

**QUEENSTOWN BANCORP
OF MARYLAND, INC.**



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**2021
AUDITED FINANCIAL
STATEMENTS**

AUDITED FINANCIAL STATEMENTS

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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors and Stockholders of
Queenstown Bancorp of Maryland, Inc. and Subsidiary
Queenstown, Maryland

Opinion

We have audited the consolidated financial statements of Queenstown Bancorp of Maryland, Inc. and Subsidiary (the Company), which comprise the consolidated balance sheet as of December 31, 2021, and the related consolidated statements of income, comprehensive income, changes in stockholders' equity, and cash flows for the year then ended, and the related notes to the consolidated financial statements.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2021, and the results of its operations and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Basis for Opinion

We conducted our audit in accordance with auditing standards generally accepted in the United States of America (GAAS). Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report. We are required to be independent of the Company and to meet our other ethical responsibilities, in accordance with the relevant ethical requirements relating to our audit. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Responsibilities of Management for the Consolidated Financial Statements

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

In preparing the consolidated financial statements, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the Company's ability to continue as a going concern within one year after the date that the consolidated financial statements are available to be issued.



Auditors' Responsibilities for the Audit of the Consolidated Financial Statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with GAAS will always detect a material misstatement when it exists. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Misstatements are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users made on the basis of these consolidated financial statements.

In performing an audit in accordance with GAAS, we:

- Exercise professional judgement and maintain professional skepticism throughout the audit.
- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the consolidated financial statements.
- Obtain an understanding of internal control relevant to the audit 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 Company's internal control. Accordingly, no such opinion is expressed.
- Evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the consolidated financial statements.
- Conclude whether, in our judgement, there are conditions or events, considered in the aggregate, that raise substantial doubt about the Company's ability to continue as a going concern for a reasonable period of time.

We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings, and certain internal control-related matters that we identified during the audit.

Prior Period Consolidated Financial Statements

The consolidated financial statements of Queenstown Bancorp of Maryland, Inc. and Subsidiary as of and for the year ended December 31, 2020, were audited by other auditors, whose report dated February 22, 2021, expressed an unmodified opinion on those statements.

Yount, Hyde & Barbour, P.C.

Baltimore, Maryland
March 10, 2022

QUEENSTOWN BANCORP OF MARYLAND, INC. AND SUBSIDIARY
CONSOLIDATED BALANCE SHEETS

(Dollars in thousands)

	December 31	
	2021	2020
ASSETS		
Cash and due from banks	\$ 4,536	6,603
Interest bearing deposits with banks	70,295	69,897
Total cash and cash equivalents	74,831	76,500
Securities available-for-sale (at fair value)	177,863	81,941
Federal Home Loan Bank stock (at cost)	302	439
Loans	385,104	401,680
Less allowance for loan losses	(7,401)	(7,170)
Loans, net	377,703	394,510
Premises and equipment, net	6,301	6,346
Bank owned life insurance	14,829	11,819
Deferred income taxes	3,365	2,420
Accrued interest receivable	1,741	2,240
Prepaid expenses	296	329
Other assets	856	433
TOTAL ASSETS	\$658,087	576,977
 LIABILITIES AND STOCKHOLDERS' EQUITY		
Noninterest bearing deposits	\$188,993	150,727
Interest bearing deposits	395,576	354,837
Total deposits	584,569	505,564
Accrued expenses and other liabilities	3,383	3,097
Total liabilities	587,952	508,661
 Common stock - \$10 par value; shares authorized 10,000,000, shares issued and outstanding 1,200,248 and 1,195,786 , respectively		
	12,002	11,958
Additional paid in capital	615	460
Retained earnings	59,708	55,762
Accumulated other comprehensive (loss) income	(2,190)	136
Total stockholders' equity	70,135	68,316
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$658,087	576,977

See accompanying notes to consolidated financial statements.

QUEENSTOWN BANCORP OF MARYLAND, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF INCOME

(Dollars in thousands, except per share information)

	Years Ended		
	2021	2020	2019
INTEREST INCOME:			
Interest and fees on loans	\$ 19,378	19,837	20,284
Interest and dividends on investment securities	1,608	566	435
Other interest income	288	485	884
Total interest income	21,274	20,888	21,603
INTEREST EXPENSE:			
Interest on deposits	1,764	2,720	2,455
Net interest income	19,510	18,168	19,148
Provision for loan losses	-	1,600	-
Net interest income after provision for loan losses	19,510	16,568	19,148
NONINTEREST INCOME:			
Service charges on deposit accounts	363	402	594
Other income	1,290	992	942
Net gain on sales of real estate	6	8	51
Total noninterest income	1,659	1,402	1,587
NONINTEREST EXPENSES:			
Salaries and employee benefits	7,259	6,695	6,573
Data processing and electronic banking expenses	1,009	987	1,047
Occupancy expense	669	622	638
Equipment expenses	458	415	351
FDIC insurance premiums	166	110	62
Other expenses	2,238	1,909	1,822
Total noninterest expenses	11,799	10,738	10,493
Income before income taxes	9,370	7,232	10,242
Income tax expense	2,423	1,849	2,722
Net income	\$ 6,947	5,383	7,520
Basic net income per common share	\$ 5.79	4.50	6.31
Diluted net income per common share	\$ 5.75	4.47	6.28
Basic weighted average common shares outstanding	1,199,302	1,195,322	1,191,168
Diluted weighted average common shares outstanding	1,208,576	1,205,044	1,197,659

See accompanying notes to consolidated financial statements.

QUEENSTOWN BANCORP OF MARYLAND, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Dollars in thousands)

	Years Ended		
	2021	2020	2019
Net income	\$ 6,947	5,383	7,520
Other comprehensive income (loss), before tax:			
Securities available for sale:			
Unrealized holding (losses) gains arising during the period	(3,211)	169	356
Other comprehensive income (loss), before tax	(3,211)	169	356
Income tax effect	885	(47)	(98)
Other comprehensive (loss) income, net of tax	(2,326)	122	258
Total comprehensive income	<u>\$ 4,621</u>	<u>5,505</u>	<u>7,778</u>

QUEENSTOWN BANCORP OF MARYLAND, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY

For the Years Ended December 31, 2021, 2020 and 2019

(Dollars in thousands, except per share information)

	<u>Common Stock</u>		Additional paid- in capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Totals
	Shares	Par Value				
	Balances at January 1, 2019	1,188,081				
Net Income	-	-	-	7,520	-	7,520
Other comprehensive income, net of tax	-	-	-	-	258	258
Stock options exercised	4,200	42	106	-	-	148
Stock option compensation	-	-	19	-	-	19
Cash dividends (\$2.75 per share)	-	-	-	(3,279)	-	(3,279)
Balances at December 31, 2019	1,192,281	11,923	309	53,368	14	65,614
Net Income	-	-	-	5,383	-	5,383
Other comprehensive income, net of tax	-	-	-	-	122	122
Stock options exercised	3,505	35	120	-	-	155
Stock option compensation	-	-	31	-	-	31
Cash dividends (\$2.50 per share)	-	-	-	(2,989)	-	(2,989)
Balances at December 31, 2020	1,195,786	11,958	460	55,762	136	68,316
Net Income	-	-	-	6,947	-	6,947
Other comprehensive (loss), net of tax	-	-	-	-	(2,326)	(2,326)
Restricted stock issued	562	5	28	-	-	33
Stock options exercised	3,900	39	95	-	-	134
Stock option compensation	-	-	32	-	-	32
Cash dividends (\$2.50 per share)	-	-	-	(3,001)	-	(3,001)
Balances at December 31, 2021	<u>1,200,248</u>	<u>\$ 12,002</u>	<u>615</u>	<u>59,708</u>	<u>(2,190)</u>	<u>70,135</u>

QUEENSTOWN BANCORP OF MARYLAND, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS

(Dollars in thousands)

	Years Ended		
	2021	2020	2019
OPERATING ACTIVITIES:			
Net Income	\$ 6,947	5,383	7,520
Adjustments to reconcile net income to net cash provided by operating activities:			
Premium amortization on securities	996	236	45
Depreciation and amortization	446	395	372
Net (gain) loss on sales of real estate	(6)	(8)	(51)
Provision for loan losses	-	1,600	-
Deferred tax (benefit) expense	(61)	(1,304)	355
Stock option compensation	32	31	19
Net changes in:			
Accrued interest receivable	499	(650)	38
Accrued expenses and other liabilities	286	502	298
Prepaid expenses	33	(32)	36
Other operating activities	(386)	392	17
Net cash provided by operating activities	8,786	6,545	8,649
INVESTING ACTIVITIES:			
Purchases of securities available-for-sale	(116,620)	(73,589)	(2,327)
Proceeds from calls and maturities of securities available-for-sale	5,000	2,450	1,000
Principal payments received on securities available-for-sale	11,509	4,458	1,854
Net decrease (increase) in loans	16,773	(6,635)	(14,982)
Purchases of FHLB stock	-	(7)	-
Proceeds from redemptions of FHLB stock	137	-	-
Purchases of bank owned life insurance	(3,000)	-	-
Purchases of premises and equipment	(421)	(942)	(710)
Proceeds from sales of real estate	29	97	279
Net cash (used) by investing activities	(86,593)	(74,168)	(14,886)
FINANCING ACTIVITIES:			
Net increase (decrease) in deposits	79,005	100,651	3,147
Stock options exercised	134	155	148
Dividends paid	(3,001)	(2,989)	(3,279)
Net cash provided by financing activities	76,138	97,817	16
Net (decrease) increase in cash and cash equivalents	(1,669)	30,194	(6,221)
Cash and cash equivalents at beginning of year	76,500	46,306	52,527
Cash and cash equivalents at end of year	\$ 74,831	76,500	46,306
Supplemental disclosures:			
Interest payments	\$ 2,277	2,747	2,435
Income tax payments	2,509	3,043	2,503
Noncash investing and financing activities:			
Transfers to other real estate	-	-	266

See accompanying notes to consolidated financial statements.

QUEENSTOWN BANCORP OF MARYLAND, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEARS ENDED DECEMBER 31, 2021, 2020 AND 2019 (Dollars in thousands, except per share information)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting and reporting policies of the Company, which includes Queenstown Bancorp of Maryland, Inc. and its wholly owned subsidiary, Queenstown Bank of Maryland (the Bank), conform to accounting principles generally accepted in the United States of America and to general practices in the banking industry. Certain reclassifications have been made to amounts previously reported to conform with the classifications made in 2021.

Basis of Presentations

The consolidated financial statements include the accounts of Queenstown Bancorp of Maryland, Inc. and its subsidiary, Queenstown Bank of Maryland, with all significant intercompany transactions eliminated.

Nature of Operations

The Company provides a full range of banking services to individuals and businesses through its main office and five branches in Queen Anne's County and one branch each in Talbot County and Caroline County Maryland. The Company also operates a loan production office in Dorchester County. Its primary deposit products are certificates of deposit and demand, savings, and money market accounts. Its primary lending products are commercial and consumer loans and real estate mortgages. The Company's loan portfolio has a concentration of residential and commercial real estate loans in Queen Anne's County and the surrounding area.

Use of Estimates

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

Securities

At the purchase date, the Company classifies securities as held to maturity or available for sale. Interest and dividend income on securities are recognized in interest income on the accrual basis. Premiums and discounts on securities are amortized as an adjustment to yield using the interest method. Premiums are amortized through the earliest call date. Discounts are accreted through the maturity date.

Debt securities acquired with both the intent and ability to hold to maturity are classified as held to maturity and reported at amortized cost. Federal Home Loan Bank stock is carried at cost and is restricted as to marketability.

Securities classified as available-for-sale are used as part of the Company's asset/liability management strategy. Sales may occur in response to changes in interest rate conditions, balance sheet composition or other economic factors. All debt securities classified as available for sale are reported at estimated fair value, with unrealized gains and losses reported as accumulated other comprehensive income or loss, net of deferred income taxes, in the stockholders' equity section of the Consolidated Balance Sheets.

Gains or losses realized from the sale of securities are determined by specific identification and are included in noninterest income. The Company evaluates each investment security in an unrealized loss position for other than temporary impairment. If management determines that all contractual obligations from an investment may not be received, then other than temporary impairment would be recognized. The unrealized loss for other than temporary impairment on debt securities are reported in current period earnings.

Loans

Loans are stated at their principal balance outstanding net of deferred loan fees and costs. Overdrafts are included in loans outstanding. Interest income on loans is accrued at the contractual rate on the principal amount outstanding. The Company places loans, except for consumer, on nonaccrual 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. Generally, consumer loans are not placed on nonaccrual, but are charged off when they are over 100 days past due. Interest received on impaired loans placed on nonaccrual status is generally applied to reduce the carrying value of the loan or, if principal is considered fully collectible, recognized as interest income. For all other loans, loan balances are charged off when it becomes evident that such balances are not fully collectible. For loans secured by real estate, the excess of the loan balances over the net realizable value of the property collateralizing the loan is charged off. Accrual of interest resumes when the loan is brought current and the borrower demonstrates the ability to service the debt on a current basis.

Loans are considered impaired, based upon current information and circumstances, if it is probable that the Company will not collect all principal and interest payments according to contractual terms. Restructured loans, meeting the definition of troubled debt restructurings, are considered impaired loans. Impaired loans do not include large groups of smaller balance homogeneous loans that are evaluated collectively for impairment such as consumer installment loans. The impairment of a loan is measured by the present value of expected future cash flows discounted at the loan's effective interest rate, or the fair value of the collateral if the repayment is expected to be provided by the collateral.

Loan origination fees and certain direct loan origination costs are being deferred and the net amount is amortized over the contractual life of the loan as an adjustment to the loan's yield.

Allowance for Loan Losses

The allowance for loan losses is maintained at a level which, in management's judgment, is adequate to absorb credit losses inherent in the loan portfolio. The allowance is determined by management's evaluation of the loan and lease portfolio based on such factors as the differing economic risks associated with each loan category, the current financial condition of specific borrowers, the economic environment in which borrowers operate, the level of delinquent loans, the value of any collateral and, where applicable, the existence of any guarantees or indemnification. As a result, these judgments are inherently subjective and involve material estimates that may be susceptible to significant change. The allowance is increased by the loan loss provision charged to operating expenses and reduced by charge-offs, net of recoveries. The provision for loan losses is based on the ongoing review of the loan portfolios, past loss experience and current economic conditions which could impact the borrowers' repayment performance.

Premises and Equipment

Premises and equipment are stated at cost less accumulated depreciation and amortization. Land is stated at cost. The Company's policy is to provide for depreciation of physical properties over their estimated useful lives or the lease term (whichever is shorter) as a charge to operations at straight-line rates. Expenditures for maintenance, repairs and minor renewals are charged to operations; expenditures for betterments are charged to the property accounts. Upon retirement or other disposition of properties, the carrying value and the related accumulated depreciation or amortization are removed from the accounts.

Advertising Costs

Advertising costs are expensed as incurred.

Off-Balance Sheet Credit Risk

The Company issues financial or standby letters of credit that represent conditional commitments to fund transactions by the Company, typically to guarantee performance of a customer to a third party related to borrowing arrangements. The credit risk associated with issuing letters of credit is essentially the same as occurs when extending loan facilities to borrowers. The Company monitors the exposure to the letters of credit as part of its credit review process. Extensions of letters of credit, if any, would become part of the loan balance outstanding and would be evaluated in accordance with the Company's credit policies. Potential exposure to loss for unfunded letters of credit if deemed necessary would be recorded in other liabilities.

Other Real Estate

Real estate properties acquired through, or in lieu of, loan foreclosure are held for sale and carried at the lower of fair value minus estimated costs of disposal or cost. Fair value is based on independent appraisals and other relevant factors. At the time of acquisition any excess of loan balance over fair value is charged to the allowance for loan losses.

Income Taxes

Deferred income taxes are calculated by applying enacted statutory tax rates to temporary differences consisting of all significant items which are reported for tax purposes in different years than for accounting purposes. Deferred tax assets are recognized only to the extent that it is more likely than not that such amounts will be realized based on considerations of available evidence. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

Per Share Data

Basic net income per share is computed by dividing the net income by the weighted average number of shares of common stock outstanding during the year presented. Diluted net income per share is computed by dividing net income by the weighted average number of shares of common stock plus the assumed conversions of common stock equivalents outstanding using the treasury method.

Subsequent Events

Subsequent events have been evaluated for potential recognition and disclosure through the date of the independent auditors' report, the date these consolidated financial statements were available to be issued. No subsequent events were identified that would affect the presentation of the consolidated financial statements.

Statement of Cash Flows

For purposes of reporting cash flows, cash equivalents are composed of cash and due from banks and interest bearing deposits with banks.

Comprehensive Income

Accounting principles generally accepted in the United States of America require that recognized revenue, expenses, gains, and losses be included in net income. However, certain changes in assets and liabilities, such as unrealized gains and losses on available for sale securities, are reported as a separate component of the stockholders' equity section of the consolidated balance sheet. Such items, along with net income, are components of comprehensive income.

Recent Accounting Pronouncements

During February 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2016-02, “Leases (Topic 842).” Among other things, in the amendments in ASU 2016-02, lessees will be required to recognize the following for all leases (with the exception of short-term leases) at the commencement date: (1) a lease liability, which is a lessee’s obligation to make lease payments arising from a lease, measured on a discounted basis; and (2) a right-of-use asset, which is an asset that represents the lessee’s right to use, or control the use of, a specified asset for the lease term.. The ASU was initially effective for non-public business entities’ financial statements issued for fiscal years beginning after December 15, 2019, and interim periods within fiscal years beginning after December 15, 2020. In June 2020, the FASB issued ASU 2020-05. Under ASU 2020-05, private companies may apply the new leases standard for fiscal years beginning after December 15, 2021, and to interim periods within fiscal years beginning after December 15, 2022. The Company does not expect the adoption of this standard to have a material impact on our consolidated financial statements.

During June 2016, the FASB issued ASU 2016-13, “Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments.” The amendments in this ASU, among other things, require the measurement of all expected credit losses for financial assets held at the reporting date based on historical experience, current conditions, and reasonable and supportable forecasts. Financial institutions and other organizations will now use forward-looking information to better inform their credit loss estimates. Many of the loss estimation techniques applied today will still be permitted. . In addition, the ASU amends the accounting for credit losses on available-for-sale debt securities and purchased financial assets with credit deterioration. The FASB has issued multiple updates to ASU 2016- 13 as codified in Topic 326, including ASU’s 2019-04, 2019-05, 2019-10, 2019-11, 2020-02, and 2020-03. The ASU is effective for fiscal years beginning after December 15, 2022, including interim periods within those fiscal years. The Company is currently evaluating the potential impact of this standard on our consolidated financial statements.

During December 2019, the FASB issued ASU 2019-12, “Income Taxes (Topic 740) – Simplifying the Accounting for Income Taxes.”, which simplifies the accounting for income taxes by removing multiple exceptions to the general principals in Topic 740. The amendments are effective for fiscal years beginning after December 15,2021 and interim periods within fiscal years beginning after December 15,2022. The Company does not expect the adoption of these amendments to have a material impact on our consolidated financial statements.

In March 2020, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2020-04 “Reference Rate Reform (Topic 848): Facilitation of the Effects of Reference Rate Reform on Financial Reporting.” The new standard results from the London Interbank Offered Rate (“LIBOR”) being discontinued as an available benchmark rate. The standard is elective and provides optional expedients and exceptions for applying GAAP to contracts, hedging, or other transactions that reference LIBOR, or another reference rate expected to be discontinued. The amendments in the update are effective for all entities between March 12,2020 and December 31, 2022. The Company has few transactions referencing LIBOR and has begun transitioning to alternative rates, consistent with industry guidelines.

2. SECURITIES

The amortized cost, gross unrealized gains and losses, and fair values of securities are as follows:

	December 31, 2021			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available-for-sale				
U.S. treasuries and government agencies	\$ 27,136	94	285	26,945
State and municipal	37,845	69	709	37,205
Mortgage - backed	112,894	67	2,224	110,737
Corporate debt	3,011	-	35	2,976
Totals	\$ 180,886	230	3,253	177,863

	December 31, 2020			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available-for-sale				
U.S. treasuries and government agencies	\$ 12,626	1	54	12,573
State and municipal	23,509	229	69	23,669
Mortgage - backed	45,617	241	159	45,699
Totals	\$ 81,752	471	282	81,941

The table below shows our securities' gross unrealized losses and fair value, aggregated by category and length of time that individual securities have been in a continuous unrealized loss position, at December 31, 2021 and 2020.

	Less than 12 months		12 months or more		Totals	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
	As of December 31, 2021					
U.S. treasuries and government agencies	\$ 14,693	182	1,457	103	16,150	285
State and municipal	22,843	418	7,787	291	30,630	709
Mortgage - backed	82,172	1,434	22,731	790	104,903	2,224
Corporate debt	2,976	35	-	-	2,976	35
Totals	\$ 122,684	2,069	31,975	1,184	154,659	3,253
As of December 31, 2020						
U.S. treasuries and government agencies	\$ 9,741	47	872	7	10,613	54
State and municipal	7,380	69	-	-	7,380	69
Mortgage - backed	25,239	159	41	-	25,280	159
Totals	\$ 42,360	275	913	7	43,273	282

The unrealized losses that exist are the result of changes in market interest rates since original purchases. These unrealized losses are considered temporary in nature and will decline over time and recover as these securities approach maturity.

The amortized cost and fair values of debt securities at December 31, 2021 by contractual maturity are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Available-for-Sale	
	Amortized Cost	Fair Value
As of December 31, 2021		
One to five years	\$ 7,247	7,117
Five to ten years	35,292	34,747
After ten years	25,453	25,262
	<u>67,992</u>	<u>67,126</u>
Mortgage-backed	112,894	110,737
Totals	<u>\$ 180,886</u>	<u>177,863</u>

There were no sales of securities in 2021, 2020 nor 2019.

At December 31, 2021 and 2020, securities with a carrying value of \$22,856 thousand and \$6,814 thousand respectively, were pledged as collateral for certain government deposits and for other purposes as required or permitted by law.

3. LOANS

At December 31, 2021 and 2020, loans are as follows:

	2021	2020
Real estate:		
Construction and land development	\$ 37,215	\$ 30,602
Secured by farmland	31,253	34,028
Commercial	133,916	123,378
Residential	160,124	178,022
Commercial and agricultural	16,014	13,916
U.S. S.B.A. Paycheck Protection Program Loans	430	15,019
Consumer	6,152	6,715
Totals	<u>\$ 385,104</u>	<u>401,680</u>

Unamortized net deferred loan costs amounted to \$397 thousand and \$50 thousand at December 31, 2021 and 2020.

A summary of current, past due, and nonaccrual loans as of December 31, 2021 and 2020 was as follows:

	Current	30-89 Days Past Due	90 Days or more Past Due and accruing	Nonaccrual	Total
As of December 31, 2021					
Real estate:					
Construction and land development	\$ 37,215	-	-	-	37,215
Secured by farmland	30,693	-	-	560	31,253
Commercial	132,708	128	314	766	133,916
Residential	159,643	238	104	139	160,124
Commercial and agricultural	16,014	-	-	-	16,014
U.S. S.B.A. Paycheck Protection Program Loans	430	-	-	-	430
Consumer	6,149	3	-	-	6,152
Totals	<u>\$ 382,852</u>	<u>369</u>	<u>418</u>	<u>1,465</u>	<u>385,104</u>

	Current	30-89 Days Past Due	90 Days or more Past Due and accruing	Nonaccrual	Totals
As of December 31, 2020					
Real estate:					
Construction and land development	\$ 30,602	-	-	-	30,602
Secured by farmland	33,170	283	-	575	34,028
Commercial	122,158	327	-	893	123,378
Residential	175,771	995	696	560	178,022
Commercial and agricultural	13,876	40	-	-	13,916
U.S. Paycheck Protection Program Loans	15,019	-	-	-	15,019
Consumer	6,679	36	-	-	6,715
Totals	\$ 397,275	1,681	696	2,028	401,680

Loans on which the accrual of interest has been discontinued totaled \$1,465 and \$2,028 thousand at December 31, 2021 and 2020 respectively. Interest that would have been accrued on these loans totaled \$93 thousand and \$132 thousand for the years ended December 31, 2021 and 2020 respectively. At December 31, 2021 there were residential mortgages in the process of foreclosure totaling \$157 thousand.

4. ALLOWANCE FOR LOAN LOSSES AND IMPAIRED LOANS

Changes in the allowance for credit losses for the year ended December 31, 2021 and 2020 were as follows:

	Real estate construction	Real estate residential	Real estate commercial and farmland	Commercial and agriculture	Consumer	Totals
As of December 31, 2021						
Beginning Balance	\$ 741	1,751	4,496	136	46	7,170
Provision for loan losses	(457)	(823)	1,306	(1)	(25)	-
Net charge-offs:						
Charge-offs	-	(45)	-	(42)	(22)	(109)
Recoveries	14	173	87	45	21	340
Net (charge-offs) recoveries	14	128	87	3	(1)	231
Ending balance	\$ 298	1,056	5,889	138	20	7,401
As of December 31, 2020						
Beginning Balance	\$ 148	2,044	3,449	96	15	5,752
Provision for loan losses	530	(323)	1,242	110	41	1,600
Net charge-offs:						
Charge-offs	(8)	(3)	(228)	(99)	(20)	(358)
Recoveries	71	33	33	29	10	176
Net (charge-offs) recoveries	63	30	(195)	(70)	(10)	(182)
Ending balance	\$ 741	1,751	4,496	136	46	7,170

Although the above allocation is performed, the allowance for loan losses is general in nature and is available to absorb losses from any loan type.

The process for calculating the adequacy of the allowance for loan losses encompasses loss estimates attributable to specific troubled credits identified during the credit review process and estimates of losses inherent in other loans not reviewed specifically. The process of determining the level of the allowance for loan losses involves classifying the loans according to characteristics of loss risk for nonperforming and criticized loans and by type of loan for all other loans. For nonaccrual loans, loans over 89 days past due accruing and any other criticized loans according to the Company's loan rating system, the loans are first reviewed for specific loss measurement. Measurement of the specific loss component is based on expected future cash flows, collateral values and other relevant factors impacting the borrower's ability to pay. The Company utilizes a loan rating system which is applied to all loans but is particularly designed for monitoring loss characteristics of the real estate and commercial loan portfolios. Loan ratings are continually monitored by the loan officer and the credit review department in accordance with the loan rating guidelines established in the loan policy. Factors considered in assigning loan ratings include borrower specific cash flows and financial condition analyses, collateral values, payment status and other relevant data impacting repayment ability. Loss allocations assigned to the various loan type pools are continually monitored and adjusted for adequacy based on trends in portfolio charge-offs and recoveries, trends in portfolio delinquencies and impaired loans, changes in the risk profile of the pools, and changes in trends within the local economy.

Loans that have their terms restructured (e.g., interest rates, loan maturity date, payment and amortization period, etc.) in circumstances that provide payment relief or other concessions to a borrower experiencing financial difficulty are considered trouble debt restructured loans. All restructurings that constitute concessions to a troubled borrower are considered impaired loans that may either be in accruing status or non-accruing status. Troubled debt restructurings are considered to be impaired loans and for purposes of establishing the allowance for loan losses are evaluated for impairment giving consideration to the impact of the modified loan terms and the present value of the loan's expected cash flows. Impairment of troubled debt restructurings that have subsequently defaulted may also be measured based on the loan's observable market price or the fair value of collateral if the loan is collateral-dependent. Non-accruing restructured loans may return to accruing status provided there is a sufficient period of payment performance in accordance with the restructure terms. Loans may be removed from the restructured category in the year subsequent to the restructuring if their revised terms are considered to be consistent with terms that can be obtained in the credit market for loans with comparable risk. At December 31, 2021 restructured loans totaled \$5,735 thousand, of which \$4,387 thousand were accruing and \$1,348 thousand were non-accruing. Restructured loans at December 31, 2020 totaled \$6,572 thousand, of which \$5,072 thousand were accruing and \$1,500 thousand were non-accruing.

The following table provides information with respect to impaired loans as of and for the years ended December 31, 2021 and 2020.

	2021	2020
Impaired loans with a valuation allowance	\$ 2,474	2,690
Impaired loans without a valuation allowance	3,483	5,106
Total impaired loans	<u>\$ 5,957</u>	<u>7,796</u>
Allowance for loan losses applicable to impaired loans	\$ 228	206
Allowance for loan losses applicable to other loans	7,173	6,964
Total allowance for loan losses	<u>\$ 7,401</u>	<u>7,170</u>
Average recorded investment in impaired loans	\$ 6,876	8,517

The following table provides information on impaired loans by loan category as of December 31, 2021 and 2020:

	Recorded investment	Unpaid principal balance	Related allowance	Average recorded investment
As of December 31, 2021				
With a related allowance recorded:				
Real estate – residential	\$ 1,913	1,917	182	2,019
Real estate – commercial & farmland	561	561	46	563
Totals	<u>\$ 2,474</u>	<u>2,478</u>	<u>228</u>	<u>2,582</u>

As of December 31, 2021				
Without a related allowance recorded:				
Real estate – residential	\$ 1,867	2,266	-	2,500
Real estate – commercial & farmland	1,447	1,898	-	1,520
Commercial & agricultural	169	169	-	274
Totals	<u>\$ 3,483</u>	<u>4,333</u>	<u>-</u>	<u>4,294</u>

As of December 31, 2020				
With a related allowance recorded:				
Real estate – residential	2,125	2,130	170	1,947
Real estate – commercial & farmland	565	565	36	637
Totals	<u>\$ 2,690</u>	<u>2,695</u>	<u>206</u>	<u>2,584</u>

As of December 31, 2020				
Without a related allowance recorded:				
Real estate – residential	3,133	3,653	-	3,272
Real estate – commercial & farmland	1,593	1,977	-	1,835
Commercial & Agricultural	380	380	-	489
Totals	<u>\$ 5,106</u>	<u>6,010</u>	<u>-</u>	<u>5,596</u>

During 2020, the Bank provided short-term deferrals of loan principal and/or interest payments for generally up to six months for borrowers who were affected by the COVID-19 pandemic. Borrowers receiving deferrals were required to meet certain criteria, such as being in good standing, and not more than 30 days past due prior to the pandemic. Certain borrowers requested additional deferrals due to the continuing impact of the pandemic. At December 31, 2021, all loans that received COVID-19 related deferrals have resumed repayment.

The following table summarizes the loan risk ratings applied to the Company's real estate mortgages and commercial loans as of December 31, 2021 and 2020. Criticized loans are considered inadequately protected by the current paying capacity of the borrower or of the collateral pledged, if any. These loans have weaknesses that jeopardize the liquidation of the debt. Loans not meeting the definition of criticized are considered pass rated loans. U.S. Paycheck Protection Program Loans and Consumer Loans are not risk rated by the Company, so they are excluded from the tables below.

	Real estate construction	Real estate residential	Real estate commercial and farmland	Commercial and agriculture	Totals
As of December 31, 2021					
Pass	\$ 37,215	159,520	159,746	16,014	372,495
Criticized accrual	-	465	4,097	-	4,562
Criticized nonaccrual	-	139	1,326	-	1,465
Total	\$ 37,215	160,124	165,169	16,014	378,522
As of December 31, 2020					
Pass	\$ 29,814	174,924	151,758	13,666	370,162
Criticized accrual	788	2,538	4,180	250	7,756
Criticized nonaccrual	-	560	1,468	-	2,028
Totals	\$ 30,602	178,022	157,406	13,916	379,946

At December 31, 2021 and 2020 the allocation of the allowance for loan losses summarized on the basis of impairment methodology was as follows:

	Real estate construction	Real estate residential	Real estate commercial and farmland	Commercial and agriculture	Consumer	Totals
As of December 31, 2021						
Individually evaluated for impairment	\$ -	182	46	-	-	228
Collectively evaluated for impairment	298	874	5,843	138	20	7,173
Total	\$ 298	1,056	5,889	138	20	7,401
As of December 31, 2020						
Individually evaluated for impairment	\$ -	170	36	-	-	206
Collectively evaluated for impairment	741	1,581	4,460	136	46	6,964
Totals	\$ 741	1,751	4,496	136	46	7,170

The recorded investment in loans summarized based on impairment methodology as of December 31, 2021 and 2020 was as follows:

	Real estate construction	Real estate residential	Real estate commercial and farmland	Commercial and agriculture	S.B.A. Paycheck Protection	Consumer	Total
As of December 31, 2021							
Individually evaluated for impairment	\$ -	3,780	2,008	169	-	-	5,957
Collectively evaluated for impairment	37,215	156,344	163,161	15,845	430	6,152	379,147
Total	<u>\$ 37,215</u>	<u>160,124</u>	<u>165,169</u>	<u>16,014</u>	<u>430</u>	<u>6,152</u>	<u>385,104</u>
As of December 31, 2020							
Individually evaluated for impairment	\$ -	5,258	2,158	380	-	-	7,796
Collectively evaluated for impairment	30,602	172,764	155,248	13,536	15,019	6,715	393,884
Total	<u>\$ 30,602</u>	<u>178,022</u>	<u>157,406</u>	<u>13,916</u>	<u>-</u>	<u>6,715</u>	<u>401,680</u>

Information on troubled debt restructurings for the year ended December 31, 2021 and 2020 is as follows:

	Number of contracts	Pre-modification outstanding recorded investment	Post-modification outstanding recorded investment
As of December 31, 2021			
Real estate – residential accrual	18	\$ 4,541	\$ 3,537
Real estate – commercial accrual	2	893	681
Commercial & agricultural- accrual	1	274	169
Real estate – residential nonaccrual	1	129	22
Real estate- commercial nonaccrual	2	1,149	766
Real estate – farmland nonaccrual	1	818	560
Totals	<u>25</u>	<u>\$ 7,804</u>	<u>\$ 5,735</u>
As of December 31, 2020			
Real estate – residential accrual	20	\$ 4,997	\$ 4,003
Real estate – commercial accrual	2	893	689
Commercial & agricultural accrual	2	825	380
Real estate – residential nonaccrual	1	129	31
Real estate- commercial nonaccrual	2	1,149	894
Real estate – farmland nonaccrual	1	818	575
Totals	<u>28</u>	<u>\$ 8,811</u>	<u>\$ 6,572</u>

During 2021, there were no loans modified that were considered TDRs. During 2020, there was one loan modified as a TDR with a balance of approximately \$79 thousand. At December 31, 2021 there are no commitments to lend additional funds to any borrower whose loan terms have been modified in a troubled debt restructuring. Information on the payment status of troubled debt restructurings is as follows:

	2021	2020
Current	\$ 4,196	5,072
30-89 days past due accruing	191	-
90 days or more past due accruing	-	-
Nonaccruals	1,348	1,500
Totals	<u>\$ 5,735</u>	<u>6,572</u>

5. PREMISES AND EQUIPMENT

Premises and equipment consisted of the following:

	December 31	
	2021	2020
Land	1,885	1,908
Leasehold improvements	161	161
Buildings and land improvements	7,339	7,228
Furniture and equipment	3,440	3,129
	12,825	12,426
Accumulated depreciation and amortization	(6,524)	(6,080)
Premises and equipment – net	<u>\$ 6,301</u>	<u>6,346</u>

Depreciation expense was \$446 thousand, \$395 thousand and \$372 thousand for each of the years ended December 31, 2021, 2020 and 2019, respectively.

Rent expense applicable to operating leases amounted to \$34 thousand for 2021 and 2020, and \$39 thousand for 2019. The Bank has lease obligations for office locations. Future minimum lease payments subsequent to 2021 are \$9 thousand for 2022.

6. DEPOSITS

A breakdown of interest bearing deposits at December 31, 2021 and 2020, by type of account is as follows:

	2021	2020
Savings and money market	\$ 174,355	131,014
Interest bearing demand	84,273	66,987
Time deposits through \$250,000	109,795	119,102
Time deposits of more than \$250,000	27,153	37,734
Total interest bearing deposits	<u>\$ 395,576</u>	<u>354,837</u>

At December 31, 2021, the scheduled maturities of time deposits are as follows:

2022	\$ 81,124
2023	35,770
2024	4,443
2025	9,839
2026	5,772
	<u>\$ 136,948</u>

Interest on deposits for the years ended December 31, 2021, 2020 and 2019 consisted of the following:

	2021	2020	2019
Savings and money market	\$ 245	197	166
Interest bearing demand	213	253	186
Time deposits more than \$ 250,000	325	583	472
Other time deposits	981	1,687	1,631
Total interest on deposits	<u>\$ 1,764</u>	<u>2,720</u>	<u>2,455</u>

7. BORROWINGS AND CREDIT FACILITIES

Short-term borrowings consist of advances from the Federal Home Loan Bank of Atlanta with original maturities of up to one year and federal funds purchased from correspondent banks. There were no short-term borrowings outstanding during 2021 and 2020.

At December 31, 2021, credit available under the FHLB credit facility approximates \$54 million with letters of credit issued for the benefit of public funds depositors of \$37 million outstanding. The Bank is required to maintain an investment in stock of the FHLB in the amount of \$302 thousand as a condition for the credit facility. The Bank has also pledged its portfolios of 1-4 family first and second mortgage loans plus home equity loans as collateral for this credit facility. Certain qualifying commercial mortgages are also pledged as collateral for this credit facility. Principal balances outstanding on these mortgage loans total approximately \$177 million at December 31, 2021.

8. STOCKHOLDERS' EQUITY

The Board of Directors has approved plans authorizing the Company to purchase shares of its common stock. Purchased shares will be used for corporate purposes including issuance under the Company's stock based compensation plans. The number of shares remaining available for purchase under the plans was 111,641 shares at December 31, 2021.

Cash dividends paid to the holding company by its wholly owned subsidiary, Queenstown Bank of Maryland were \$3 million for 2021.

The Company and the Bank are subject to various regulatory capital requirements. Failure to meet minimum capital requirements can initiate certain mandatory - and possibly additional discretionary - actions by regulators that, if undertaken, could have a direct material effect on the Company's and the Bank's financial statements. Regulatory non-objection may be required to pay certain dividends. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Company and the Bank must meet specific capital guidelines that involve quantitative measures of the Company's assets, liabilities, and certain off-balance sheet items as calculated under regulatory capital practices. The Company'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 Company and the Bank to maintain amounts and ratios (as set forth in the following table) of total and Tier I Capital (as defined in the regulations) to risk-weighted assets (as defined). As of December 31, 2021, the capital levels of the Company and the Bank exceed all capital adequacy requirements to which they are subject.

As of December 31, 2021, the most recent notification from the Bank's primary regulators categorized the Bank as well capitalized under the prompt corrective action regulations. To be categorized as well capitalized, a bank must maintain a minimum total risk-based, Tier I risk-based and Tier I leverage ratios as set forth in the following tables. There are no conditions or events since the last notifications that management believes have changed the Company's and Bank's category. Actual capital amounts and ratios are presented in the following table for the Company and the Bank.

	Amount	Actual Ratio	For Capital Adequacy Purposes	To Be Well Capitalized Under Prompt Corrective Action Provisions
As of December 31, 2021				
Total capital (to risk weighted assets):				
Company (consolidated)	\$ 77,602	18.47%	8%	
Bank	77,248	18.39%	8%	10%
Tier I capital (to risk weighted assets):				
Company (consolidated)	72,325	17.22%	6%	
Bank	71,971	17.13%	6%	8%
Common equity tier I				
Company (consolidated)	72,325	17.22%	4.50%	
Bank	71,971	17.13%	4.50%	6.50%
Tier I capital (to average assets):				
Company (consolidated)	72,325	10.81%	4%	
Bank	71,971	10.77%	4%	5%
As of December 31, 2020				
Total capital (to risk weighted assets):				
Company (consolidated)	\$ 72,841	19.67%	8%	
Bank	72,655	19.64%	8%	10%
Tier I capital (to risk weighted assets):				
Company (consolidated)	68,180	18.41%	6%	
Bank	67,998	18.37%	6%	8%
Common equity tier I				
Company (consolidated)	68,180	18.41%	4.50%	
Bank	67,998	18.37%	4.50%	6.50%
Tier I capital (to average assets):				
Company (consolidated)	68,180	11.92%	4%	
Bank	67,998	11.89%	4%	5%

9. INCOME TAXES

Applicable income taxes on net income for 2021, 2020 and 2019 consist of the following:

	2021	2020	2019
Current income tax expense:			
Federal	\$ 1,745	2,202	1,642
State	739	951	725
	<u>2,484</u>	<u>3,153</u>	<u>2,367</u>
Deferred income tax (benefit) expense:			
Federal	(36)	(899)	268
State	(25)	(405)	87
	<u>(61)</u>	<u>(1,304)</u>	<u>355</u>
Total income tax expense	<u>\$ 2,423</u>	<u>1,849</u>	<u>2,722</u>

Components of deferred income tax (benefit) expense for 2021, 2020 and 2019 consist of the following:

	2021	2020	2019
Provision for loan losses	\$ (64)	(1,257)	432
Loan fees and costs	85	(132)	11
Deferred compensation	(71)	(60)	(77)
Depreciation and amortization	36	70	86
Interest income	(57)	(7)	(105)
Other real estate owned sales	-	73	-
Stock option compensation	10	9	8
Total deferred income tax (benefit) expense	<u>\$ (61)</u>	<u>(1,304)</u>	<u>355</u>

A reconciliation of income taxes computed at the maximum statutory federal tax rate to total income taxes for the years ended December 31, 2021, 2020, and 2019 follows:

	2021		2020		2019	
	Amount	Percent	Amount	Percent	Amount	Percent
Tax computed at statutory rate	\$ 1,968	21.0%	1,519	21.0%	2,151	21.0%
Increase (decrease) resulting from						
Tax-exempt interest income	(36)	-0.4%	(28)	-0.4%	(16)	-0.2%
Bank owned life insurance income	(85)	-0.9%	(65)	-0.9%	(64)	-0.6%
State income tax, net of federal income tax benefit	562	6.0%	431	6.0%	641	6.3%
Other	14	0.2%	(8)	-0.1%	10	0.1%
Total income taxes	<u>\$ 2,423</u>	<u>25.9%</u>	<u>1,849</u>	<u>25.6%</u>	<u>2,722</u>	<u>26.6%</u>

Significant components of the Company's deferred tax assets and liabilities at December 31, 2021 and 2020 are as follows:

	2021	2020
Deferred tax assets:		
Allowances for credit losses	\$2,036	1,972
Deferred compensation	661	590
Interest income	254	197
Stock options	-	10
Others	3	3
Unrealized loss on securities available-for-sale	832	-
Total deferred tax assets	<u>3,786</u>	<u>2,772</u>
Deferred tax liabilities:		
Accumulated depreciation and amortization	322	286
Loan fees and costs	99	14
Unrealized gain on securities available-for-sale	-	52
Total deferred tax liabilities	<u>421</u>	<u>352</u>
Net deferred tax assets	<u>\$3,365</u>	<u>2,420</u>

Management has determined that no valuation allowance is required as it is more likely than not that the net deferred tax assets will be fully realizable in future years. The Company remains subject to examination of income tax returns for the years ending after December 31, 2017.

10. RETIREMENT PLANS AND OTHER EMPLOYEE BENEFIT AGREEMENTS

The Company has a Section 401(k) profit sharing plan which covers substantially all employees who meet certain service requirements. Employer contributions to the plan include a discretionary contribution and matching contributions of a percentage of employee elective salary deferral contributions. Employer contributions included in operating expenses for 2021, 2020 and 2019 were \$181 thousand, \$152 thousand, and \$161 thousand, respectively.

The Company has provided additional retirement benefits as well as pre-retirement death benefits to selective executives through deferred compensation agreements. The deferred compensation plan agreements provide for monthly benefit payments for fifteen years after retirement. Benefit payments were \$109 thousand, \$109 thousand, and \$62 thousand, for 2021, 2020 and 2019, respectively. The Company is accruing the present value of these benefits over the remaining number of years to the employees' retirement dates. Benefit accruals included in operating expenses for 2021, 2020 and 2019 were \$292 thousand, \$218 thousand, and \$287 thousand, respectively. The accrued liability for deferred compensation agreements were \$1,962 thousand at December 31, 2021 and \$1,779 thousand at December 31, 2020.

The Company provides retirement benefits to directors. The agreements provide for annual benefit payments for ten years after retirement. Benefit payments were \$23 thousand, \$23 thousand, and \$11 thousand, for 2021, 2020 and 2019, respectively. The Company is accruing the present value of these benefits over the remaining number of years to the directors' retirement dates. Benefit accruals included in operating expenses for 2021, 2020 and 2019, were \$68 thousand, \$97 thousand and \$64 thousand, respectively. The accrued liability for deferred compensation for directors was \$373 thousand at December 31, 2021 and \$327 thousand at December 31, 2020.

11. STOCK-BASED COMPENSATION

The Company has a qualified incentive stock option plan for officers and employees and a nonqualified stock option plan for directors. The total number of shares of Common Stock that may be granted is 126,000 for the incentive plan and 63,000 for the nonqualified plan. Information with respect to the options granted is as follows:

	2021		2020		2019	
	Options Outstanding	Weighted Average Exercise price	Options Outstanding	Weighted Average Exercise price	Options Outstanding	Weighted Average Exercise price
Balance, January 1	27,225	\$ 36.78	37,130	\$ 38.61	50,730	\$ 41.01
Options granted	-	-	-	-	-	-
Options exercised	(3,900)	34.31	(3,505)	43.13	(4,200)	35.14
Options forfeited	-	-	(1,000)	34.00	(600)	40.00
Options expired	-	-	(5,400)	45.78	(8,800)	54.00
Balance, December 31	23,325	\$ 37.19	27,225	\$ 36.78	37,130	\$ 38.61
Options exercisable, December 31	20,725	\$ 36.84	19,625	\$ 36.26	23,530	\$ 39.13

Stock options outstanding at December 31, 2021 were as follows:

Exercise Price Range	Issued and Outstanding Options			Exercisable (Vested) Options		
	Number Outstanding	Weighted Average Remaining Life (years)	Weighted Average Exercise Price	Number Exercisable	Weighted Average Remaining Life (years)	Weighted Average Exercise Price
\$0.00 through \$34.99	10,925	5.34	\$ 34.00	10,925	5.34	\$ 34.00
\$35.00 through \$54.99	12,400	6.28	\$ 40.00	9,800	6.28	\$ 40.00
Totals:	23,325	5.84	\$ 37.19	20,725	5.59	\$ 36.84

The maximum term of stock options granted under the plans is 10 years.

There were no options granted in 2021, 2020 or 2019.

Additionally, the Company has a restricted stock plan to provide designated employees and directors the opportunity to receive grants of stock awards. The Restricted Stock Plan authorizes the issuance of up to 10,000 shares of common stock, of which 9,438 shares are available for issuance at December 31, 2021. Restricted stock awards are subject to a three year vesting schedule. Restricted shares granted in 2021 were 1,659 shares, shares vested were 562 shares as of December 31, 2021. The fair market value at the date of grant was \$60 per share. Compensation costs are recognized on a straight line basis over the vesting period.

Stock based compensation costs for 2021, 2020, and 2019, were \$99 thousand, \$64 thousand and \$19 thousand, respectively. As of December 31, 2021, the total remaining unrecognized compensation cost related to the issuance of stock options was \$29 thousand, which will be amortized over the expected life of these options. The intrinsic value for the stock options exercised was \$108 thousand, \$55 thousand, and \$72 thousand in the years ended December 31, 2021, 2020 and 2019, respectively. The total intrinsic value of outstanding stock options was \$579 thousand at December 31, 2021. The total intrinsic value of exercisable stock options was \$521 thousand at December 31, 2021.

12. RELATED PARTY TRANSACTIONS

In the ordinary course of business, the Company makes extensions of credit to its directors and their associates and several of its policy making officers on substantially the same terms, including interest rates and collateral, as those prevailing for comparable transactions with other customers. Extensions of credit outstanding, both direct and indirect, to directors and policy making officers were \$2,186 thousand at December 31, 2021 and \$2,163 thousand at December 31, 2020. New or additional extensions of credit during 2021 were \$1,056 thousand. Credit reductions and retirements were \$1,033 thousand during 2021. Deposit balances of directors and policy making officers were \$4,360 thousand and \$3,426 thousand at December 31, 2021 and 2020, respectively.

13. CORRESPONDENT BANK BALANCES

The company has balances due from correspondent banks in excess of FDIC insured deposit limits. These correspondent banks meet the regulatory definitions of well capitalized financial institutions. The uninsured deposit balances with FDIC insured correspondent banks were \$2.7 million at December 31, 2021.

14. FINANCIAL INSTRUMENTS

The Company is a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit and standby letters of credit.

The Company's exposure to credit losses in the event of nonperformance by the other party to these financial instruments are represented by the contractual amount of the instruments. The Company uses the same credit policies in making commitments and conditional obligations as it does for on-balance sheet instruments. Included in other liabilities are allowances for losses on unfunded credit commitments of \$24 thousand at December, 2021 and December 2020 respectively. There were no provisions for losses on unfunded letters of credit in 2021, 2020 and 2019.

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitments do not necessarily represent future cash requirements. The Company evaluates each customer's creditworthiness on a case-by-case basis.

Standby letters of credit are conditional commitments issued by the Company to guarantee the performance of a customer to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers.

A summary of the contract amounts of the Company's financial instruments with off-balance sheet risk at December 31, 2021 is as follows:

Commitments to extend credit	\$60,957 thousand
Standby letters of credit	\$1,938 thousand

15. FAIR VALUE MEASUREMENTS

The Company discloses fair value information about financial instruments for which it is practicable to estimate the value, whether or not such financial instruments are recognized on the balance sheet. Fair value is the amount at which a financial instrument could be exchanged in a current transaction between willing parties, other than in a forced sale or liquidation, and is best evidenced by quoted market price, if one exists.

Quoted market prices, if available, are shown as estimates of fair value. Because no quoted market prices exist for a substantial portion of the Company's financial instruments, the fair value of such instruments has been derived based on management's assumptions with respect to future economic conditions, the amount and timing of future cash flows and estimated discount rates. Different assumptions could significantly affect these estimates. Accordingly, the net realizable value could be materially different from the estimates presented. In addition, the estimates are only indicative of individual financial instrument values and should not be considered an indication of the fair value of the Company taken as a whole.

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

- Cash and due from banks and federal funds sold: The carrying amounts reported are considered to approximate their fair values.
- Investment securities: Fair values for investment securities are based on quoted market prices, where available. If quoted market prices are not available, fair values are based on quoted market prices of comparable instruments.
- Loans: For variable-rate loans that reprice frequently and with no significant change in credit risk, fair values are based on carrying amounts. The fair values for other loans are estimated using discounted cash flow analysis, based on interest rates currently being offered for loans with similar terms to borrowers of similar credit quality. Loan fair value estimates include judgments regarding future expected loss experience and risk characteristics. The carrying amount of accrued interest receivable approximates its fair value.
- Deposits: The fair value disclosed for deposits with no defined maturity are, by definition, equal to the amount payable on demand at the reporting date (that is, their carrying amounts). The fair values for certificates of deposit are estimated using a discounted cash flow calculation that applies interest rates currently being offered on certificates to a schedule of aggregated contractual maturities on such time deposits. The carrying amount of accrued interest payable approximates fair value.
- Borrowings: The fair value is estimated based on interest rates currently available for debt with similar terms and remaining maturities.

The estimated fair values of the Company's financial instruments as December 31, 2021 and 2020 are as follows:

	2021		2020	
	Carrying Value	Estimated Fair Value	Carrying Value	Estimated Fair Value
Financial assets:				
Total Cash and due from banks	\$ 4,536	4,536	\$ 6,603	6,603
Interest bearing deposits with banks	70,295	70,295	69,897	69,897
Investment securities:				
Available-for-sale	177,863	177,863	81,941	81,941
Federal Home Loan Bank stock	302	302	439	439
Loans, net of allowance	377,703	384,526	394,510	400,769
Accrued interest receivable	1,741	1,741	2,240	2,240
Financial liabilities:				
Deposits	584,569	584,208	505,564	506,230
Accrued interest payable	101	101	241	241

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

FASB's guidance 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 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 standard describes three levels of inputs that may be used to measure fair value.

Fair Value Hierarchy

Level 1 – Quoted prices in active markets for identical assets or liabilities

Level 2 – Other significant observable inputs (including quoted prices in active markets for similar assets or liabilities)

Level 3 – Significant unobservable inputs (including the Company's own assumptions in determining the fair value of assets or liabilities)

The following table presents fair value measurements on a recurring basis as of December 31, 2021 and 2020:

	<u>2021</u>			Fair
	Level 1	Level 2	Level 3	Value
Securities				
U.S. treasuries and government agencies	\$ -	26,945	-	26,945
State and municipal	-	37,205	-	37,205
Mortgage-backed	-	110,737	-	110,737
Corporate debt		2,976		2,976
Totals	\$ -	177,863	-	177,863

	<u>2020</u>			Fair
	Level 1	Level 2	Level 3	Value
U.S. treasuries and government agencies	\$ -	12,573	-	12,573
State and municipal	-	23,669	-	23,669
Mortgage-backed	-	45,699	-	45,699
Totals	\$ -	81,941	-	81,941

Securities available-for-sale are based on quoted market prices, where available. If quoted market prices are not available, fair values are based on quoted market prices of comparable instruments.

The Bank may also be required, from time to time, to measure certain other financial assets and liabilities at fair value on a nonrecurring basis in accordance with accounting principles generally accepted in the United States of America. The following table presents fair value measurements on a non-recurring basis as of December 31, 2021 and 2020:

	<u>2021</u>			Fair
	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Value</u>
Impaired loans	\$ -	-	5,729	5,729

	<u>2020</u>			Fair
	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Value</u>
Impaired loans	\$ -	-	7,590	7,590

Loans which are deemed to be impaired are primarily valued on a nonrecurring basis at the fair values of the underlying real estate collateral. Such fair values are derived as follows:

Level 3 inputs are independent appraisals and other available market evaluations used by management in estimating fair value.