbor Bankshares Corporation and Subsidiaries (the Company), which comprise the consolidated balance sheet as of December 31, 2020, the related consolidated statements of operations, comprehensive income (loss), changes in stockholders' equity and cash flows for the year then ended, and the related notes to the consolidated financial statements (collectively, the financial statements).

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

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

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

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

Opinion
In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Harbor Bankshares Corporation and its Subsidiaries as of December 31, 2020, and the results of their operations their cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matter
The financial statements of the Company, as of and for the year ended December 31, 2019, were audited by other auditors, whose report, dated March 23, 2020, expressed an unmodified opinion on those statements.

Yount, Hyde & Barbour, P.C.

Richmond, Virginia
March 23, 2021

Harbor Bankshares Corporation and Subsidiaries
Consolidated Balance Sheets
December 31, 2020 and 2019

	2020	2019
ASSETS		
Cash and cash equivalents:		
Cash and due from banks	$ 5,562,057	$ 5,048,294
Federal funds sold	9,885,986	6,334,147
Interest-bearing deposits in other banks	43,954,107	63,464,039
Cash and cash equivalents	59,402,150	74,846,480
Investment securities		
Available-for-sale, at fair value	35,574,722	30,644,851
Federal Home Loan Bank of Atlanta stock, at cost	280,200	254,200
Loans	216,309,197	197,339,424
Allowance for loan losses	(2,428,622)	(2,238,748)
Loans, net	213,880,575	195,100,676
Premises and equipment, net	2,332,057	2,378,203
Other real estate owned	214,203	-
Bank-owned life insurance	6,139,321	5,972,648
Deferred income taxes	-	-
Other assets	4,853,827	2,433,489
Total assets	$ 322,677,055	$ 311,630,547

See accompanying notes.

	2020	2019
LIABILITIES AND STOCKHOLDERS' EQUITY		
Deposits:		
Noninterest-bearing demand	**$ 80,306,122**	$ 62,642,976
Interest-bearing transaction accounts	**34,097,218**	31,524,563
Savings and money markets	**68,742,689**	86,431,275
Time, $250,000 or more	**14,667,261**	39,150,897
Other time	**63,259,304**	63,554,648
Total deposits	**261,072,594**	283,304,359
Federal Reserve Bank borrowings	**32,259,756**	-
Junior subordinated debentures	**7,217,000**	7,217,000
Other borrowings	**5,000**	2,000,000
Accrued interest payable	**804,007**	1,615,384
Other liabilities	**11,839,608**	9,383,548
Total liabilities	**313,197,965**	303,520,291
Stockholders' equity:		
Common stock (par value $0.01)		
Authorized 10,000,000 shares; issued and outstanding 5,399,328 at December 31, 2020 and 5,273,568 at December 31, 2019 in addition to 33,795 common nonvoting at December 31, 2020 and 2019	**54,331**	53,074
Additional paid-in capital	**15,185,083**	14,982,240
Accumulated deficit	**(5,773,802)**	(6,881,751)
Accumulated other comprehensive income (loss)	**13,478**	(43,307)
Total stockholders' equity	**9,479,090**	8,110,256
Total liabilities and stockholders' equity	**$ 322,677,055**	$ 311,630,547

Harbor Bankshares Corporation and Subsidiaries
Consolidated Statements of Operations
December 31, 2020 and 2019

	2020	2019
Interest income:		
Interest and fees on loans	$ 10,598,865	$ 11,121,265
Interest on investments	443,856	695,823
Other interest income	256,448	765,785
Total interest income	11,299,169	12,582,873
Interest expense:		
Interest-bearing transaction accounts	120,352	158,720
Savings and money markets	199,334	342,315
Time, $250,000 or more	429,100	942,625
Other time	1,368,669	1,548,490
Federal Home Loan Bank borrowings	1,282	187,344
Federal Reserve Bank PPPLF Borrowings	72,540	-
Interest on junior subordinated debentures	275,338	403,959
Interest on other borrowings	71,771	146,667
Total interest expense	2,538,386	3,730,120
Net interest income	8,760,783	8,852,753
Provision for loan losses	185,000	410,500
Net interest income after provision for loan losses	8,575,783	8,442,253
Noninterest income:		
Management fees - New Market Tax Credits	3,043,842	3,201,923
Service charges on deposit accounts	141,894	171,820
Other service charges	334,143	400,127
Income from bank-owned life insurance	166,673	189,860
Income from CDFI Financial Assistance award	455,426	-
Origination income from Main Street Lending Program	285,440	-
Gain on sale of securities	27,933	-
Other income	430,220	349,683
Total noninterest income	4,885,571	4,313,413

See accompanying notes.

Harbor Bankshares Corporation and Subsidiaries
Consolidated Statements of Operations
December 31, 2020 and 2019

	2020	2019
Noninterest expenses:		
Salaries and benefits	**5,708,473**	6,525,708
Occupancy expense of premises	**1,393,227**	1,530,015
Equipment expense	**196,539**	197,599
Data processing fees	**1,456,805**	1,613,172
Professional fees	**1,617,727**	1,881,564
Advertising	**265,499**	390,664
FDIC insurance	**245,049**	210,803
Telephone	**307,753**	322,502
Loan and collection expense	**135,480**	116,038
Off balance sheet provision (benefit)	**(150,000)**	45,400
Other expense	**984,941**	1,241,769
Total noninterest expense	**12,161,493**	14,075,234
Income (Loss) before income taxes	**$ 1,299,861**	$ (1,319,568)
Income tax expense	**191,912**	581,899
Net income (loss)	**$ 1,107,949**	$ (1,901,467)
Income (loss) per common share	**$ 0.21**	$ (0.36)

See accompanying notes.

Harbor Bankshares Corporation and Subsidiaries
Consolidated Statements of Comprehensive Income (Loss)
Years Ended December 31, 2020 and 2019

	2020	2019
Net income (loss):	**$ 1,107,949**	$ (1,901,467)
Changes in unrealized gains on securities available for sale, net of income taxes of $0 in 2020 and 2019	**84,718**	1,281,709
Reclassficiation adjustment, net of income taxes of $0 in 2020 and 2019	**(27,933)**	-
Total comprehensive income (loss)	**$ 1,164,734**	$ (619,758)

See accompanying notes.

Harbor Bankshares Corporation and Subsidiaries
Consolidated Statements of Changes in Stockholders' Equity
Years Ended December 31, 2020 and 2019

	Common Stock	Paid-in Capital	Accumulated (Deficit)	Accumulated Other Comprehensive Income (Loss)	Total Stockholders' Equity
Balance, January 1, 2019	$ 65,118	$ 15,969,696	$ (4,980,284)	$ (1,325,016)	$ 9,729,514
Redemption of common stock	(12,048)	(987,952)			(1,000,000)
Issuance of common stock	4	496			500
Net loss			(1,901,467)		(1,901,467)
Other comprehensive income				1,281,709	1,281,709
Balance, December 31, 2019	$ 53,074	$ 14,982,240	$ (6,881,751)	$ (43,307)	$ 8,110,256
Issuance of common stock	**1,257**	**202,843**			**204,100**
Net income			**1,107,949**		**1,107,949**
Other comprehensive income				**56,785**	**56,785**
Balance, December 31, 2020	**$ 54,331**	**$ 15,185,083**	**$ (5,773,802)**	**$ 13,478**	**$ 9,479,090**

See accompanying notes.

Harbor Bankshares Corporation and Subsidiaries
Consolidated Statements of Cash Flows
Years Ended December 31, 2020 and 2019

	2020	2019
Cash flows from operating activities:		
Net income (loss)	$ 1,107,949	$ (1,901,467)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation and amortization	237,141	325,805
Amortization of premiums and discounts on investment securities	1,184	17,678
Provision for loan losses	185,000	410,500
Off balance sheet provision (benefit)	(150,000)	45,400
Gains on sale of securities	(27,933)	-
Deferred income tax provision	-	350,219
Income from bank-owned life insurance	(166,673)	(189,860)
Decrease (increase) in other assets	(2,420,338)	213,719
Increase in accrued interest payable and other liabilities	1,794,683	4,854,950
Net cash provided by operating activities	561,013	4,126,944
Cash flows from investing activities:		
Redemption (purchase) of FHLB stock	(26,000)	1,685,100
Purchases of securities available-for-sale	(72,104,270)	(999,744)
Proceeds from calls, maturities and principal payments of investment securities available-for-sale	67,257,933	3,700,000
Redemption of bank-owned life insurance	-	2,170,953
Purchase of loans	(11,543,532)	-
Net decrease (increase) in loans	(7,635,570)	18,723,824
Purchases of premises and equipment	(190,995)	(131,990)
Net cash provided by (used in) investing activities	(24,242,434)	25,148,143
Cash flows from financing activities:		
Net increase (decrease) in deposits	(22,231,765)	65,479,971
Net decrease in advances from FHLB	-	(40,000,000)
Net increase in PPPLF advances from FRB	32,259,756	
Decrease in other borrowings	(1,995,000)	-
Issuance of common stock	204,100	500
Redemption of common stock	-	(1,000,000)
Net cash provided by financing activities	8,237,091	24,480,471
Net increase (decrease) in cash equivalents	(15,444,330)	53,755,558
Cash and cash equivalents, beginning of period	74,846,480	21,090,922
Cash and cash equivalents, end of period	$ 59,402,150	$ 74,846,480
Supplemental disclosure of cash flow information:		
Cash paid for income taxes	$ -	$ -
Cash paid for interest	$ 3,423,584	$ 2,098,547

See accompanying notes.

Notes to Consolidated Financial Statements

1. Nature of Operations

Harbor Bankshares Corporation (the "Corporation") is a bank holding company organized under the laws of the State of Maryland in 1992. The Corporation owns all of the outstanding stock of the Harbor Bankshares Capital Corporation ("HBCC") and The Harbor Bank of Maryland (the "Bank"). HBCC owns 100% of Harbor Bankshares Asset Management, LLC, a limited liability company and the Bank owns all of the outstanding stock of the Bank's subsidiary, Harbor Financial Services. The Bank was incorporated under the laws of the State of Maryland in 1980 and began operations in 1982. The parent-only consolidated financial statements of the Corporation account for the subsidiaries using the equity method of accounting. Consolidated financial statements include the accounts of Harbor Bankshares Corporation and its subsidiaries. All significant intercompany accounts and transactions have been eliminated.

The Bank is a commercial bank headquartered in Baltimore, Maryland. The deposits of the Bank are insured by the Federal Deposit Insurance Corporation. The Bank conducts general banking business in seven locations and primarily serves the Baltimore, Maryland metropolitan area. It offers checking, savings and time deposits, commercial real estate, personal, home improvement, automobile, and other installment and term loans. The Bank is also a member of a national ATM network. The retail nature of the Bank allows for diversification of depositors and borrowers, which limits its dependency upon a single or a few customers.

HBCC is an operating entity headquartered in Baltimore. Its activities include providing private capital to businesses through loans and principal investments.

2. Basis of Presentation and Significant Accounting Policies

The accounting and reporting policies of the Corporation and its subsidiaries conform to U.S. generally accepted accounting principles and those within the banking industry. Certain reclassifications have been made to amounts previously reported to conform to the classifications made in 2020. These reclassifications were immaterial and did not change total stockholders' equity or net income (loss). The following is a summary of the more significant accounting policies:

Use of estimates

The preparation of consolidated financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash and cash equivalents

For purposes of the consolidated statements of cash flows, the Corporation considers all highly liquid debt instruments and money market funds to be cash equivalents. Cash and due from banks, federal funds sold, and interest-bearing deposits in other banks have overnight maturities and are generally in excess of amounts that would be recoverable under Federal Deposit Insurance Corporation ("FDIC") insurance. The amount of cash with other banks in excess of FDIC insured limits totals $5,302,859 as of December 31, 2020.

Investment securities

Debt securities that the Corporation has the positive intent and ability to hold to maturity are classified as held-to-maturity and recorded at amortized cost. Debt and equity securities are classified as trading securities if bought and held principally for the purpose of selling them in the near term. Trading securities are reported at estimated fair value, with unrealized gains and losses included in earnings. Debt securities not classified as held to maturity or as trading securities are considered available-for-sale and are reported at estimated fair value, with unrealized gains and losses excluded from earnings and reported as a separate component of stockholders' equity, net of tax effects, in accumulated other comprehensive income (loss).

The Corporation designates securities into one of the three categories at the time of purchase. If a decline in value of an individual security classified as held-to-maturity or available-for-sale is judged to be other-than-temporary, the cost basis of that security is reduced to its fair value and the amount of the write-down is reflected in earnings. Estimated fair value is determined based on bid prices published in financial newspapers or bid quotations received from securities dealers. Gains or losses on the sales of investments are calculated using a specific identification basis and are determined on a trade-date basis. Premiums and discounts on investment and mortgage-backed securities are amortized over the lesser of the term or the earliest call date of the security using methods that approximate the interest method.

Management reviews all debt securities that are in an unrealized loss position for other-than-temporary impairment and evaluates outstanding available-for-sale and held-to-maturity securities for other-than-temporary impairment on at least a quarterly basis. An investment security is deemed impaired if the fair value of the investment is less than its amortized cost. Amortized cost includes adjustments (if any) made to the cost basis of an investment for accretion, amortization, and previous other-than-temporary impairments. After an investment security is determined to be impaired, management evaluates whether the decline in value is other-than-temporary. In estimating other-than-temporary impairment losses for debt securities, management considers whether the Corporation (1) has the intent to sell the security, or (2) will more likely than not be required to sell the security before its anticipated recovery, or (3) will suffer a credit loss as the present value of the cash flows expected to be collected from the security are less than its amortized cost basis. Declines in the fair value of available-for-sale debt securities that are deemed other-than-temporary are recognized in the consolidated statement of operations in net securities gains/(losses) in the period in which the determination is made. Such impairment charges include the impact of declines in both credit quality and liquidity. Declines deemed to be temporary as a result of changes in market conditions are recorded as unrealized gains or losses and recorded in accumulated other comprehensive income (loss).

Loans

Loans are stated at their principal balance outstanding net of any deferred fees and costs. Interest income on loans is accrued at the contractual rate based on the principal outstanding. The Corporation places loans on non-accrual when any portion of the principal or interest is ninety days past due and collateral is insufficient to discharge the debt in full. Interest accrual may also be discontinued earlier if, in management's opinion, collection is unlikely. Loans are considered delinquent when the borrower is in arrears two or more monthly payments and is greater than 30 days past due.

Loans are considered impaired when, based on current information, it is probable that the Corporation will not collect all principal and interest payments according to contractual terms when due. Management also considers the financial condition of the borrower, cash flows of the loan and the net realizable value of the related collateral. Impaired loans do not include large groups of smaller balance homogeneous credits such as residential real estate and consumer installment loans, which are evaluated collectively for impairment. The impairment of a loan is measured based on the present value of expected future cash flows discounted at the loan's effective interest rate, or the fair value of the collateral if repayment is expected to be provided by the collateral. Generally, the Corporation's impairment on such loans is measured by reference to the fair value of the collateral.

Discounts and premiums on purchased loans are amortized to income using the interest method over the remaining period to contractual maturity, adjusted for anticipated prepayments.

Federal Home Loan Bank of Atlanta stock

The Bank, as a member of the Federal Home Loan Bank system, is required to maintain an investment in capital stock of the Federal Home Loan Bank of Atlanta ("FHLB") in varying amounts based on balances of outstanding home loans and on amounts borrowed from the FHLB. Because no ready market exists for this stock and it has no quoted market value, the Bank's investment in this stock is carried at cost.

Allowance for Loan Losses

The allowance for loan losses represents an amount which, in management's judgment, will be adequate to absorb probable and estimable losses on existing loans that may become uncollectible. The allowance for loan losses consists of an allocated component and an unallocated component. The components of the allowance for loan losses represent an estimation done as prescribed in accounting guidance issued by the Financial Accounting Standards Board ("FASB"). The adequacy of the allowance for loan losses is determined through careful and continuous review and evaluation of the loan portfolio and involves the balancing of a number of factors as outlined below to establish a prudent level. Loans deemed uncollectible are charged against, while recoveries are credited to, the allowance. Management adjusts the level of the allowance through the provision for loan losses, which is recorded as a current period operating expense on the statement of operations. The Corporation's methodology for assessing the appropriateness of the allowance consists of several key elements, which include the formula allowance, specific allowances and the unallocated allowance.

The formula allowance is calculated by applying loss factors to corresponding categories of outstanding loans. Loss factors are based on the Corporation's historical loss experience and include management's evaluation of various qualitative/environmental conditions that are not directly measured in the determination of specific allowances. Such conditions include general economic and business conditions affecting key lending areas, credit quality trends (including trends in delinquencies and nonperforming loans expected to result from existing conditions), loan volumes and concentrations, specific industry conditions within portfolio categories, recent loss experience in particular loan categories, duration of the current business cycle, bank regulatory examination results, findings of internal loan examiners, and management's judgment with respect to various other conditions including loan administration and management and the quality of risk identification systems. Executive management reviews these conditions quarterly. The use of these loss factors is intended to reduce the difference between estimated losses inherent in the portfolio and observed losses.

Specific allowances are established in cases where management has identified significant conditions or circumstances related to a loan that management believes indicate the probability that a loss may be incurred in an amount different from the amount determined by application of the formula allowance. Management determines the fair value of the loan and recognizes any impairment in accordance with FASB's accounting guidance and recognizes any such impairment as a specific allowance. For other problem graded credits, allowances are established according to the application of credit risk factors. These factors are set by management to reflect its assessment of the relative level of risk inherent in each grade.

The imprecision of the above calculations in estimating probable losses on existing loans that may become uncollectible may result in management's assessment that there is a probability that a loss may be incurred in an amount different from the amount determined by application of the formula allowance, resulting in an unallocated allowance.

Management believes that the allowance for loan losses is adequate. However, the determination of the allowance requires significant judgment, and estimates of probable losses inherent in the loan portfolio can vary significantly from the amounts actually observed. While management uses available information to recognize probable losses, future additions to the allowance may be necessary based on changes in the loans comprising the loan portfolio and changes in the financial condition of borrowers, such as may result from changes in economic conditions. In addition, various regulatory agencies, as an integral part of their examination process, periodically review the Bank's loan portfolio and allowance for loan losses. Such review may result in recognition of additions to the allowance based on their judgments of information available to them at the time of their examination.

Premises and equipment

Premises and equipment are stated at cost less accumulated depreciation and amortization computed using the straight-line method. Premises and equipment are depreciated over the useful lives of the assets, except for leasehold improvements which are amortized over the terms of the respective leases or the estimated useful lives of the improvements, whichever is shorter. Useful lives range from three to fifteen years for furniture, fixtures and equipment and building improvements, and forty years for buildings. The costs of major renewals and betterments are capitalized, while the costs of ordinary maintenance and repairs are expensed as incurred. Land is stated at cost.

Other Real Estate Owned

Real estate acquired through or in lieu of loan foreclosure is initially recorded at the fair value of the property less estimated selling costs at the date of foreclosure, establishing a new cost basis. Any write-downs based on the asset's fair value at the date of acquisition are charged to the allowance for loan losses. After foreclosure, any declines in fair value are recorded as a write down to Other real estate owned and are recorded as a charge to non-interest expense, to reduce the carrying value of the property to the lower of cost or fair value less costs to sell. Costs of significant property improvements are capitalized, and costs related to holding the property are expensed.

Bank-owned life insurance

The Corporation is the beneficiary of insurance policies on the lives of certain officers of the Corporation. The Corporation has recognized the cash surrender value that could be realized under the insurance policies as an asset in the consolidated balance sheets. Appreciation in the value of the insurance policies is classified in non-interest income.

Revenue Recognition

The Corporation's revenue includes net interest income on financial instruments and noninterest income. Specific categories of revenue are presented in the Consolidated Statement of Operations. Most of the Corporation's revenue is not within the scope of Accounting Standard Update *(ASU) No. 2014-09 – Revenue from Contracts with Customers*. For revenue within the scope of ASU 2014-09, the Corporation provides services to customers and has related performance obligations. The revenue from such services is recognized upon satisfaction of all contractual performance obligations. The following discuss the key revenue streams within the scope of the new revenue recognition guidance.

Management fees from NMTC – The Corporation receives fee income related to the transfer of its New Market Tax Credits ("NMTC"), which varies with each transaction, but which are all similar in nature. There are three types of fees associated with these transactions. The first is a "sub-allocation fee" that is paid to the Corporation when the tax credits are allocated to an entity at the time a qualified equity investment is made. There is also a structuring fee that is paid to the Corporation for providing certain administrative, tax credit advisory and financial structuring services. These two fees are recognized by the Corporation at the time the NMTC transaction is closed. The third type of fee is an asset management fee that is paid to cover the administrative and servicing costs associated with ongoing compliance with the NMTC reporting requirements. This fee is recognized as the services are rendered.

Service charges on deposit accounts – Service charges on deposit accounts represent general service fees for monthly account maintenance and activity or transaction-based fees and consist of transaction-based revenue, time-based revenue (i.e. service period), item-based revenue or some other individual attribute-based revenue. Revenue is recognized when the Corporation's performance obligation is completed which is generally monthly for account maintenance services or when the transaction has been completed (such as stop payments). Payment for such performance obligations are generally received at the time the performance obligations are satisfied.

Other service charges – Generally the Corporation receives compensation when a customer issues checks drawn on insufficient funds or when a customer or a non-customer utilizes the Corporation's ATM machines. The timing and amount of revenue recognition is not materially impacted by the new standard.

Other income – The Corporation receives income from merchant discount fees and other transaction fees such as wire, check, item handling and other charges related to specific services. Payment for such performance obligations are generally received at the time the transaction has been completed.

Income from CDFI Financial Assistance award **–** The Corporation receives income from the CDFI Fund based on a successful application process. As the Corporation achieves certain performance goals with respect to the origination of loans or the delivery of certain services in designated communities, as outlined in the grant agreement, income from the award is recognized in proportion to the achievement of those goals to the total goal. In late 2019, the Bank was designated to receive a Financial Assistance (FA) Award of $649,000 but did not recognize income as none of the goals were achieved. In 2020, $455,426 of the FA Award was recognized as income based on a prorata achievement of the designated goals.

Income taxes

Income tax expense is based on the results of operations, adjusted for permanent differences between items of income or expense reported in the consolidated financial statements and those reported for tax purposes. Under the liability method, deferred income taxes are determined based on the differences between the financial statement carrying amounts and the income tax basis of assets and liabilities and are measured at the enacted tax rates that will be in effect when these differences reverse. Deferred tax assets are recognized only to the extent that it is more likely than not that such amounts will be realized based upon consideration of available evidence, including tax planning strategies and other factors.

The Corporation recognizes a tax position as a benefit only if it is "more likely than not" that the tax position would be sustained in a tax examination, with a tax examination being presumed to occur. The amount recognized is the largest amount of tax benefit that is greater than 50% likely to be realized on examination. For tax positions not meeting the "more likely than not" test, no tax benefit is recorded. The Corporation recognizes interest and penalties related to income tax matters in income tax expense.

The Corporation's income tax returns are subject to review and examination by federal and state taxing authorities for the years ended December 31, 2017 through and including 2020.

Income (Loss) per common share

Basic and dilutive net income (loss) per common share is computed by dividing net income (loss) available to common stockholders by the weighted-average number of shares outstanding during the period. The impact of common stock equivalents has been excluded from the computation of diluted weighted average common shares outstanding in periods where there is a net loss, as their effect is anti-dilutive. The Corporation did not have any potential common stock equivalents at December 31, 2020.

Business segments

The Corporation has determined that its current business and operations consist of one business segment.

3. Restrictions on Cash and Due from Banks

The Bank is required by Federal Reserve to maintain a reserve balance based principally on deposit liabilities. The balance maintained is included in cash and due from banks. The reserve balances kept at the Federal Reserve Bank as of December 31, 2020 and 2019, were $38,031,343 and $58,025,000, respectively, with a restricted amount of $25,000 for each year. The reserve balances kept at M&T Bank, the Bank's principal correspondent bank, were $2,500,000 for each year.

4. Investment Securities

The amortized cost and estimated fair values of investments securities are as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Balance at December 31, 2020				
Available-for-sale:				
U.S. government agencies	**$ 34,550,228**	**$ 12,299**	**$ (15,205)**	**$ 34,547,322**
State and municipals	**1,011,016**	**16,384**	**-**	**1,027,400**
Total	**$ 35,561,244**	**$ 28,683**	**$ (15,205)**	**$ 35,574,722**
Balance at December 31, 2019				
Available-for-sale:				
U.S. Treasuries	$ 999,795	$ -	$ (336)	$ 999,459
U.S. government agencies	26,527,862	25,957	(92,639)	26,461,180
State and municipals	3,160,501	24,168	(457)	3,184,212
Total	$ 30,688,158	$ 50,125	$ (93,432)	$ 30,644,851

The Corporation held nine securities with unrealized losses at December 31, 2020. Securities with unrealized losses segregated by length of impairment at December 31, 2020, and December 31, 2019, were as follows:

	Less than 12 Months		More than 12 Months		Total	
	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses
December 31, 2020						
Available-for-sale:						
U.S. government agencies	**$ 34,547,322**	**$ (15,205)**	**$ -**	**$ -**	**$ 34,547,322**	**$ (15,205)**
State and municipals	**$ -**	**$ -**	**$ 1,027,400**	**$ -**	**$ 1,027,400**	**$ -**
December 31, 2019						
Available-for-sale:						
U.S. Treasuries	$ 999,459	$ (336)	$ -	$ -	$ 999,459	$ (336)
U.S. government agencies	$ 18,912,470	$ (81,824)	$ 7,551,505	$ (10,815)	$ 26,463,975	$ (92,639)
State and municipals	$ 2,684,097	$ -	$ 500,115	$ (457)	$ 3,184,212	$ (457)

Declines in the fair value of available-for-sale securities below their cost that are deemed to be other-than-temporary are reflected in earnings as realized losses.

Management has the intent to hold the securities classified as available-for-sale for a period of time sufficient for a recovery of cost and it is not likely they will be required to sell the securities before their anticipated recovery. The fair value is expected to recover as the debt securities approach their maturity date or repricing date. Management does not believe any of the securities are impaired due to reasons of credit quality. Accordingly, as of

December 31, 2020, management believes the unrealized losses detailed in the table above are temporary and no loss has been realized in the Corporation's consolidated statements of operations.

The amortized cost and estimated fair value of debt securities at December 31, 2020, by contractual maturity, are shown below. Expected maturities may differ from contractual maturities because borrowers have the right to call or repay obligations without call or prepayment penalties.

	Amortized Cost	Estimated Fair Value
Available-for-sale:		
Due within three months	$ 2,000,000	$ 2,000,140
Due after three months through one year	499,292	503,730
Due after one year through three years	1,011,724	1,023,720
Due after three years through five years	32,050,228	32,047,132
Total	$ 35,561,244	$ 35,574,722

Securities with a fair value of $32,548,134 and $27,463,425 at December 31, 2020 and 2019, respectively have been pledged as collateral for demand, money market and certificate of deposit accounts.

The only investments to a single issuer that exceed 10% of stockholders' equity are to federal government sponsored entities.

5. Loans and Allowance for Loan Losses

Loans consist of the following at December 31:

	2020	2019
Real estate loans:		
Construction and land development	**$ 3,013,091**	$ 7,679,752
Commercial	**109,547,696**	106,721,267
Residential	**41,579,350**	50,711,202
	154,140,137	165,112,221
Commercial and industrial	**59,546,652**	29,493,324
Consumer	**2,622,408**	2,733,879
Total loans	**216,309,197**	197,339,424
Less allowance for loan losses	**(2,428,622)**	(2,238,748)
	$ 213,880,575	$ 195,100,676

The Bank has segregated its loan portfolio into five segments, including construction and land development, commercial real estate, residential real estate, commercial and industrial, and consumer. The Bank primarily serves the Baltimore-Maryland Metropolitan area; therefore, exposure to credit risk is significantly affected by changes in this market area.

Construction lending includes lending for construction and development of residential properties (including multifamily), although the Bank does lend funds for the construction of commercial properties, including faith-based properties. The Bank has financed the construction of nonresidential properties on a case by case basis. Loan proceeds are disbursed during the construction phase according to a draw schedule based on the stage of completion. Construction loans are underwritten on the basis of the estimated value of the property as completed. The Corporation's credit monitoring process for construction lending includes property inspections throughout the construction process each time a draw is requested before funds are disbursed.

The Bank offers fixed rate conventional mortgage loans on one-to-four family residential dwellings. Most loans are originated on properties located in the Bank's primary market area. These loans are offered for terms ranging from five to thirty years, typically with a five-year demand clause, and are amortized on a monthly basis with interest and principal due each month.

The Bank originates commercial real estate loans in its market area. These loans are generally larger and involve greater risks than residential real estate loans. Because payments on these loans are often dependent on the successful operation or management of the property, repayment of such loans may be subject to a greater extent to adverse conditions in the real estate market or the economy. The Bank seeks to minimize these risks in a variety of ways, including limiting the size and loan-to-value ratios. The loans are typically originated with a five-year maturity (five-year call or balloon). The Bank's commercial real estate loans are typically secured by retail or wholesale establishments, service industries, faith-based properties and industrial or warehouse facilities.

Commercial and residential real estate loans including construction loans comprised 71.3% and 83.7% of the Corporation's total loan portfolio at December 31, 2020 and 2019, respectively, as follows:

	2020	**% of Loans Outstanding**	2019	% of Loans Outstanding
Commercial real estate	**$112,560,787**	**52.0%**	$114,401,019	58.0%
Residential real estate	**41,579,350**	**19.3%**	50,711,202	25.7%
	$ 154,140,137	**71.3%**	$165,112,221	83.7%

Most of the real estate collateralizing these loans is within the greater Baltimore metropolitan area. Consequently, the Corporation and its borrowers are affected by the economic conditions prevailing in our market area.

The Bank offers secured and unsecured commercial business loans and lines of credit to businesses primarily located in its market area. Most business loans have terms of one to five years, with lines of credit that can be open for longer periods. The security for a business loan depends on the amount borrowed, the business involved, and the strength of the borrower. Commercial business lending entails significant risk, as the payments on such loans may depend upon successful operation or management of the business involved. The Bank attempts to limit its risk of loss on such loans by limiting the amount and the term, and by requiring personal guarantees of the principals of the business.

Commercial loans include Paycheck Protection Program (PPP) loans authorized under the Coronavirus Aid, Relief and Economic Security Act (the "CARES Act"). PPP loans are fully guaranteed by the Small Business Administration (SBA) and totaled $31,498,893 at December 31, 2020.

The Bank's consumer loans consist of automobile loans, deposit account loans, and installment loans. The loans are generally offered for terms of up to five years at fixed interest rates. Consumer loans are generally originated at higher interest rates than residential mortgage loans because of their higher risk. Repossessed collateral for a defaulted loan may not provide an adequate source of repayment as a result of damage, loss, or depreciation. In addition, collections are dependent on the borrower's continuing financial stability, and thus are more likely to be adversely affected by job loss, divorce, illness, or personal bankruptcy.

On an ongoing basis, the Bank assigns a grade to each of its loans. The internal grades are pass, special mention, substandard, doubtful and loss. Loans graded pass are high quality loans where the borrower exhibits a strong balance sheet position and good earnings and cash flow history. Loans graded special mention show potential weaknesses that deserve the Bank's close attention. If these potential weaknesses are not corrected, they may result in deterioration of the repayment prospects for the loan and in the Bank's credit position at some future date. Substandard loans are inadequately protected by the current financial strength and paying capacity of the borrower or of the collateral pledged, if any. Substandard loans have a well-defined weakness that could jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the Bank will sustain some loss if the weaknesses are not corrected. Loans graded doubtful have all the weaknesses inherent in substandard loans with the added characteristic that the weaknesses make collection or liquidation in full highly improbable. Assets graded loss are considered uncollectible and of such little value that their continuance as an asset is not warranted. The classification does not mean the loan has absolutely no recovery value, but that it is not practical to defer charging off the loan even though partial recovery may be received in the future.

The following tables show credit quality indicators, the aging of receivables, and disaggregated balances of loan losses as of December 31, 2020 and 2019.

Information with respect to credit quality indicators is as follows:

	Construction and Land Development	Commercial Real Estate	Residential Real Estate	Commercial and Industrial	Consumer	Total
As of December 31, 2020:						
Credit risk profile by internally assigned grade:						
Pass	**$ 3,013,091**	**$ 105,258,231**	**$ 41,247,030**	**$ 59,139,816**	**$ 2,622,408**	**$ 211,280,576**
Special mention	**-**	**3,532,321**	**-**	**-**	**-**	**3,532,321**
Substandard	**-**	**757,144**	**332,320**	**406,836**	**-**	**1,496,300**
Doubtful	**-**	**-**	**-**	**-**	**-**	**-**
Total	**$ 3,013,091**	**$ 109,547,696**	**$ 41,579,350**	**$ 59,546,652**	**$ 2,622,408**	**$ 216,309,197**
Credit risk profile based on payment activity:						
Performing	**$ 3,013,091**	**$ 106,683,831**	**$ 40,471,605**	**$ 58,577,911**	**$ 2,613,641**	**$ 211,360,079**
Nonperforming	**-**	**2,863,865**	**1,107,745**	**968,741**	**8,767**	**4,949,118**
Total	**$ 3,013,091**	**$ 109,547,696**	**$ 41,579,350**	**$ 59,546,652**	**$ 2,622,408**	**$ 216,309,197**
As of December 31, 2019:						
Credit risk profile by internally assigned grade:						
Pass	$ 7,679,752	$ 101,919,864	$ 49,790,086	$ 28,790,409	$ 2,733,879	$ 190,913,990
Special mention	-	-	11,609	495,759	-	507,368
Substandard	-	4,801,403	909,507	207,156	-	5,918,066
Doubtful	-	-	-	-	-	-
Total	$ 7,679,752	$ 106,721,267	$ 50,711,202	$ 29,493,324	$ 2,733,879	$ 197,339,424
Credit risk profile based on payment activity:						
Performing	$ 7,679,752	$ 103,966,371	$ 49,790,192	$ 28,973,432	$ 2,733,879	$ 193,143,626
Nonperforming	-	2,754,896	921,010	519,892	-	4,195,798
Total	$ 7,679,752	$ 106,721,267	$ 50,711,202	$ 29,493,324	$ 2,733,879	$ 197,339,424

Information on aging analysis of past due loans is as follows:

	Construction and Land Development	Commercial Real Estate	Residential Real Estate	Commercial and Industrial	Consumer	Total
As of December 31, 2020:						
30-59 days past due	$ -	$ 686,291	$ 13,869	$ 5,222,361	$ 67,149	$ 5,989,670
60-89 days past due	-	6,377,851	-	2,401,930	254	8,780,035
Greater than 90 days past due	-	2,749,146	1,107,745	467,509	8,767	4,333,167
Total past due	-	9,813,288	1,121,614	8,091,800	76,170	19,102,872
Current	3,013,091	99,734,408	40,457,736	51,454,852	2,546,238	197,206,325
Total loans receivable	$ 3,013,091	$109,547,696	$ 41,579,350	$ 59,546,652	$ 2,622,408	$216,309,197
Recorded investment >90 days and accruing	$ -	$ 1,938,291	$ 765,527	$ 167,502	$ 8,767	$ 2,880,087
As of December 31, 2019:						
30-59 days past due	$ -	$ 3,845,227	$ 31,241	$ 586,404	$ 20,850	$ 4,483,722
60-89 days past due	-	755,733	10,514	197,421	-	963,668
Greater than 90 days past due	-	2,754,896	921,010	519,892	15,099	4,210,897
Total past due	-	7,355,856	962,765	1,303,717	35,949	9,658,287
Current	7,679,752	99,365,411	49,748,437	28,189,607	2,697,930	187,681,137
Total loans receivable	$ 7,679,752	$106,721,267	$ 50,711,202	$ 29,493,324	$ 2,733,879	$197,339,424
Recorded investment >90 days and accruing	$ -	$ -	$ -	$ -	$ 15,099	$ 15,099

The following table shows the allowance for loan losses and recorded investment in loans for each of the Bank's segments:

	Construction and Land Development	Commercial Real Estate	Residential Real Estate	Commercial and Industrial	Consumer	Unallocated	Total
December 31, 2020:							
Allowance for loan losses:							
Beginning balance	$ 46,079	$ 1,367,779	$ 292,765	$ 375,004	$ 18,466	$ 138,655	$ 2,238,748
Charge-offs	-	-	-	(6,666)	(15,461)	-	(22,127)
Recoveries	-	18,175	-	6,051	2,775	-	27,001
Provision	(35,600)	195,039	(72,856)	(25,034)	11,009	112,442	185,000
Ending balance	$ 10,479	$ 1,580,993	$ 219,909	$ 349,355	$ 16,789	$ 251,097	$ 2,428,622
Allowance for loan losses individually evaluated for impairment	$ -	$ 69,799	$ -	$ 47,416	$ -	$ -	$ 117,215
Allowance for loan losses collectively evaluated for impairment	$ 10,479	$ 1,511,194	$ 219,909	$ 301,939	$ 16,789	$ 251,097	$ 2,311,407

	Construction and Land Development	Commercial Real Estate	Residential Real Estate	Commercial and Industrial	Consumer	Unallocated	Total
Loans receivable:							
Ending balance	**$ 3,013,091**	**$ 109,547,696**	**$ 41,579,350**	**$ 59,546,652**	**$ 2,622,408**	**$ -**	**$ 216,309,197**
Ending balance individually evaluated for impairment	**$ -**	**$ 6,487,493**	**$ 954,037**	**$ 406,836**	**$ -**	**$ -**	**$ 7,848,366**
Ending balance collectively evaluated for impairment	**$ 3,013,091**	**$ 103,060,203**	**$ 40,625,313**	**$ 59,139,816**	**$ 2,622,408**	**$ -**	**$ 208,460,831**
December 31, 2019:							
Allowance for loan losses:							
Beginning balance	$ 9,215	$ 657,209	$ 304,858	$ 1,064,374	$ 4,483	$ 44,225	$ 2,084,364
Charge-offs	-	(298,168)	-	-	(2,851)	-	(301,019)
Recoveries	-	11,168	-	28,610	5,125	-	44,903
Provision	36,864	997,570	(12,093)	(717,980)	11,709	94,430	410,500
Ending balance	$ 46,079	$ 1,367,779	$ 292,765	$ 375,004	$ 18,466	$ 138,655	$ 2,238,748
Allowance for loan losses individually evaluated for impairment	$ -	$ 96,156	$ 1,976	$ -	$ -	$ -	$ 98,132
Allowance for loan losses collectively evaluated for impairment	$ 46,079	$ 1,271,623	$ 290,789	$ 375,004	$ 18,466	$ 138,655	$ 2,140,616
Loans receivable:							
Ending balance	$ 7,679,752	$ 106,721,267	$ 50,711,202	$ 29,493,324	$ 2,733,879	$ -	$ 197,339,424
Ending balance individually evaluated for impairment	$ -	$ 5,658,978	$ 1,525,211	$ 2,912,332	$ -	$ -	$ 10,096,521
Ending balance collectively evaluated for impairment	$ 7,679,752	$ 101,062,289	$ 49,185,991	$ 26,580,992	$ 2,733,879	$ -	$ 187,242,903

Management reviews and identifies loans that require designation as nonperforming assets. Nonperforming assets include loans accounted for on a non-accrual basis, loans past due 90 days or more but still accruing, and other real estate owned. Information with respect to nonperforming assets at December 31, is as follows:

	2020	2019
Non-accrual loans	**$ 2,069,031**	$ 4,195,798
Loans 90 days or more past due and still accruing	**2,880,087**	15,099
Total nonperforming loans	**4,949,118**	4,210,897
Other real estate owned	**214,203**	-
Total nonperforming assets	**$ 5,163,321**	$ 4,210,897

Loans past due 90 days or more which were still accruing included $2,083,248 in loans which were matured and in the process of renewal or for which funds were on deposit at Harbor but were not applied to the loan as per agreement.

The balance of non-accrual loans for each of the Bank's loan segments is as follows:

	Construction and Land Development	Commercial Real Estate	Residential Real Estate	Commercial and Industrial	Consumer	Total
As of December 31, 2020:						
Unpaid principal balance	**$ -**	**$ 925,575**	**$ 342,218**	**$ 801,238**	**$ -**	**$ 2,069,031**
As of December 31, 2019:						
Unpaid principal balance	$ -	$ 2,754,896	$ 921,010	$ 519,892	$ -	$ 4,195,798

Troubled debt restructured ("TDR") loans result from renewals or modifications for which concessions are granted. These concessions include offering an interest rate that is not considered to be a market rate or an extension to the maturity which would not otherwise be considered for other loans with similar credit risk. TDR loans are individually evaluated for impairment and specific reserves are included in the allowance for loan losses as necessary. The following table shows information on TDR loans:

	Construction and Land Development	Commercial Real Estate	Residential Real Estate	Commercial and Industrial	Consumer	Total
As of December 31, 2020:						
Troubled debt restructuring outstanding principal balance	**$ -**	**$ 2,512,725**	**$ 926,455**	**$ 209,290**	**$ -**	**$ 3,648,470**
Number of loans	**-**	**6**	**3**	**2**	**-**	**11**
Pre-modification principal balance	**$ -**	**$ 3,791,772**	**$ 1,113,731**	**$ 908,997**	**$ -**	**$ 5,814,500**
Post-modification principal balance	**$ -**	**$ 3,741,156**	**$ 1,113,731**	**$ 908,997**	**$ -**	**$ 5,763,884**
Troubled debt restructuring that subsequently defaulted:						
Number of loans	**-**	**-**	**-**	**-**	**-**	**-**
Current principal balance	**$ -**	**$ -**	**$ -**	**$ -**	**$ -**	**$ -**

	Construction and Land Development	Commercial Real Estate	Residential Real Estate	Commercial and Industrial	Consumer	Total
As of December 31, 2019:						
Troubled debt restructuring outstanding principal, balance	$ -	$ 3,071,673	$ 966,751	$ 121,502	$ -	$ 4,159,926
Number of loans	-	9	3	1	-	13
Pre-modification principal balance	$ -	$ 5,671,275	$ 1,113,731	$ 134,028	$ -	$ 6,919,034
Post-modification principal balance	$ -	$ 5,620,038	$ 1,113,731	$ 134,028	$ -	$ 6,867,797
Troubled debt restructuring that subsequently defaulted:						
Number of loans	-	3	2	1	-	6
Current principal balance	$ -	$ 115,280	$ 351,048	$ 121,502	$ -	$ 587,830

The CARES Act allows banks to elect to suspend requirements under GAAP for loan modifications related to the COVID-19 pandemic (for loans that were not more than 30 days past due as of December 31, 2019) that would otherwise be categorized as a TDR, including impairment for accounting purposes, until the earlier of 60 days after the termination of the national emergency or December 31, 2020. The Bank provided COVID-19 payment relief on loans totaling $51,809,743 as of December 31, 2020.

Other than COVID-19 payment relief noted above, the Bank did not modify any loans during 2020. Two individual loans were modified during 2019. The restructuring in 2019 was the result of rate concessions given to the borrowers but there was no reduction in the outstanding principal balances. As of December 31, 2019, one of the loans is on non-accrual status while the remaining loan is considered a performing TDR. Information on the loans modified as a troubled debt restructure for the year ended 2019 is as follows:

	Number of Contracts	Pre-modification outstanding recorded investment	Post-modification outstanding recorded investment
2019 Troubled Debt Restructures			
Loans type			
Commercial RE	2	$ 91,380	$ 91,380

There are no outstanding commitments to lend additional funds to any loans classified as a TDR as of December 31, 2020 or 2019.

Impaired loans include loans that management has identified where it is probable that all amounts due will not be collected in accordance with the contractual terms of the loan when due. An impaired loan may involve deficiencies in the borrower's overall financial condition, payment history, support available from financial guarantors, changes in expected future cash flows or the fair market value of any collateral. Loans that are returned to accrual status are no longer considered to be impaired.

Information with respect to impaired loans at December 31 and for the years then ended is as follows:

	2020	2019
Impaired loans with a valuation allowance	**$ 1,536,687**	$ 1,743,457
Impaired loans without a valuation allowance	**6,311,679**	8,353,064
Total impaired loans	**$ 7,848,366**	$ 10,096,521
Allowance for loan losses related to impaired loans	**$ 117,215**	$ 98,132
Allowance for loan losses related to other than impaired loans	**2,311,407**	2,140,616
Total allowance for loan losses	**$ 2,428,622**	$ 2,238,748
Average impaired loans for the year	**$ 9,264,992**	$ 10,610,347
Interest income recognized on impaired loans	**$ 532,808**	$ 612,944

Information on impaired loans for each of the Bank's loan segments is as follows:

	Construction and Land Development	**Commercial Real Estate**	**Residential Real Estate**	**Commercial and Industrial**	**Consumer**	**Total**
As of December 31, 2020						
Loans with a valuation allowance:						
Recorded Investment	**$ -**	**$ 1,339,142**	**$ -**	**$ 197,545**	**$ -**	**$ 1,536,687**
Unpaid principal balance	**$ -**	**$ 1,368,580**	**$ -**	**$ 197,545**	**$ -**	**$ 1,566,125**
Related allowance for loan losses	**$ -**	**$ 69,799**	**$ -**	**$ 47,416**	**$ -**	**$ 117,215**
Average recorded investment	**$ -**	**$ 1,369,672**	**$ -**	**$ 1,480,439**	**$ -**	**$ 2,850,111**
Interest income recognized	**$ -**	**$ 102,817**	**$ -**	**$ -**	**$ -**	**$ 102,817**
Loans without a valuation allowance:						
Recorded Investment	**$ -**	**$ 5,148,351**	**$ 954,037**	**$ 209,291**	**$ -**	**$ 6,311,679**
Unpaid principal balance	**$ -**	**$ 6,082,153**	**$ 997,769**	**$ 233,988**	**$ -**	**$ 7,313,910**
Average recorded Investment	**$ -**	**$ 5,232,662**	**$ 967,509**	**$ 214,710**	**$ -**	**$ 6,414,881**
Interest income recognized	**$ -**	**$ 394,835**	**$ 33,140**	**$ 2,016**	**$ -**	**$ 429,991**

	Construction and Land Development	Commercial Real Estate	Residential Real Estate	Commercial and Industrial	Consumer	Total
Totals:						
Recorded Investment	**$ -**	**$ 6,487,493**	**$ 954,037**	**$ 406,836**	**$ -**	**$ 7,848,366**
Unpaid principal balance	**$ -**	**$ 7,450,733**	**$ 997,769**	**$ 431,533**	**$ -**	**$ 8,880,035**
Related allowance for loan losses	**$ -**	**$ 69,799**	**$ -**	**$ 47,416**	**$ -**	**$ 117,215**
Average recorded investment	**$ -**	**$ 6,602,334**	**$ 967,509**	**$ 1,695,149**	**$ -**	**$ 9,264,992**
Interest income recognized	**$ -**	**$ 497,652**	**$ 33,140**	**$ 2,016**	**$ -**	**$ 532,808**
As of December 31, 2019:						
Loans with a valuation allowance:						
Recorded Investment	$ -	$ 1,414,179	$ 329,278	$ -	$ -	$ 1,743,457
Unpaid principal balance	$ -	$ 1,427,664	$ 356,709	$ -	$ -	$ 1,784,373
Related allowance for loan losses	$ -	$ 96,156	$ 1,976	$ -	$ -	$ 98,132
Average recorded investment	$ -	$ 1,429,394	$ 332,396	$ -	$ -	$ 1,761,790
Interest income recognized	$ -	$ 95,972	$ -	$ -	$ -	$ 95,972
Loans without a valuation allowance:						
Recorded Investment	$ -	$ 4,244,799	$ 1,195,933	$ 2,912,332	$ -	$ 8,353,064
Unpaid principal balance	$ -	$ 5,046,773	$ 1,199,242	$ 2,964,315	$ -	$ 9,210,330
Average recorded Investment	$ -	$ 4,661,321	$ 1,203,245	$ 2,983,990	$ -	$ 8,848,556
Interest income recognized	$ -	$ 237,284	$ 38,873	$ 240,815	$ -	$ 516,972
Totals:						
Recorded Investment	$ -	$ 5,658,978	$ 1,525,211	$ 2,912,332	$ -	$10,096,521
Unpaid principal balance	$ -	$ 6,474,437	$ 1,555,951	$ 2,964,315	$ -	$10,994,703
Related allowance for loan losses	$ -	$ 96,156	$ 1,976	$ -	$ -	$ 98,132
Average recorded investment	$ -	$ 6,090,715	$ 1,535,641	$ 2,983,990	$ -	$10,610,346
Interest income recognized	$ -	$ 333,256	$ 38,873	$ 240,815	$ -	$ 612,944

The Bank has granted loans to certain officers and directors of the Bank and their associates. Related party loans are made on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with unrelated persons and do not involve more than the normal risk of collectability. The aggregate dollar amount of these loans was $697,614 and $2,465,979 at December 31, 2020 and 2019, respectively. During 2020 and 2019, loans totaling $160,170 and $0, respectively, were made. During 2020, repayments of $1,378,556 were made while repayments in 2019 totaled $365,802.

Loans serviced for others by the Corporation under its New Market Tax Credits Program totaled $230,790,000 at December 31, 2020 and $189,140,000 at December 31, 2019.

Unamortized loan premiums total $493,489 at December 31, 2020 and $523,985 at December 31, 2019.

At December 31, 2020, three residential real estate loans were in the process of foreclosure totaling $327,726. At December 31, 2019, six residential real estate loans were in the process of foreclosure totaling $1,226,360.

6. Premises and Equipment

The major classes of premises and equipment at December 31, are summarized as follows:

	2020	2019
Land	$ 631,900	$ 631,900
Buildings	2,265,463	2,265,463
Furniture, fixtures and equipment	747,828	3,516,174
Leasehold improvements	6,189,676	6,314,411
	9,834,867	12,727,948
Less accumulated depreciation and amortization	(7,502,810)	(10,349,745)
	$ 2,332,057	$ 2,378,203

Depreciation and amortization expense was $237,141 and $325,805 for the years ended December 31, 2020 and 2019, respectively.

7. Deposits

Maturities of time deposits as of December 31, 2020 are as of follows:

2021	$ 33,628,489
2022	5,642,627
2023	4,903,851
2024	32,464,306
2025	1,091,848
Thereafter	195,444
	$ 77,926,565

Deposits are the Bank's primary funding source for loans and investment securities. The mix and repricing alternatives can significantly affect the cost of this source of funds and, therefore, impact the net interest margin.

The Corporation has one deposit relationship in excess of 5% of total deposits at December 31, 2020, and two deposit relationships in excess of 5% of total deposits at December 31, 2019. Total related party deposits are estimated at $4,154,970 and $3,995,336 at December 31, 2020 and 2019, respectively.

Overdrawn demand deposits reclassified as loans receivable in the consolidated balance sheets amounted to $169,262 and $12,231 as of December 31, 2020 and 2019, respectively.

8. Federal Home Loan Bank and Federal Reserve Bank Borrowings

The Bank has approved credit facilities of $81,863,000 and $76,438,000 with the Federal Home Loan Bank of Atlanta as of December 31, 2020 and 2019, respectively. There were no borrowings outstanding under these facilities as of December 31, 2020 and 2019, respectively. At December 31, 2019, the Bank pledged $25 million of its collateral position under this FHLB line to secure public funds on deposit with the bank. Loans with a collateral value totaling $48,893,074 at December 31, 2020, and $47,908,345 at December 31, 2019, have been pledged as collateral for these facilities.

During 2020, the Bank originated loans under the Small Business Administration Payroll Protection Program (PPP). Loans originated under this program served as eligible collateral under the Federal Reserve Bank's Payroll Protection Program Loan Facility (PPPLF). As of December 31, 2020, the Bank had borrowings of $32,259,756 under the PPPLF program and pledged loans in the same amount. Advances under the PPPLF are summarized by year of maturity and weighted average interest rate as of December 31, 2020:

	Outstanding	Weighted Average Rate
2022	$ 30,463,606	0.35%
2025	1,796,150	0.35%
Total	$ 32,259,756	0.35%

9. Junior Subordinated Debentures

On October 9, 2003, the Corporation issued floating rate junior subordinated debt securities due 2033 in the amount of $7.2 million. The debt securities were issued by the Corporation pursuant to an indenture, dated as of October 9, 2003, between the Corporation and Wilmington Trust Company. Upon the receipt of the net funds, the Corporation paid off long-term debt in the amount of $1.8 million, and invested $4.9 million as capital in the Bank, increasing the Bank's tier one capital. Payments on the debt securities are used to fund dividends on the Corporation's trust preferred securities. The interest rate on the debentures was approximately 3.21% at December 31, 2020.

The Corporation exercised its right to defer interest payments on the debt securities beginning with the payment due February 8, 2010. This deferment is permitted by the terms of the junior subordinated debentures and does not constitute an event of default so long as there is no other event of default. Interest on the debt securities continues to accrue and is required to be paid in full prior to the expiration of the deferral period. The total deferral period may not exceed 20 consecutive quarters.

While in deferment, the Corporation, after obtaining regulatory approval, paid dividends on its Troubled Asset Relief Program ("TARP") preferred stock. Under the indenture and the trust preferred documents, the payment of dividends on junior securities, such as TARP preferred stock during the interest deferral period and while interest is due on the trust preferred can result in an event of default. An event of default may result in the trust preferred becoming immediately and fully due and an obligation to pay costs and expenses of collection. Attempts were made by the Corporation to cure the potential event of default including a request for permission from its regulators to pay all interest due on its trust preferred at the end of the extension period dated May 8, 2011, which was denied, and a request for the Department of Treasury to refund the TARP dividends previously made during the deferral period, which also was denied. The Corporation received a notice of an event of default from its trust preferred trustee during 2011 requesting the event of default be remedied. Since then, no action or demand for immediate repayment has been brought against the Corporation. The Corporation may not make any distributions of interest or principal on the subordinated debentures without the approval of the Federal Reserve Bank of Richmond. After receiving regulatory approval, a payment of $1,410,506 was made on January 29, 2015 to bring the obligation current. Additional quarterly payments totaling $304,436 and $404,323 were made during 2020 and 2019, respectively. The Corporation guarantees the debt obligation of the trust which remains current as of December 31, 2020.

10. Other Borrowings

On July 15, 2018, the Corporation entered into a promissory note with an individual related to one of the Corporation's directors. The $2,000,000 promissory note had a stated interest rate of 8% per year and was originally due in full along with all accrued interest on January 5, 2019. On February 27, 2019, this note was renewed at an interest rate of 4% per year and a maturity date of February 1, 2020. This note was subsequently renewed at an interest rate of 5% per year and a maturity date of October 1, 2020. On December 17, 2020, this note was repaid in full.

11. Income Tax

The Corporation's provision for income taxes for the years ended December 31, is summarized as follows:

	2020	2019
Taxes currently payable	$ 191,912	$ 231,680
Deferred tax expense (benefit)	(186,959)	350,219
Change in valuation allowance	186,959	-
Income tax expense for the year	$ 191,912	$ 581,899

A reconcilement of the difference between the statutory federal income tax rate and the effective tax rate for the Corporation is as follows:

	2020	2019
Federal income tax statutory rate	21.0 %	(21.0)%
State income taxes net of federal benefit	(14.8)%	13.8 %
Alternative minimum tax	- %	(3.7)%
Increase in value of bank-owned life insurance	(7.9)%	(3.0)%
Surrender of bank-owned life insurance	- %	21.7 %
Other permanent differences	3.0 %	1.0 %
Change in valuation allowance	13.5 %	35.3 %
Effective tax rate	14.8 %	44.1%

Temporary differences between the amounts reported in the consolidated financial statements and tax bases of assets and liabilities result in deferred taxes. The types of temporary differences that give rise to significant portions of the deferred tax assets and liabilities are as follows for the years ended December 31:

	2020	2019
Deferred tax assets:		
Net operating loss	$ 1,626,093	$ 2,294,632
Depreciation	927,316	962,493
Deferred compensation	629,756	629,699
Allowance for loan losses	485,220	423,241
Non-accrual loan interest	74,015	48,613
New market tax credit	1,719,937	1,437,643
Deferred loan fees	191,630	24,571
Other, net	-	4,408
Total gross deferred tax assets	$ 5,653,967	$ 5,825,300

	2020	2019
Net deferred tax assets attributable to operations	$ 5,653,967	$ 5,825,300
Deferred tax on unrealized loss on investments charged to other comprehensive income	(3,709)	11,917
Less valuation allowance	(5,650,258)	(5,837,217)
Net deferred income tax assets	$ -	$ -

The Corporation has net operating loss carryforwards for federal income tax purposes of approximately $3 million at December 31, 2020, which are available to offset future taxable income, and which will expire in 2032 through 2037.

Management assesses the available positive and negative evidence to estimate whether sufficient future taxable income will be generated to permit use of the existing deferred tax assets. A significant piece of objective negative evidence evaluated was the cumulative loss incurred over two of the last three years ended December 31, 2020. Such objective evidence limited the ability to consider other subjective evidence, such as our projections for future growth.

On the basis of this evaluation, as of December 31, 2020, a valuation allowance of $5,650,258 has been recorded to recognize only the portion of the deferred tax asset that is more likely than not to be realized. The amount of the deferred tax asset considered realizable, however, could be adjusted if estimates of future taxable income during the carryforward period are reduced or increased or if objective negative evidence in the form of cumulative losses is no longer present and additional weight is given to subjective evidence such as our projections for growth.

12. Preferred Stock

On July 17, 2009 the Corporation entered into and consummated a Letter Agreement (the “Purchase Agreement”) with the United States Department of the Treasury (the “Treasury”), pursuant to which the Corporation issued 6,800 shares of the Corporation’s Fixed Rate Cumulative Perpetual Preferred Stock, Series A (the “Series A Preferred Stock”), having a liquidation amount per share equal to $1,000, for a total purchase price of $6,800,000. The Series A Preferred Stock pays cumulative dividends at a rate of 5% per year for the first five years and thereafter at a rate of 9% per year.

On July 6, 2018, the Corporation and the United States Treasury (the “Treasury”) agreed to exchange the 6,800 preferred shares outstanding and $4,545,234 of accrued and unpaid dividends payable on the preferred shares beneficially owned and held by the Treasury for 5,491,843 shares of the Company’s common stock and a cash payment of $2,272,617, resulting in a deemed preferred stock dividend in the amount of $2,272,617.

In 2019, the Corporation purchased 1,204,819 shares of the Company’s common stock held by the Treasury and retired the common stock.

13. Employee Benefit Plans

Profit sharing retirement savings plan

The Corporation has established a defined-contribution plan covering employees meeting certain age and service eligibility requirements. The plan provides for cash deferrals qualifying under Section 401(k). Matching contributions made by the Corporation approximated $51,000 for the year ended December 31, 2020 and $48,000 for the year ended December 31, 2019.

Deferred compensation

The Bank entered into deferred compensation agreements with three of its executive officers. Under the agreements, the Bank is obligated to provide for the officers or their beneficiaries certain lump-sum benefit payments after the employee's death, disability, or retirement. The estimated present value of future benefits to be paid to the remaining executive officer still employed by the Bank is being accrued over the period from the effective date of the agreement until the full eligibility dates of the participant and totaled $2,288,357 at both December 31, 2020 and 2019. The expense incurred for this plan for the years ended December 31, 2020 and 2019 was $0 and $35,423, respectively. The Bank is the beneficiary of life insurance policies, purchased as a method of partially financing benefits under this plan. In 2019, the Bank surrendered two of these insurance policies covering former employees. The aggregate cash surrender value of the remaining life insurance policies was $6,139,321 and $5,972,648 at December 31, 2020 and 2019, respectively.

14. Operating Leases

The Corporation enters into leases in the normal course of business primarily for branch locations and loan production offices. The Corporation's leases have remaining terms ranging from one to five years, some of which include renewal options to extend the lease for up to three years.

The Corporation includes lease extensions if it is deemed reasonably certain the Corporation will exercise the option.

Leases are classified as operating or finance leases at the lease commencement date. Lease expense for operating leases is recognized on a straight-line basis over the lease term. Right-of-use assets represent the Corporation's right to use an underlying asset for the lease term and the lease liabilities represent the Corporation's obligation to make lease payments arising from the lease. Lease liabilities are recognized at the lease commencement date based on the estimated present value of lease payments over the lease term. Lease liabilities represent the Corporation's obligation to make lease payments and are presented at each reporting date as the net present value of the remaining contractual cash flows. Upon adoption, the Corporation elected certain practical expedients within the standard and consistent with such elections did not reassess whether any expired or existing contracts are or contain leases, did not reassess the lease classification for any expired or existing leases and did not reassess any initial direct costs for existing leases.

The Corporation uses the incremental borrowing rate at lease commencement to calculate the present value of lease payments when the rate implicit in the lease is not known. The Corporation's incremental borrowing rate is based on the FHLB amortizing advance rate for the comparable lease period.

Right-of-use assets of $1,402,172 at December 31, 2020 are reflected as Other assets while the lease liabilities of $1,458,845 at December 31, 2020 are reflected as Other liabilities.

Future minimum payments for each of the five succeeding years under non-cancelable operating leases consisted of the following at December 31, 2020:

2021	$ 501,910
2022	379,770
2023	295,125
2024	256,844
2025	192,376
Thereafter	-
Total lease payments	1,626,025
Imputed interest	(167,180)
Lease obligation	$ 1,458,845

Total lease expense under operating leases amounted to $606,002 and $570,266 for the years ended December 31, 2020 and 2019, respectively.

15. Regulatory Matters

The Corporation and Bank are subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory, and possibly additional discretionary, actions by regulators that, if undertaken, could have a direct material effect on the Corporation's and the Bank's consolidated financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of the Bank's assets, liabilities, and certain off-balance-sheet items as calculated under regulatory accounting practices. The Bank's capital amounts, and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

Quantitative measures established by regulation to ensure capital adequacy require the Corporation and the Bank to maintain amounts and ratios (set forth in the table below) of total and Tier 1 capital (as defined in the regulations) to risk-weighted assets (as defined), and of Tier 1 capital (as defined) to average assets (as defined). As of December 31, 2020, the capital levels of the Corporation and the Bank exceed all minimum capital adequacy requirements to which they are subject. There are no conditions or events since December 31, 2020 that management believes have changed the Bank's capital rating.

The Federal Reserve Bank and the FDIC approved final rules implementing the Basel Committee on Banking Supervision ("BCBS") capital guidelines for U.S. banks. Under the final rules, minimum requirements increased for both the quantity and quality of capital held by the Corporation. The rules include a new common equity Tier 1 capital to risk-weighted assets minimum ratio of 4.5%, raise the minimum ratio of Tier 1 capital to risk-weighted assets to 6.0%, require a minimum ratio of Total Capital to risk-weighted assets of 8.0% and require a minimum Tier 1 leverage ratio of 4.0%. A capital conservation buffer, comprised of common equity Tier 1 capital, is also established above the regulatory minimum capital requirements. This capital conservation buffer was phased in beginning January 1, 2016 at 0.625% of risk-weighted assets and increased each subsequent year by an additional 0.625% until reaching its final level of 2.5% on January 1, 2019. Strict eligibility criteria for regulatory capital instruments were also implemented under the final rules. The final rules also revise the definition and calculation of Tier 1 capital, Total Capital, and risk-weighted assets. At December 31, 2020, the Bank's specific capital conservation buffer was 4.1%.

In August of 2018, the Economic Growth, Regulatory Relief, and Consumer Protection Act ("EGRRCPA") directed the Federal Reserve Board to revise the Small Bank Holding Company Policy Statement to raise the total consolidated asset limit in the Policy Statement from $1 billion to $3 billion. The Corporation meets the conditions of the revised policy statement and was, therefore, exempt from the consolidated capital requirements at December 31, 2019 and 2020.

The Bank's actual capital amounts and ratios are also presented in the table (in thousands):

	Actual		For Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Corrective Action Provision	
	Amount	Ratio	Minimum Amount	Required Ratio	Minimum Amount	Required Ratio
As of December 31, 2020:						
Total Capital (to risk-weighted total assets)	**$ 23,197**	**12.1%**	**$ 15,320**	**8.0%**	**$ 19,150**	**10.0%**
Tier 1 Capital (to risk-weighted assets)	**$ 20,807**	**10.9%**	**$ 11,490**	**6.0%**	**$ 15,320**	**8.0%**
Common Equity Tier 1 Capital (to risk-weighted assets)	**$ 20,807**	**10.9%**	**$ 8,618**	**4.5%**	**$ 12,448**	**6.5%**
Tier 1 Capital (to average assets)	**$ 20,807**	**7.2%**	**$ 11,492**	**4.0%**	**$ 14,365**	**5.0%**
As of December 31, 2019:						
Total Capital (to risk-weighted total assets)	$ 22,971	11.4%	$ 16,116	8.0%	$ 20,145	10.0%
Tier 1 Capital (to risk-weighted assets)	$ 20,487	10.2%	$ 12,087	6.0%	$ 16,116	8.0%
Common Equity Tier 1 Capital (to risk-weighted assets)	$ 20,487	10.2%	$ 9,065	4.5%	$ 13,094	6.5%
Tier 1 Capital (to average assets)	$ 20,487	6.6%	$ 12,352	4.0%	$ 15,440	5.0%

Bank and holding company regulations, as well as Maryland law, impose certain restrictions on dividend payments by the Bank, as well as restricting extensions of credit and transfers of assets between the Bank and the Corporation. At December 31, 2020, the Bank is restricted from paying dividends to its parent company without regulatory approval.

On April 5, 2010, the Bank entered into a Consent Order (the "Order") with the Federal Deposit Insurance Corporation (the "FDIC") and the Maryland Commissioner of Financial Regulation (the "Commissioner"), which directs the Bank to (i) increase its capitalization, (ii) reduce nonperforming loans and concentrations in commercial real estate loans, (iii) strengthen management policies and practices, (iv) establish a comprehensive policy and methodology for determining an appropriate allowance for loan losses, and (v) increase its Board of Directors participation in the affairs of the Bank. On February 13, 2013 the order was terminated and replaced with a Memorandum of Understanding, "MOU", which was superseded by a Memorandum of Understanding as of September 20, 2017 and which is still in effect as of December 31, 2020. The "MOU" provides for certain restrictions on dividend payments and expresses management's fiduciary responsibility, requests progress reports to be filed by the Corporation within 45 days of each quarter end while under the "MOU" and compels the board of directors to monitor the Corporation's adherence to the memorandum.

Harbor Bankshares Corporation was also a party to a written agreement with the Federal Reserve Bank of Richmond (the "FRB Agreement"), which requires it to serve as a source of strength to the Bank, including taking steps to ensure that the Bank complies with the Consent Order entered into with the FDIC and the Commissioner and any other supervisory action taken by the Bank's federal or state regulator. As noted above, the Bank had its consent order lifted and replaced with an "MOU", and accordingly Harbor Bankshares Corporation also had its written agreement lifted and replaced with an "MOU". The agreement also prohibits the Corporation from taking any of the following actions without the FRB's prior written approval: (i) declaring or paying any dividends; (ii) taking dividends from the Bank; (iii) making any distributions of interest, principal or other sums on Harbor Bankshares Corporation's subordinated debentures or trust preferred securities; (iv) incurring, increasing or guaranteeing any debt; or (v) repurchasing or redeeming any shares of its stock.

16. Earnings Per Common Share

Basic and diluted income (loss) per common share calculations for the years ended December 31, 2020 and 2019 are as follows:

	2020	2019
Basic and diluted:		
Income (loss) attributable to common stockholders	$ 1,107,949	$ (1,901,467)
Average common shares outstanding	5,396,104	5,322,783
Income (loss) per common share	$ 0.21	$ (0.36)

Basic earnings per common share is calculated by dividing net income (loss) available to common stockholders by the weighted-average number of common shares outstanding for the period.

17. Financial Instruments with Off-Balance Sheet Risk

In the normal course of business, the Corporation has various outstanding credit commitments which are properly not reflected in the consolidated financial statements. These commitments are made to satisfy the financing needs of the Corporation's clients. The associated credit risk is controlled by subjecting such activity to the same credit and quality controls as exist for the Corporation's lending and investing activities. The commitments are generally variable rate and involve diverse business and consumer customers and are generally well collateralized. Management does not anticipate that losses, if any, which may occur as a result of these commitments would materially affect the stockholders' equity of the Corporation. Since a portion of the commitments have some likelihood of not being exercised, the amounts do not necessarily represent future cash requirements.

Loan and credit line commitments totaled $13,168,959 and $19,335,429 at December 31, 2020 and 2019, respectively. These commitments are contingent upon continuing customer compliance with the terms of the agreement.

Commercial letters of credit, totaling $186,290 and $352,153 at December 31, 2020 and 2019, respectively, are obligations to make payments under certain conditions to meet contingencies related to customers' contractual agreements. They are primarily used to guarantee a customer's contractual and/or financial performance and are seldom exercised.

At December 31, 2020 and 2019, the Corporation had a reserve established for off balance sheet commitments in the amount of $95,400 and $245,400, respectively.

18. Fair Value Measurements

Accounting guidance under GAAP defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. This accounting guidance also establishes a fair value hierarchy, which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value.

The Corporation uses fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. Securities available for sale and equity securities with readily determinable fair values are recorded at fair value on a recurring basis. Additionally, from time to time, the Corporation may be required to record at fair value other assets on a nonrecurring basis, such as impaired loans, loans held for sale and other real estate owned (foreclosed assets). These nonrecurring fair value adjustments typically involve the application of lower of cost or market accounting or write downs of individual assets. In support of this principle, the FASB established a fair value hierarchy that prioritizes the information used to develop those assumptions. The fair value hierarchy is as follows:

1. Level 1 Inputs - Unadjusted quoted prices in active markets for identical assets or liabilities that the entity has the ability to access at the measurement date.

2. Level 2 Inputs - Inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. These might include quoted prices for similar assets and liabilities in active markets, and inputs other than quoted prices that are observable for the asset or liability, such as interest rates and yield curves that are observable at commonly quoted intervals.

3. Level 3 Inputs - Unobservable inputs for determining the fair values of assets or liabilities that reflect an entity's own assumptions about the assumptions that market participants would use in pricing the assets or liabilities.

The following table presents the Bank's assets measured at fair value on a recurring basis as of December 31, 2020 and 2019:

		Fair Value Measurements at Reporting Date Using		
	Fair Value	**Quoted Prices in Active Mkts. for Identical Assets (Level 1)**	**Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**
December 31, 2020				
Available-for-sale securities -				
U.S. government agencies	**$ 34,547,322**	**$ -**	**$ 34,547,322**	**$ -**
State and municipals	**$ 1,027,400**	**$ -**	**$ 1,027,400**	**$ -**
December 31, 2019				
Available-for-sale securities -				
U.S. Treasuries and government agencies	$ 27,460,639	$ -	$ 27,460,639	$ -
State and municipals	$ 3,184,212	$ -	$ 3,184,212	$ -

Securities classified as available-for-sale are reported at fair value utilizing Level 2 inputs. For these securities, the Bank obtains fair value measurements from an independent pricing service. The fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, live trading levels, trade execution data, market consensus prepayment speeds, credit information, and the terms and conditions of the security, among other things.

The following table presents the assets measured at fair value on a nonrecurring basis as of December 31, 2020 and 2019:

		Fair Value Measurements at Reporting Date Using		
	Fair Value	Quoted Prices in Active Mkts. for Identical Assets (Level 1)	Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
December 31, 2020				
Impaired loans (net of related allowances):				
Construction and Land Development	$ -	$ -	$ -	$ -
Commercial Real Estate	1,269,343	-	-	1,269,343
Residential Real Estate	-	-	-	-
Commercial and Industrial	150,129	-	-	150,129
Consumer	-	-	-	-
Total	$ 1,419,472	$ -	$ -	$ 1,419,472
Other real estate owned	$ 225,000	$ -	$ -	$ 225,000
December 31, 2019				
Impaired loans (net of related allowances)	$ 9,998,389	$ -	$ -	$ 9,998,389
Other real estate owned	$ -	$ -	$ -	$ -

Loans for which it is probable that the Corporation will not collect all principal and interest due according to contractual terms are measured for impairment as prescribed by accounting guidance for accounting by creditors for impairment of a loan. Allowable methods for estimating fair value include using the fair value of the collateral for collateral dependent loans or, where a loan is determined not to be collateral dependent, using the discounted cash flow method. In our determination of fair value, we have categorized both methods of valuation as estimates based on Level 3 inputs. Quantitative information considered in developing Level 3 Fair Value measurements at December 31, 2020 and 2019 for impaired loans include appraisal values adjusted for estimated selling costs for collateral dependent Commercial and Residential Real Estate impaired loans and discounted cash flows under modified repayment terms adjusted for third party guarantees, if any, for Commercial and Industrial impaired loans. The weighted average discount rate used at December 31, 2020 to discount cash flow dependent Commercial and Industrial impaired loans was 7.81% with rates ranging from 5.00% to 8.75%. Quantitative information considered for developing Level 3 Fair Value measurements at December 31, 2020 reflect actual sales contracts, less estimated sales costs, if any.

19. Fair Value of Financial Instruments

Accounting guidance requires the Corporation to disclose fair value information about financial instruments for which it is practicable to estimate, whether or not such fair values are reflected in the consolidated balance sheets. Estimated fair value amounts have been determined using available market information and other valuation methodologies. However, considerable judgment is required to interpret market data in developing the estimates of fair value. Accordingly, the estimates presented are not necessarily indicative of the amount that could be realized in a current market exchange. The use of different market assumptions and estimation methodologies may have a material effect on the estimated fair value amounts.

The carrying values and estimated fair values of the Corporation's financial assets and liabilities are as follows:

		Fair Value Measurements at Reporting Date Using		
	Carrying Value	Quoted Prices in Active Mkts. for Identical Assets (Level 1)	Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
December 31, 2020				
Financial assets:				
Cash and due from banks	**$ 5,562,057**	**$ 5,562,057**	**$ -**	**$ -**
Federal funds sold	**9,885,986**	**9,885,986**	**-**	**-**
Interest bearing deposits in other banks	**43,954,107**	**43,954,107**	**-**	**-**
Investment securities	**35,574,722**	**-**	**35,574,722**	**-**
Loans, net of allowances	**213,880,575**	**-**	**-**	**213,407,903**
FHLB of Atlanta stock	**280,200**	**280,200**	**-**	**-**
Accrued interest receivable	**1,571,143**	**1,571,143**	**-**	**-**
BOLI	**6,139,321**	**-**	**6,139,321**	**-**
Financial liabilities:				
Deposits	**$261,072,594**	**$ -**	**$183,146,028**	**$ 81,963,655**
Accrued interest payable	**804,007**	**804,007**	**-**	**-**
Junior subordinated debentures	**7,217,000**	**-**		**6,094,573**
Federal Reserve Bank borrowings	**32,259,756**	**-**	**32,259,756**	**-**
Other borrowings	**5,000**	**-**	**5,000**	**-**
December 31, 2019				
Financial assets:				
Cash and due from banks	$ 5,048,294	$ 5,048,294	$ -	$ -
Federal funds sold	6,334,147	6,334,147	-	-
Interest bearing deposits in other banks	63,464,039	63,464,039	-	-
Investment securities	30,644,851	-	30,644,851	-
Loans, net of allowances	195,100,676	-	-	195,106,000
FHLB of Atlanta stock	254,200	254,200	-	-
Accrued interest receivable	1,151,097	1,151,097	-	-
BOLI	5,972,648	-	5,972,648	-
Financial liabilities:				
Deposits	$283,304,359	$ -	$181,295,000	$107,580,000
Accrued interest payable	1,615,384	1,615,384	-	-
Junior subordinated debentures	7,217,000	-	7,217,000	-
Other borrowings	2,000,000	-	2,000,000	-

Commitments for off balance lending approximate fair value.

20. Risks and Contingencies

The Corporation is party to certain legal actions in the course of business. There was no material litigation against the Corporation at December 31, 2020. Management is unaware of any additional outstanding risks and contingencies as of the date that the consolidated financial statements were available for issue.

New market tax credits indemnifications

The Corporation has indemnified certain tax credit investors for potential Recapture Events in connection with the Corporation's participation in the Community Development Financial Institutions New Markets Tax Credit Program. Events of Recapture include the Corporation or the applicable community development entity ("CDE") or subsidiary CDE ("sub-CDE") ceasing to be a CDE; redemption of investment in the sub-CDE; failure to meet certain compliance requirements; and indemnitor's gross negligence, fraud, willful misconduct, malfeasance, material violation of law, or bad faith action which results in a Recapture Event. The Corporation's indemnification obligations total $19,265,979 as of December 31, 2020. The Corporation's compliance obligations associated with each indemnification will expire over time as shown in the schedule below. During 2020, none of the Corporation's compliance obligations expired. In addition, the Corporation and sub-CDE income tax returns are subject to review and examination by federal and state taxing authorities and are currently open to audit under the applicable statutes of limitations by the Internal Revenue Service ("IRS") for the years ended December 31, 2017 through and including 2020.

Maturities of compliance obligations as of December 31, 2020 are as of follows:

2021	$ 2,588,500
2022	-
2023	-
2024	6,085,400
2025	1,695,400
2026	5,065,600
2027	3,831,079
	$ 19,265,979

The Corporation is in compliance with the rules and regulations of the Community Development Financial Institutions New Markets Tax Credit Program and engages experts on an annual basis to monitor such compliance. Management believes that the probability that the Corporation's indemnification obligations will be triggered is low.

21. Subsequent Events

The Corporation has evaluated subsequent events for potential recognition and/or disclosure through March 23, 2021, the date the consolidated financial statements were available to be issued.

In 2021, the Corporation received approval to repurchase all of the remaining shares of the Corporation's common stock held by the Treasury. On February 16, 2021, the Corporation repurchased the remaining 4,287,024 shares at a price of $1,071,756.

THE HARBOR BANK OF MARYLAND

Branch Locations

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410-528-1801 or 1-888-833-7920
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Pimlico Office

5000 Park Heights Avenue
Baltimore, Maryland 21215
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Friday 9:00 a.m. to 6:00 p.m.
Saturday 9:00 a.m. to 12:00 p.m.
410-367-3331
ATM Available

Science & Technology Park East Office

855 N. Wolfe Street, Suite C
Baltimore, Maryland 21205
Monday - Thursday 9:00 a.m. to 3:00 p.m.
Friday 9:00 a.m. to 5:00 p.m.
410-675-1167
ATM Available

Research Park Office

800 West Baltimore Street
Baltimore, Maryland 21201
Monday - Thursday 9:00 a.m. to 3:00 p.m.
Friday 9:00 a.m. to 5:00 p.m.
410-545-0633
ATM Available
Safe Deposit Box Available

Randallstown Office

8530 Liberty Road
Randallstown, Maryland 21133
Monday - Thursday 9:00 a.m. to 3:00 p.m.
Friday 9:00 a.m. to 6:00 p.m.
Saturday 9:00 a.m. to 12:00 p.m.
Drive-in Hours:
Monday - Thursday 9:00 a.m. to 4:00 p.m.
Friday 9:00 a.m. to 6:00 p.m.
Saturday 9:00 a.m. to 12:00 p.m.
410-922-3003
ATM Available
Safe Deposit Box Available

Inner Harbor East Office

1000 Lancaster Street, Suite C
Baltimore, Maryland 21202
Monday - Thursday 9:00 a.m. to 3:00 p.m.
Friday 9:00 a.m. to 5:00 p.m.
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