Howard Bancorp Inc
Form 10-K
March 30, 2016

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

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

For the fiscal year ended December 31, 2015

Commission file number: 001-35489

HOWARD BANCORP, INC.

(Exact name of registrant as specified in its charter)

Maryland	**20-3735949**
State or other jurisdiction	(I.R.S. Employer
of incorporation or organization	Identification No.)

6011 University Blvd. Suite 370, Ellicott City, MD	**21043**
(Address of principal executive offices)	(Zip Code)

(410) 750-0020

(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common Stock, par value $0.01 per share	The NASDAQ Stock Market LLC

Securities registered pursuant to Section 12(g) of the Act:

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act Yes ¨ No x

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes ¨ No x

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No ¨

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. x

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a small reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "small reporting

company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer ¨ Accelerated filer ¨ Non-accelerated filer ¨ Smaller reporting company x

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

The aggregate market value of the voting common stock of the registrant held by non-affiliates on June 30, 2015, was approximately $73.6 million. At March 15, 2016, the number of outstanding shares of Common Stock, $0.01 par value, of the Corporation was 6,964,918.

DOCUMENTS INCORPORATED BY REFERENCE

Part III of this Form 10-K incorporates by reference certain information from the registrant's definitive Proxy Statement for the 2016 Annual Meeting of Stockholders.

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As used in this report, “the Company,” “we,” “us,” and “ours” refer to Howard Bancorp, Inc. and its subsidiaries. References to the “Bank” refer to Howard Bank.

This report contains forward-looking statements, which can be identified by the use of words such as “estimate,” “project,” “believe,” “intend,” “anticipate,” “plan,” “seek,” “expect,” “will,” “may,” “should” and words of similar meaning. You can also them by the fact that they do not relate strictly to historical or current facts.

These forward-looking statements include, but are not limited to:

- statements of our goals, intentions and expectations, particularly with respect to our business plan and strategies, including the expected opening of our new Columbia, Maryland branch, opening of additional branches, expansion into new markets, potential acquisitions, market share and asset growth, revenue and profit growth and expanding client relationships;
- impact of new branches and expansion into new markets on expenses compared to revenue growth;
- statements regarding the asset quality of our investment portfolios and anticipated recovery and collection of unrealized losses on securities available for sale;
- expected continued growth in our residential real estate lending;
- statements with respect to our allowance for credit losses, and the adequacy thereof;
- expected continuing increases in occupancy and equipment expenses;
- expectation regarding payment on non-accrual commercial loans with Small Business Administration guarantees;
- statement with respect to having adequate liquidity levels;
- our belief that we will retain a large portion of maturing certificates of deposit;
- the impact on us of recent changes to accounting standards;
- future cash requirements relating to commitments to extend credit; and
- the impact of interest rate changes on our net interest income.

These forward-looking statements are based on our current beliefs and expectations and are inherently subject to significant business, economic and competitive uncertainties and contingencies, many of which are beyond our control. In addition, these forward-looking statements are subject to assumptions with respect to future business strategies and decisions that are subject to change. We are under no duty to and do not undertake any obligation to update any forward-looking statements after the date of this report.

The following factors, among others, could cause actual results to differ materially from the anticipated results or other expectations expressed in the forward-looking statements:

- deterioration in general economic conditions, either nationally or in our market area, or a return to recessionary conditions;
- competition among depository and other financial institutions;

- inflation and changes in the interest rate environment that reduce our margins or reduce the fair value of financial instruments;
- adverse changes in the securities markets;
- changes in laws or government regulations or policies affecting financial institutions, including changes in regulatory fees and capital requirements;
- our ability to enter new markets successfully and capitalize on growth opportunities, and to otherwise implement our growth strategy;
- our ability to successfully integrate acquired entities, if any;
- changes in consumer spending, borrowing and savings habits;
- changes in accounting policies and practices, as may be adopted by the bank regulatory agencies, the Financial Accounting Standards Board, the Securities and Exchange Commission and the Public Company Accounting Oversight Board;
- changes in our organization, compensation and benefit plans
- loss of key personnel; and
- other risk discussed in this report.

Because of these and a wide variety of other uncertainties, our actual future results may be materially different from the results indicated by these forward-looking statements. You should not put undue reliance on any forward-looking statements.

Part I

Item 1. Business

Howard Bancorp, Inc.

Howard Bancorp, Inc. was incorporated in April 2005 under the laws of the State of Maryland to serve as the bank holding company of Howard Bank. The Company's primary business is owning all of the capital stock of Howard Bank. In addition to regulation of the Bank, as a bank holding company registered under the Bank Holding Company Act of 1956, we are subject to regulation and review by the Board of Governors of the Federal Reserve (the "FRB"). See "— Supervision and Regulation."

Howard Bank

Howard Bank is a trust company chartered under Subtitle 2 of Title 3 of the Financial Institutions Article of the Annotated Code of Maryland. The Bank was formed in March 2004 and commenced banking operations on August 9, 2004. Howard Bank has chosen, for the time being, not to seek and exercise trust powers, and our business, powers and regulatory structure are the same as a Maryland-chartered commercial bank. The Bank is subject to regulation, supervision and regular examination by the Maryland Commissioner of Financial Regulation and the Federal Deposit Insurance Corporation ("FDIC"), and our deposits are insured by the FDIC. The Bank has four operating subsidiaries, three of which hold foreclosed real estate and the other of which owns and manages real estate that we use for one of our branch locations and that also contains office and retail space.

Howard Bank is headquartered in Ellicott City, which is located in Howard County, Maryland. The Bank has branches in Howard County as well as in Anne Arundel County, Baltimore County, Baltimore City, Cecil County and Harford County in Maryland and one branch in Lancaster County, Pennsylvania. We engage in a general commercial banking business, making various types of loans and accepting deposits. We have traditionally marketed our financial services to small and medium sized businesses and their owners, professionals and executives, and high-net-worth individuals (the "mass affluent"), and have recently expanded to meet the financial needs of consumers generally.

Our core business strategy involves delivering advice and superior customer service to clients through local decision makers. We combine the Bank's specialized focus on both local markets and small and medium-sized business related market segments with a broad array of products, new technology and seasoned banking professionals to position the

Bank differently from most competitors. Our experienced executives establish a relationship with each client and bring value to all phases of a client's business and personal banking needs. To develop this strategy, we have established long-standing relationships with key customers in the community and with local business leaders who can create business opportunities. Since opening our residential lending division in 2014, we have extended our focus to residential mortgage lending as well.

Our primary source of revenue is net interest income, with fees generated by lending, mortgage banking and depository service charges constituting a smaller, but growing, percentage of revenues. We have positioned the balance sheet to hold a high percentage of earning assets and, in turn, to have those earning assets dominated by loans rather than investment securities. Generally speaking, loans earn more attractive returns than investments and are a key source of product cross sales and customer referrals. Certain economic conditions may favor investments over loans, such as poor corporate earnings, downturns in real estate cycles and other general slowing economic conditions. At all times, our loan and investment strategies seek to balance the need to maintain adequate liquidity via excess cash or federal funds sold with opportunities to appropriately leverage our capital.

Our strategic plan focuses on enhancing stockholder value through market share growth as reflected in balance sheet growth, related revenue growth and resulting growth in operating profits. We continue to expand our branch locations both through opening new branches and acquiring branch offices via acquisition. In 2014 we opened a de novo branch in Bel Air, Maryland, acquired a branch in Havre de Grace, Maryland, and added five new locations with our FDIC-assisted acquisition of NBRS Financial Bank ("NBRS"). In addition in 2015 we added four branches in the Patapsco Bancorp merger, three in Baltimore County and one in Baltimore City. We plan to open additional branches in the counties where we now operate and contiguous counties over the next several years, however, other than a new location in Columbia, Maryland that we expect will open in 2017 we currently have no definitive plans or agreements in place with respect to any other additional branches. Our long-term vision includes supplementing our historically organic growth with strategically significant acquisitions. We believe that acquiring other financial institutions - in whole or in part (through business line spin-offs, branch sales or the hiring of teams of individuals) will allow us to expand our market, achieve certain operating efficiencies, and grow our stockholder base and thus our share value and liquidity. We believe that our demonstrated expertise in commercial lending, deposit gathering (especially non-interest bearing transactional deposits), our demonstrated ability to attract additional investment and capital, and community leadership positions us as an attractive acquirer. We also anticipate that increasing our capital levels will give us the ability to continue our organic asset growth and expand our relationships with key clients through a larger legal lending limit.

Recent Developments

On June 2, 2015, we sold 2,173,913 shares of our common stock, at a purchase price of $11.50 per share or an aggregate of $25 million, to certain institutional accredited investors pursuant to investment agreements between Howard Bancorp and such institutional investors dated as of March 2, 2015, in a private placement offering. The Company used the proceeds of the private placement in part to support its acquisition of Patapsco Bancorp as well as to support continued organic and acquired growth for the combined institution. Howard has no present intent to use the proceeds of the private placement to redeem its preferred stock issued to the U.S. Department of the Treasury under its Small Business Lending Fund (SBLF) program, but is evaluating other alternatives for the potential redemption of the SBLF preferred stock.

On August 28, 2015, we completed our acquisition of Patapsco Bancorp, Inc., the parent company of The Patapsco Bank through the merger of Patapsco Bancorp with and into the Company pursuant to the Agreement and Plan of Merger dated as of March 2, 2015, as amended, by and between the Company and Patapsco Bancorp. As a result of the merger, each outstanding share of common stock of Patapsco Bancorp was converted into the right to receive, at the holder's election, $5.09 in cash or 0.3547 shares of our common stock, provided that (i) cash was paid in lieu of any fractional shares of our common stock and (ii) 20% of the shares of common stock of Patapsco Bancorp outstanding at the time of the merger were exchanged for cash in the merger, with the remaining shares of Patapsco Bancorp common stock exchanged for an aggregate of 560,891 shares of our common stock. The aggregate merger consideration was $10.064 million. In connection with the merger, immediately thereafter Patapsco Bank merged with and into the Bank, with the Bank the surviving bank.

Our Market Area

Our headquarters are located in Ellicott City, Maryland, and we consider our primary market area to be the Greater Baltimore Metropolitan Area in Maryland. We also have loans in our loan portfolio that are outside our market area, although to grow our loan portfolio we do not actively solicit business outside our primary market.

We have sixteen full services branches, located throughout Maryland and Lancaster, Pennsylvania.

HOWARD COUNTY

Snowden River	**Maple Lawn**	**Centennial Place**
6011 University Blvd.	10985 Johns Hopkins Rd.	10161 Baltimore National Pk.
Suite 150	Laurel, MD 20723	Ellicott City, MD 21042
Ellicott City, MD 21043		

ANNE ARUNDEL COUNTY

Defense Highway
116 Defense Hwy.
Annapolis, MD 21401

BALIMORE COUNTY

Towson
22 W Pennsylvania Ave.
Towson, MD 21204

Dundalk
1301 Merritt Blvd.
Baltimore, MD 21222

Parkville
2028 E. Joppa Rd.
Baltimore, MD 21234

Glen Arm
12128 Long Green Pk.
Glen Arm, MD 21057

BALTIMORE CITY

Hampden
821 W. 36th St.
Baltimore, MD 21211

HARFORD COUNTY

Aberdeen
3 West Bel Air Ave.
Aberdeen, MD 21001

Bel Air
101 N. Main St.
Bel Air, MD 21014

Havre de Grace
800 Revolution St.
Havre de Grace, MD 21078

Dublin
3535 Conowingo Rd.
Street, MD 21154

CECIL COUNTY

Rising Sun
6 Pearl St.
Rising Sun, MD 21911

Elkton
305 Augustine Herman Hwy.
Elkton, MD 21921

LANCASTER COUNTY, PA

Penn Hill
2006 Lancaster Pike
Peach Bottom, PA 17563

Competitive Position

We believe that our position as a community bank with just under $1 billion in assets positions us well to navigate the current economic environment, ongoing market consolidation and heightened regulatory environment. We continue to have the ability to outsource certain activities (internal audit, compliance review, information security monitoring) and to source new products and services (check imaging, online banking) in a highly efficient manner and thus avoid the risk of impairment of operating earnings faced by some banks who, we believe, are locked into legacy systems and are finding the onslaught of new regulations challenging. Strategic partnerships for these outsourced activities include contractual relationships with some of the largest and strongest providers of item processing, data processing, information monitoring and payment systems alternatives. We believe that this provides the Bank with the best of technology and product selection without sacrificing the more intimate delivery advantages of a community bank. We believe the current economic and regulatory environment will lead to greater consolidation among financial institutions, including community banks. Some of that consolidation will occur with larger banks, thus exacerbating the scarcity of banks able to underwrite traditionally and offer advice in interactions with customers as we do, which we believe gives us a wider window of opportunity to extend our brand and value proposition. We believe, however, that to the extent some of that consolidation occurs between and among smaller banks, the resulting combined institutions will be better positioned to differentiate themselves.

We believe that our “Hands On” approach to delivering small and medium-sized businesses a very broad and deep array of competitive credit and cash management services through a team of experienced advisors and providing them with access to local policy and decision makers fills a “white space” between the sophisticated but distracted large banks whose best personnel work with the largest companies and the small banks who are very responsive but less capable of being proactive in providing advice. Relationship managers, team leaders and executive management at the Bank generally have decades of banking experiences and are well established in the communities that they serve. They are

able to interface with clients directly to share that experience and to provide connections with their own network of other specialized advisors. We believe we also benefit from our committed leadership at both the executive management and board level who bring a broad array of skills and experiences to our company and are able to position the Bank for consistent profitable growth.

Lending Activities

General

Our primary market focus is on making loans to and gathering deposits from small and medium size businesses and their owners, professionals and executives, and high-net-worth individuals in our primary market area. Our loans are made to customers primarily in the Greater Baltimore market. Our lending activities consist generally of short to medium term commercial lending, commercial mortgage lending for both owner occupied and investor properties, residential mortgage lending and consumer lending, both secured and unsecured. A substantial portion of our loan portfolio consists of loans to businesses secured by real estate and/or other business assets.

Credit Policies and Administration

We have adopted a comprehensive lending policy, which includes stringent underwriting standards for all types of loans. Our lending teams follow pricing guidelines established periodically by our management team. In an effort to manage risk, only small lending authority is given to individual loan officers. Most loan officers can approve loans of up to $50,000. The Chief Lending Officer, the Chief Credit Officer and a select number of senior managers can approve loans up to $500,000, or $750,000 combined. Our President can approve loans up to $1,000,000. Loans above these amounts must be reviewed and approved by an officers' loan committee. Under the leadership of our executive management team, we believe that we employ experienced lending officers, secure appropriate collateral and carefully monitor the financial conditions of our borrowers and the concentration of loans in our portfolio.

In addition to the normal repayment risks, all loans in the portfolio are subject to the state of the economy and the related effects on the borrower and/or the real estate market. Generally, longer-term loans have periodic interest rate adjustments and/or call provisions. Senior management monitors the loan portfolio closely to ensure that we minimize past due loans and that we swiftly deal with potential problem loans.

Howard Bank also retains an outside, independent firm to review the loan portfolio. This firm performs a detailed annual review. We use the results of the firm's report primarily to validate the risk ratings applied to loans in the portfolio and identify any systemic weaknesses in underwriting, documentation or management of the portfolio. Results of the annual review are presented to executive management, the Audit Committee of the board and the full board of directors and are available to and used by regulatory examiners when they review the Bank's asset quality. We currently use the firm of Clifton Larsen Allen to perform this review.

The Bank maintains the normal checks and balances on the loan portfolio not only through the underwriting process but through the utilization of an internal credit administration group that both assists in the underwriting and serves as an additional reviewer of underwriting. The separately-managed loan administration group also has oversight for documentation, compliance and timeliness of collection activities. Our outsourced internal audit firm also reviews documentation, compliance and file management.

Commercial Lending

Our commercial lending consists of lines of credit, revolving credit facilities, accounts receivable and inventory financing, term loans, equipment loans, small business administration ("SBA") loans, stand-by letters of credit and unsecured loans. We originate commercial loans for any business purpose, including the financing of leasehold improvements and equipment, the carrying of accounts receivable, general working capital, contract administration and acquisition activities. These loans typically have maturities of seven years or less. We have a diverse client base and we do not have a concentration of these types of loans in any specific industry segment. We generally secure commercial business loans with accounts receivable and inventory, equipment, indemnity deeds of trust and other collateral such as marketable securities, cash value of life insurance, and time deposits at Howard Bank. Commercial business loans have a higher degree of risk than residential mortgage loans because the availability of funds for

repayment generally depends on the success of the business. To help manage this risk, we establish parameters/ covenants at the inception of the loan to provide early warning systems before payment default. We normally seek to obtain appropriate collateral and personal guarantees from the borrower's principal owners. We are able, given our business model, to proactively monitor the financial condition of the business.

Commercial Mortgage Lending

We finance commercial real estate for our clients, for both owner-occupied properties and investor properties (including residential properties). We generally will finance owner occupied commercial real estate at a maximum loan–to-value of 85% and non-owner occupied at a maximum loan-to-value of 80%. Our underwriting policies and processes focus on the underlying credit of the owner for owner occupied real estate and on the rental income stream (including rent terms and strength of tenants) for non-owner occupied real estate as well as an assessment of the underlying real estate. Risks inherent in managing a commercial real estate portfolio relate to vacancy rates/absorption rates for surrounding properties, sudden or gradual drops in property values as well as changes in the economic climate. We attempt to mitigate these risks by carefully underwriting loans of this type as well as by following appropriate loan-to-value standards. We are cash flow lenders and never rely solely on property valuations in reaching a lending decision. Personal guarantees are often required for commercial real estate loans as they are for other commercial loans. Most of our real estate loans carry fixed interest rates and amortize over 20 – 25 years but have five- to seven-year maturities. Properties securing our commercial real estate loans primarily include office buildings, office condominiums, distribution facilities and manufacturing plants. Substantially all of our commercial real estate loans are secured by properties located in our market area.

Commercial real estate loans generally carry higher interest rates and have shorter terms than one- to four-family residential mortgage loans. Commercial real estate loans, however, entail significant additional risks as compared with residential mortgage lending, as they typically involve larger loan balances concentrated with single borrowers or groups of related borrowers. In addition, the payment of loans secured by income-producing properties typically depends on the successful operation of the property, as repayment of the loan generally is dependent, in large part, on sufficient income from the property to cover operating expenses and debt service. Changes in economic conditions that are not in the control of the borrower or lender could affect the value of the collateral for the loan or the future cash flow of the property. Additionally, any decline in real estate values may be more pronounced for commercial real estate than residential properties.

Construction Lending

Construction lending can cover funding for land acquisition, land development and/or construction of residential or commercial structures. Our construction loans generally bear a variable rate of interest and have terms of one to two years. Funds are advanced on a percentage-of-completion basis. These loans are generally repaid at the end of the development or construction phase, although loans for both residential and commercial construction will often convert into a permanent mortgage loans at the end of the term of the loan. Loan to value parameters range from 65% of the value of land to 75% for developed land, 80% for commercial or multifamily construction and 85% for residential construction. These loan-to-value ratios represent the upper limit of advance rates to remain in compliance with Bank policy. Typically, loan-to-value ratios should be somewhat lower than these upper limits, requiring the borrower to provide significant equity at the inception of the loan. Our underwriting looks not only at the value of the property but the expected cash flows to be generated by sale of the parcels or completed construction. The borrower must have solid experience in this type of construction and personal guarantees are usually required.

Construction lending entails significant risks compared with residential mortgage lending. These risks involve larger loan balances concentrated with single borrowers with funds advanced upon the security of the land or the project under construction. The value of the project is estimated prior to the completion of construction. Thus, it is more difficult to evaluate accurately the total loan funds required to complete a project and related loan to value ratios. If the estimate of construction or development cost proves to be inaccurate, we may be required to advance additional funds beyond the amount originally committed in order to protect the value of the property. Moreover, if the estimated value of the completed project proves to be inaccurate, the borrower may hold a property with a value that is insufficient to assure full repayment. To mitigate these risks, in addition to the underwriting considerations noted above, we maintain an in-house construction monitoring unit that has oversight for the projects and we require both site visits and frequent reporting before funds are advanced.

Residential Mortgage Lending

We offer a variety of consumer-oriented residential real estate loans. Residential mortgage loans consist primarily of first mortgage loans to individuals, most of which have a loan to value not exceeding 85%. The remainder of this portion of our portfolio consists of home equity lines of credit and fixed rate home equity loans.

Our residential mortgage loans are generally for owner-occupied single family homes. These loans are generally for a primary residence although we will occasionally originate loans for a second home where the borrower has extremely strong credit. Our residential mortgage loans were historically fixed rate loans with 15- or 30-year terms. We now also originate variable rate loans with a five- to seven-year term, although such loans have a longer amortization schedule.

Our home equity loans and home equity lines of credit are primarily secured by a second mortgage on owner occupied one-to four-family residences. Our home equity loans are originated at fixed interest rates and with terms of between five and 30 years for primary residences and between five and 15 years for secondary and rental properties, and are fully amortizing. Our home equity lines allow for the borrower to draw against the line for ten years, after which the

line is refinanced into a ten-year fixed loan, with the possibility of a one-time extension of five years. Home equity lines of credit carry a variable rate of interest and minimum monthly payments during the draw period, which are the greater of (i) $50.00 or (ii) depending on credit score, loan-to-value and debt-to-income ratios, either the interest due or interest due plus 1% of the outstanding loan balance. Home equity loans and lines of credit are generally underwritten with a maximum loan-to-value ratio of 85% (80% when appraised value is greater than $1 million) for a primary residence when combined with the principal balance of the existing mortgage loan; for home equity loans on secondary and rental properties, the maximum loan-to-value ratio is 65%. We require appraisals on all real estate loans – both commercial and residential. At the time we close a home equity loan or line of credit, we record a mortgage to perfect our security interest in the underlying collateral. Home equity loans and lines of credit also require title insurance, and borrowers must obtain hazard insurance and, with respect properties located in a flood hazard area, flood insurance.

Home equity loans and lines of credit generally have greater risk than one- to four-family residential mortgage loans. In these cases, we face the risk that collateral for a defaulted loan may not provide an adequate source of repayment of the outstanding loan balance. In particular, because home equity loans are secured by second mortgages, decreases in real estate values could adversely affect the value of the property serving as collateral for these loans. Thus, the recovery of such property could be insufficient to compensate us for the value of these loans.

Loans secured by second mortgages have greater risk than owner-occupied residential loans secured by first mortgages. When customers default on their loans we attempt to foreclose on the property. However, the value of the collateral may not be sufficient to compensate for the amount of the unpaid loan, and we may be unsuccessful in recovering the remaining balance from these customers. In addition, decreases in property values could adversely affect the value of properties used as collateral for the loans. These second lien loans represent a smaller portion of our portfolio.

Our home equity and home improvement loan portfolio gives us a diverse client base. Although most of these loans are in our primary market area, the diversity of the individual loans in the portfolio reduces our potential risk.

Consumer Lending

We offer various types of secured and unsecured consumer loans. Generally, our consumer loans are made for personal, family or household purposes as a convenience to our customer base. As a general guideline, a consumer's total debt service should not exceed 40% of their gross income. The underwriting standards for consumer loans include a determination of the applicant's payment history on other debts and an assessment of his or her ability to meet existing obligations and payments on the proposed loan.

Consumer loans may present greater credit risk than residential mortgage loans because many consumer loans are unsecured or are secured by rapidly depreciating assets. Repossessed collateral for a defaulted consumer loan may not provide an adequate source of repayment of the outstanding loan balance because of the greater likelihood of damage, loss or depreciation. Consumer loan collections also depend on the borrower's continuing financial stability. If a borrower suffers personal financial difficulties, the loan may not be repaid. Also, various federal and state laws, including bankruptcy and insolvency laws, may limit the amount we can recover on such loans.

Loan Originations, Purchases, Sales, Participations and Servicing

All loans that we originate are underwritten pursuant to our policies and procedures, which incorporate standard underwriting guidelines. We originate both fixed and variable rate loans. Our loan origination activity may be adversely affected by a rising interest rate environment that typically results in decreased loan demand. We generally retain in our portfolio the majority of loans that we originate, except for first lien residential mortgage loans where we sell the majority of the loans into the secondary market. Residential loans originated for sale include loans originated on a national platform, underwritten to standards at least as conservative as those applied to in state loans, which constitute the majority of our residential loans originated for sale and over 90% of the residential loans that we add to our portfolio. We do not retain the servicing rights on sold loans.

We occasionally sell participations in commercial loans to correspondent banks if the amount of the loan exceeds our internal limits. More rarely, we purchase loan participations from correspondent banks in the local market as well. Those loans are underwritten in- house with the same care of loans directly originated.

Loan Approval Procedures and Authority

Our lending activities follow written, non-discriminatory underwriting standards and loan origination procedures established by our board of directors. The loan approval process is intended to assess the borrower's ability to repay the loan, the viability of the loan, and the adequacy of the value of the collateral that will secure the loan, if applicable. To assess a business borrower's ability to repay, we review and analyze, among other factors: current income, credit history including the Bank's prior experience with the borrower, cash flow, any secondary sources of repayment, other debt obligations in regards to the equity/net worth of the borrower and collateral available to the Bank to secure the loan.

We require appraisals of all real property securing one- to four-family residential and commercial real estate loans and home equity loans and lines of credit. All appraisers are state-licensed or state-certified appraisers, and our practice is to have local appraisers approved by the board of directors annually.

Mortgage Banking

Our residential mortgage loans consist of residential first and second mortgage loans, residential construction loans and home equity lines of credit and term loans secured by the residences of borrowers. Second mortgage and home equity lines of credit are used for home improvements, education and other personal expenditures. We make mortgage loans with a variety of terms, including fixed, floating and variable interest rates, with maturities ranging from three months to thirty years.

Residential mortgage loans generally are made on the basis of the borrower's ability to repay the loan from his or her salary and other income and are secured by residential real estate, the value of which is generally readily ascertainable. These loans are made consistent with our appraisal and real estate lending policies, which detail maximum loan-to-value ratios and maturities. Residential mortgage loans and home equity lines of credit secured by owner-occupied property generally are made within the guidelines of our investors.

Howard Bank generates revenue by providing an extensive line of consumer real estate products and services to customers nationwide. Howard Bank offers products available to customers through a retail network of mortgage loan officers and bankers as well as a sales force offering our customers direct telephone access to our products.

The Bank originates residential mortgage loans primarily as a correspondent lender. Activity in the residential mortgage loan market is highly sensitive to changes in interest rates and product availability. While the Bank does have delegated underwriting authority from most of its investors, at times it also employs the services of the investor to underwrite the loans. Because the loans are originated within investor guidelines and designated automated underwriting and product specific requirements as part of the loan application, the loans sold have a limited recourse provision. Most contracts with investors contain recourse periods. In general, the Bank may be required to repurchase a previously sold mortgage loan or indemnify the investor if there is non-compliance with defined loan origination or documentation standards, including fraud, negligence or material misstatement in the loan documents. In addition, the Bank may have an obligation to repurchase a loan if the mortgagor has defaulted early in the loan term. The potential default repurchase period varies by investor but can be up to approximately twelve months after sale of the loan to the investor. Mortgages subject to recourse are collateralized by single-family residential properties, follow investor guidelines, and will carry private mortgage insurance, where applicable.

The Bank enters into commitments to originate residential mortgage loans whereby the interest rate on the loan is determined prior to funding (i.e. rate lock commitments). Such rate lock commitments on mortgage loans to be sold in the secondary market are considered to be derivatives. To protect against the price risk inherent in residential mortgage loan commitments, the Bank utilizes “best efforts” in delivering to investors. Under a “best efforts” contract, the Bank commits to deliver an individual mortgage loan of a specified principal amount and quality to an investor and the investor commits to a price that it will purchase the loan from the Bank if the loan to the underlying borrower closes. The Bank protects itself from changes in interest rates through the use of best efforts forward delivery commitments, whereby the investor commits to purchase a loan at a price representing a premium on the day the borrower commits to an interest rate with the intent that the buyer/investor has assumed the interest rate risk on the loan. As a result, the Bank is not generally exposed to losses on loans sold utilizing best efforts. Nor will it realize gains related to rate lock commitments due to changes in interest rates. The market values of rate lock commitments and best efforts contracts are not readily ascertainable with precision because rate lock commitments and best efforts contracts are not actively traded. Because of the high correlation between rate lock commitments and best efforts contracts, no gain or loss should occur on the rate lock commitments.

Investments and Funding

We balance our liquidity needs based on loan and deposit growth via the investment portfolio and both short and long term borrowings. It is our goal to provide adequate liquidity to support our loan growth. We use the generally short term investments that represent our liquidity to generate additional positive earnings. Howard Bank’s primary source of funds is, and will continue to be, core deposits generated from the local marketplace. Additional funding is provided by customer repurchase agreements, Federal Home Loan Bank of Atlanta (“FHLB”) advances, the FRB Discount Window, and other purchased funds. Other purchased funds may include certificates of deposit over $100,000, federal funds purchased, and institutional or brokered deposits. Lines of credit are maintained to protect liquidity levels resulting from unexpected deposit withdrawals and natural-market credit demand.

Our investment policy is reviewed annually by our board of directors. The board of directors has appointed its Executive Committee to serve as the Investment Committee, and the Executive Committee therefore meets at regular intervals (not less than quarterly) and provides a report on the investment portfolio performance to the full board of directors. The investment officer is designated by the President and is responsible for managing the day-to-day activities of the liquidity and investments in accordance with the policies approved by the board of directors. We actively monitor our investment portfolio and we classify the majority of the portfolio as “available for sale.” In general, under such a classification, we may sell investment instruments as management deems appropriate.

Other Banking Products

We offer our customers wire transfer services, ATM and check cards, automated teller machines at all of our full-service branch locations, safe deposit boxes at most full service locations and credit cards through a third party processor. Additionally, we provide Internet banking capabilities to our customers and merchant card services for our business customers. With our Internet banking service, our customers may view their accounts on line and electronically remit bill payments including an option for same day payment. Our commercial account services include an overnight sweep service and remote deposit capture service.

We complement our existing internet banking services with Mobiliti Mobile Banking, PopMoney and eStatement products. These state of the art products provide the Bank's consumer customers the ability to view account information and pay bills from their mobile device, easily make payments directly to individuals and, with eStatements, to replace their paper monthly statement with an electronically delivered statement.

Deposit Activities

Deposits are the major source of our funding. We offer a broad array of consumer and business deposit products that include demand, money market, savings and individual retirement accounts, as well as certificates of deposit. We offer through key technology partnerships a competitive array of commercial cash management products, which in combination with our in-house courier service and remote deposit/ check imaging service, allow us to attract demand deposits. We believe that we pay competitive rates on our interest bearing deposits. As a relationship-oriented organization, we generally seek to obtain deposit relationships with our loan clients.

We also use customer repurchase agreements, FHLB advances, the FRB Discount Window and other purchased funds as a funding mechanism. Other purchased funds may include certificates of deposits over $100,000, federal funds purchased and institutional or brokered deposits.

Employees

Howard Bank has 253 full-time and four part-time employees as of December 31, 2015. None of our employees are represented by any collective bargaining unit, and we believe that relations with our employees are good. Howard Bancorp has no employees.

Lending Limit

The Bank's legal lending limit for loans to one borrower was approximately $13.2 million as of December 31, 2015. We further monitor our exposure to one borrower through a policy to limit our "in-house" lending limit to $10.0 million, which in-house limit can be waived by our board of directors. As part of our risk management strategy, we may attempt to participate a portion of larger loans to other financial institutions. This strategy allows us to maintain customer relationships yet observe the legal lending limit and manage credit exposure. However, this strategy may not always be available.

Competition

Our primary market area is highly competitive and heavily branched by other financial institutions of all sizes. We also compete with Internet-based banks. Competition for loans to small and medium sized businesses and their owners, professionals and executives, and high-net-worth individuals is intense, and pricing is important. We believe that acquisitions of several local competitors by larger institutions headquartered outside of the State of Maryland during the last several years have enhanced the Bank's positioning as a locally headquartered and managed community bank, but many of these competitors now have substantially greater resources and lending limits than we do and offer services, such as extensive and established branch networks and trust services, that we do not expect to provide in the near future or ever. Moreover, larger institutions operating in our primary market area may have access to borrowed funds at a lower rate than is available to us. Deposit competition is also strong among institutions in our primary market area.

However, recent mergers of other area banks into large regional and national financial institutions have created opportunities for community-focused and prudently managed community banks. While our board of directors is aware

of the competition that these larger institutions and alternative providers of financial services offer, we believe that local independent banks play and will continue to play a significant role in our primary market area. Our board of directors believes it is a significant and distinct advantage to be a community owned and operated state bank interested in serving the needs of small and medium sized businesses and their owners, professionals and executives, and high-net-worth individuals.

Participation in Small Business Lending Fund

On September 22, 2011, we entered into a securities purchase agreement with the Secretary of the Treasury pursuant to which we sold to the Secretary of the Treasury 12,562 shares of our Series AA Preferred Stock, having a liquidation amount per share equal to $1,000, for an aggregate purchase price of $12,562,000. We issued the Series AA Preferred Stock pursuant to Treasury's Small Business Lending Fund ("SBLF"). Enacted into law as part of the Small Business Jobs Act of 2010, the SBLF was a $30 billion fund designed to encourage lending to small businesses by providing Tier 1 capital to qualified community banks with assets of less than $10 billion at favorable rates. We were one of only four banks in the State of Maryland that was approved to participate in this program. The Series AA Preferred Stock qualifies as Tier 1 capital and is generally non-voting. In accordance with the terms of the SBLF program, the Series AA Preferred Stock has an initial annual dividend rate of 5%, which was eligible for reduction based on increases in our small business lending. In accordance with the terms of the Series AA Preferred Stock, the dividend rate was fixed at 9% as of March 22, 2016 and will remain at 9% until we have repaid the SBLF funding.

SUPERVISION AND REGULATION

Howard Bancorp, Inc.

We are a bank holding company under the Bank Holding Company Act of 1956, as amended (the "BHC Act"). We are subject to regulation and examination by the FRB and the Maryland Office of the Commissioner of Financial Regulation, and are required to file periodic reports and any additional information that the FRB and the Maryland Office of the Commissioner of Financial Regulation may require. In addition, the FRB and the Maryland Office of the Commissioner of Financial Regulation have enforcement authority over Howard Bancorp, Inc., which includes the power to remove officers and directors and the authority to issue cease and desist orders to prevent Howard Bancorp from engaging in unsafe or unsound practices or violating laws or regulations governing its business. In general, these enforcement actions may be initiated for violations of laws and regulations and unsafe or unsound practices. Other actions or inactions may provide the basis for enforcement action, including misleading or untimely reports filed with regulatory authorities.

Under FRB regulations, a bank holding company is required to serve as a source of financial and managerial strength to its subsidiary banks and may not conduct its operations in an unsafe or unsound manner. In addition, in serving as a source of strength to its subsidiary banks, a bank holding company should stand ready to use available resources to provide adequate capital funds to its subsidiary banks during periods of financial stress or adversity and should maintain the financial flexibility and capital raising capacity to obtain additional resources for assisting its subsidiary banks. A bank holding company's failure to meet its obligations to serve as a source of strength to its subsidiary banks will generally be considered by the FRB to be an unsafe and unsound banking practice, a violation of FRB regulations or both. The FRB may require a bank holding company to terminate any activity or relinquish control of a nonbank subsidiary (other than a nonbank subsidiary of a bank) upon the FRB's determination that such activity or control constitutes a serious risk to the financial soundness or stability of any subsidiary depository institution of the bank holding company. Further, federal bank regulatory authorities have additional discretion to require a bank holding company to divest itself of any bank or nonbank subsidiary if the agency determines that divestiture may aid the depository institution's financial condition.

The BHC Act requires regulatory filings by a stockholder or other party that seeks to acquire direct or indirect "control" of an FDIC-insured depository institution. The determination whether an investor "controls" a depository institution is based on all of the facts and circumstances surrounding the investment. As a general matter, a party is deemed to control a depository institution or other company if the party owns or controls 25% or more of any class of voting stock. Subject to rebuttal, a party may be presumed to control a depository institution or other company if the investor owns or controls 10% or more of any class of voting stock. Ownership by affiliated parties, or parties acting in concert, is typically aggregated for these purposes. If a party's ownership of Howard Bancorp were to exceed certain thresholds, the investor could be deemed to "control" Howard Bancorp for regulatory purposes. This could subject the investor to regulatory filings or other regulatory consequences.

Pursuant to provisions of the BHC Act and regulations promulgated by the FRB thereunder, Howard Bancorp, Inc. may only engage in or own companies that engage in activities deemed by the FRB to be so closely related to the business of banking or managing or controlling banks as to be a proper incident thereto, and the holding company must obtain permission from the FRB prior to engaging in most new business activities. In addition, bank holding companies like Howard Bancorp must be well capitalized and well managed in order to engage in the expanded financial activities permissible only for a financial holding company.

The FRB has adopted guidelines regarding the capital adequacy of bank holding companies, which require bank holding companies to maintain specified minimum ratios of capital to total assets and capital to risk weighted assets. See "—Capital Requirements." The FRB has issued a policy statement regarding the payment of dividends by bank holding companies. In general, the FRB's policies provide that dividends should be paid only out of current earnings and only if the prospective rate of earnings retention by the bank holding company appears consistent with the organization's capital needs, asset quality, and overall financial condition. Under the prompt corrective action rules, the ability of a bank holding company to pay dividends may be restricted if a subsidiary bank becomes undercapitalized. These regulatory policies could affect the ability of Howard Bancorp, Inc. to pay dividends or otherwise engage in capital distributions.

The status of Howard Bancorp, Inc. as a registered bank holding company under the BHC Act and a Maryland-chartered bank holding company does not exempt it from certain federal and state laws and regulations applicable to corporations generally, including, without limitation, certain provisions of the federal securities laws.

Howard Bank

Howard Bank is a Maryland chartered trust company (with all powers of a commercial bank), and its deposit accounts are insured by the FDIC up to the maximum legal limits. It is subject to regulation, supervision and regular examination by the Maryland Commissioner of Financial Regulation and the FDIC. The regulations of these various agencies govern most aspects of Howard Bank's business, including required reserves against deposits, loans, investments, mergers and acquisitions, borrowing, dividends and location and number of branch offices. The laws and regulations governing Howard Bank generally have been promulgated to protect depositors and the FDIC's Deposit Insurance Fund ("DIF"), and not for the purpose of protecting stockholders.

Set forth below is a brief description of the material regulatory requirements that are or will be applicable to Howard Bank and Howard Bancorp, Inc. The description below is limited to the material aspects of the statutes and regulations addressed, and is not intended to be a complete description of such statutes and regulations and their effects on Howard Bank and Howard Bancorp, Inc.

Financial Institutions Article of the Maryland Annotated Code

The Financial Institutions Article of the Maryland Annotated Code (the "Banking Code") contains detailed provisions governing the organization, operations, corporate powers, commercial and investment authority, branching rights and responsibilities of directors, officers and employees of Maryland banking institutions. The Banking Code delegates extensive rulemaking power and administrative discretion to the Maryland Office of the Commissioner of Financial Regulation in its supervision and regulation of state-chartered banking institutions. The Maryland Office of the Commissioner of Financial Regulation may order any banking institution to discontinue any violation of law or unsafe or unsound business practice.

Capital Requirements

In July 2013, the FDIC and the other federal bank regulatory agencies issued a final rule that revised their leverage and risk-based capital requirements and the method for calculating risk-weighted assets to make them consistent with agreements that were reached by the Basel Committee on Banking Supervision ("Basel III") and certain provisions of the Dodd-Frank Act. The final rule, which became effective on January 1, 2015, applies to all depository institutions, top-tier bank holding companies with total consolidated assets of $1 billion or more and top-tier savings and loan holding companies. The final rule creates a new common equity Tier 1 ("CET1") minimum capital requirement (4.5% of risk-weighted assets), increases the minimum Tier 1 capital ratio (from 4% to 6% of risk-weighted assets), imposes a minimum leverage ratio of 4.0%, and changes the risk-weight of certain assets to better reflect credit risk and other risk exposures. These include, among other things, a 150% risk weight for certain high volatility commercial real estate acquisition, development and construction loans and for non-residential mortgage loans that are 90 days past due or otherwise in non-accrual status, and a 20% credit conversion factor for the unused portion of a commitment with an original maturity of one year or less that is not unconditionally cancellable. The final rule also requires unrealized gains and losses on certain "available-for-sale" securities holdings to be included for purposes of calculating regulatory capital unless Howard Bank elects to opt-out from this treatment. Howard Bank has elected to permanently opt out of this treatment in our capital calculations, as permitted by the final rule.

The final rule will limit Howard Bank's capital distributions and certain discretionary bonus payments if the Bank does not hold a "capital conservation buffer" consisting of 2.5% of common equity Tier 1 capital to risk-weighted assets in addition to the amount necessary to meet its minimum risk-based capital requirements. The capital conservation buffer requirement will be phased in beginning January 1, 2016 and ending January 1, 2019, when the full capital conservation buffer requirement will be effective.

Prompt Corrective Action

Under federal prompt corrective action regulations, the bank regulatory agencies are authorized and, under certain circumstances, required to take various "prompt corrective actions" to resolve the problems of any bank subject to their

jurisdiction that is not adequately capitalized. Under the prompt corrective action regulations, a bank is considered "well capitalized" if it: (i) has a total risk-based capital ratio of 10.0% or greater; (ii) a Tier 1 risk-based capital ratio of 8.0% or greater; (iii) a common Tier 1 equity ratio of at least 6.5% or greater; (iv) a leverage capital ratio of 5.0% or greater; and (iv) is not subject to any written agreement, order, capital directive, or prompt corrective action directive to meet and maintain a specific capital level for any capital measure. As of December 31, 2015, Howard Bank remained "well capitalized" for this purpose and its capital exceeded all applicable requirements.

Howard Bank has been ''well capitalized'' since it commenced its business operations.

At this time the bank regulatory agencies are more inclined to impose higher capital requirements in order to meet well capitalized standards, and future regulatory change could impose higher capital standards as a routine matter. The regulators may also set higher capital requirements for holding companies whose circumstances warrant it. For example, holding companies experiencing internal growth or making acquisitions are expected to maintain strong capital positions substantially above the minimum supervisory levels, without significant reliance on intangible assets.

As an additional means to identify problems in the financial management of depository institutions, the Federal Deposit Insurance Act requires federal bank regulatory agencies to establish certain non-capital safety and soundness standards for institutions for which they are the primary federal regulator. The standards relate generally to operations and management, asset quality, interest rate exposure and executive compensation. The agencies are authorized to take action against institutions that fail to meet such standards.

Dividends

Howard Bancorp, Inc. is a legal entity separate and distinct from Howard Bank. Virtually all of Howard Bancorp's revenue available for the payment of dividends on its common stock results from dividends paid to Howard Bancorp by Howard Bank. Under Maryland law, Howard Bank may declare a cash dividend, after providing for due or accrued expenses, losses, interest and taxes, from its undivided profits or, with the prior approval of the Maryland Office of the Commissioner of Financial Regulation, from its surplus in excess of 100% of its required capital stock. Also, if Howard Bank's surplus is less than 100% of its required capital stock, then, until its surplus is 100% of its capital stock, Howard Bank must transfer to its surplus annually at least 10% of its net earnings and may not declare or pay any cash dividends that exceed 90% of its net earnings. In addition to these specific restrictions, the bank regulatory agencies have the ability to prohibit or limit proposed dividends if such regulatory agencies determine the payment of such dividends would result in Howard Bank being in an unsafe and unsound condition.

Deposit Insurance Assessments

Howard Bank's deposit accounts are insured by the FDIC generally up to a maximum of $250,000 per separately insured depositor. FDIC-insured depository institutions are required to pay deposit insurance assessments to the FDIC. The amount of a particular institution's deposit insurance assessment is based on that institution's risk classification under an FDIC risk-based assessment system. An institution's risk classification is assigned based on its capital levels and the level of supervisory concern the institution poses to the regulators. Assessment rates (inclusive of possible adjustments) currently range from 2.5 to 45 basis points of each institution's total assets less tangible capital. The FDIC may increase or decrease the range of assessments uniformly, except that no adjustment can deviate more than two basis points from the base assessment rate without notice and comment rulemaking. The FDIC's current system represents a change, required by the Dodd-Frank Act, from its prior practice of basing the assessment on an institution's aggregate deposits. The FDIC may terminate insurance of deposits upon a finding that the institution has engaged in unsafe or unsound practices, is in an unsafe or unsound condition to continue operations or has violated any applicable law, regulation, rule, order or condition imposed by the FDIC.

Maryland Regulatory Assessment

The Maryland Office of the Commissioner of Financial Regulation annually assesses state banking institutions to cover the expense of regulating banking institutions. The Bank's asset size determines the amount of the assessment.

Liquidity

Howard Bank is subject to the reserve requirements imposed by the State of Maryland. A Maryland banking institution is required to have at all times a reserve equal to at least 15% of its demand deposits. Howard Bank is also subject to the uniform reserve requirements of the FRB's Regulation D, which applies to all depository institutions with transaction accounts or non-personal time deposits. During 2015, amounts in transaction accounts above $14.5 million and up to $103.6 million were required to have reserves held against them in the ratio of 3% of such amounts. Amounts above $103.6 million required reserves of $2,673,000 plus 10% of the amount in excess of $103.6 million. The FRB changes its reserve requirements on an annual basis and Howard Bank is subject to new requirements for 2016. Howard Bank was in compliance with its reserve requirements at December 31, 2015 and is in compliance with its current reserve requirements.

Loans-to-One-Borrower Limitation

With certain limited exceptions, a Maryland banking institution may lend to a single or related group of borrowers an amount equal to 15% of its unimpaired capital and surplus. An additional amount may be lent, equal to 10% of unimpaired capital and surplus, if such loan is secured by readily marketable collateral, which is defined to include certain securities and bullion, but generally does not include real estate. Howard Bank is in compliance with the loans-to-one borrower limitations.

Community Reinvestment Act and Fair Lending Laws

Under the Community Reinvestment Act of 1977 ("CRA"), the FDIC is required to assess the record of all financial institutions regulated by it to determine if such institutions are meeting the credit needs of the community (including low and moderate income neighborhoods) which they serve. CRA performance evaluations are based on a four-tiered rating system: Outstanding, Satisfactory, Needs to Improve and Substantial Noncompliance. CRA performance evaluations are considered in evaluating applications for such things as mergers, acquisitions and applications to open branches. Howard Bank has a CRA rating of "Satisfactory". In addition, the Equal Credit Opportunity Act and the Fair Housing Act prohibit lenders from discriminating in their lending practices on the basis of characteristics specified in those statutes. The failure to comply with the Equal Credit Opportunity Act and the Fair Housing Act could result in enforcement actions by the FDIC, the Department of Housing and Urban Development, and the Department of Justice, and in private civil actions by borrowers.

Transactions with Related Parties

Transactions between banks and their related parties or affiliates are limited by Sections 23A and 23B of the Federal Reserve Act. An affiliate of a bank is any company or entity that controls, is controlled by or is under common control with the bank. In a holding company context, the parent bank holding company and any companies which are controlled by such parent holding company are affiliates of the bank.

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Generally, Section 23A of the Federal Reserve Act and the FRB's Regulation W limit the extent to which a bank or its subsidiaries may engage in "covered transactions" with any one affiliate to an amount equal to 10.0% of such bank's capital stock and surplus, and contain an aggregate limit on all such transactions with all affiliates to an amount equal to 20.0% of such bank's capital stock and surplus. The term ''covered transaction'' includes the making of loans, purchase of assets, issuance of guarantees and other similar transactions. In addition, loans or other extensions of credit by the bank to an affiliate are required to be collateralized in accordance with regulatory requirements and the bank's transactions with affiliates must be consistent with safe and sound banking practices and may not involve the purchase by the bank of any low-quality asset. Section 23B applies to covered transactions as well as certain other transactions and requires that all such transactions be on terms substantially the same, or at least as favorable, to the institution or subsidiary as those provided to non-affiliates.

Section 22(h) of the Federal Reserve Act and the FRB's Regulation O govern extensions of credit made by a bank to its directors, executive officers, and principal stockholders (''insiders''). Among other things, these provisions require that extensions of credit to insiders be made on terms that are substantially the same as, and follow credit underwriting procedures that are not less stringent than, those prevailing for comparable transactions with unaffiliated persons and that do not involve more than the normal risk of repayment or present other unfavorable features. Further, such extensions may not exceed certain limitations on the amount of credit extended to such persons, individually and in the aggregate, which limits are based, in part, on the amount of Howard Bank's capital. Extensions of credit in excess of certain limits must also be approved by the board of directors.

Standards for Safety and Soundness

Federal law requires each federal banking agency to prescribe certain standards for all insured depository institutions. These standards relate to, among other things, internal controls, information systems and audit systems, loan documentation, credit underwriting, interest rate risk exposure, asset growth, compensation, and other operational and managerial standards as the agency deems appropriate. Interagency guidelines set forth the safety and soundness standards that the federal banking agencies use to identify and address problems at insured depository institutions before capital becomes impaired. If the appropriate federal banking agency determines that an institution fails to meet any standard prescribed by the guidelines, the agency may require the institution to submit to the agency an acceptable plan to achieve compliance with the standard. If an institution fails to meet these standards, the appropriate federal banking agency may require the institution to implement an acceptable compliance plan. Failure to implement such a plan can result in further enforcement action, including the issuance of a "cease and desist" order or the imposition of civil money penalties.

Anti-Money Laundering and OFAC

Under federal law, financial institutions must maintain anti-money laundering programs that include established internal policies, procedures and controls; a designated compliance officer; an ongoing employee training program;

and testing of the program by an independent audit function. Financial institutions are also prohibited from entering into specified financial transactions and account relationships and must meet enhanced standards for due diligence and customer identification in their dealings with foreign financial institutions and foreign customers. Financial institutions must take reasonable steps to conduct enhanced scrutiny of account relationships to guard against money laundering and to report any suspicious transactions, and law enforcement authorities have been granted increased access to financial information maintained by financial institutions. Bank regulators routinely examine institutions for compliance with these obligations, and they must consider an institution's compliance in connection with the regulatory review of applications, including applications for banking mergers and acquisitions. The regulatory authorities have imposed "cease and desist" orders and civil money penalty sanctions against institutions found to be violating these obligations.

The Office of Foreign Assets Control, ("OFAC") is responsible for helping to ensure that U.S. entities do not engage in transactions with certain prohibited parties, as defined by various Executive Orders and Acts of Congress. OFAC sends bank regulatory agencies lists of persons and organizations suspected of aiding, harboring or engaging in terrorist acts, known as Specially Designated Nationals and Blocked Persons. If Howard Bancorp or Howard Bank finds a name on any transaction, account or wire transfer that is on an OFAC list, Howard Bancorp or Howard Bank must freeze such account, file a suspicious activity report and notify the appropriate authorities.

Consumer Protection Laws

Howard Bank is subject to a number of federal and state laws designed to protect borrowers and promote lending to various sectors of the economy. These laws include the Equal Credit Opportunity Act, the Fair Housing Act, the Fair Credit Reporting Act, the Fair and Accurate Credit Transactions Act, the Truth in Lending Act, the Home Mortgage Disclosure Act, and the Real Estate Settlement Procedures Act, and various state law counterparts. Further, the Dodd-Frank Act established the Consumer Financial Protection Bureau ("CFPB"), which has the responsibility for making rules and regulations under the federal consumer protection laws relating to financial products and services. The CFPB also has a broad mandate to prohibit unfair or deceptive acts and practices and is specifically empowered to require certain disclosures to consumers and draft model disclosure forms. Failure to comply with consumer protection laws and regulations can subject financial institutions to enforcement actions, fines and other penalties. The FDIC will examine Howard Bank for compliance with CFPB rules and will enforce CFPB rules with respect to Howard Bank.

In addition, federal law currently contains extensive customer privacy protection provisions. Under these provisions, a financial institution must provide to its customers, at the inception of the customer relationship and annually thereafter, the institution's policies and procedures regarding the handling of customers' nonpublic personal financial information. These provisions also provide that, except for certain limited exceptions, a financial institution may not provide such personal information to unaffiliated third parties unless the institution discloses to the customer that such information may be so provided and the customer is given the opportunity to opt out of such disclosure. Further, under the ''Interagency Guidelines Establishing Information Security Standards,'' banks must implement a comprehensive information security program that includes administrative, technical, and physical safeguards to ensure the security and confidentiality of customer information. Federal law makes it a criminal offense, except in limited circumstances, to obtain or attempt to obtain customer information of a financial nature by fraudulent or deceptive means.

The Dodd-Frank Act

The Dodd-Frank Act, enacted in July 2010, has had and will continue to have a broad impact on the financial services industry, imposing significant regulatory and compliance changes, including the designation of certain financial companies as systemically significant, the imposition of increased capital, leverage, and liquidity requirements, and numerous other provisions designed to improve supervision and oversight of, and strengthen safety and soundness within, the financial services sector.

The following items provide a brief description of certain provisions of the Dodd-Frank Act.

- Source of strength. The Dodd-Frank Act requires all companies, including bank holding companies, that directly or indirectly control an insured depository institution to serve as a source of strength for the institution. Under this requirement, Howard Bancorp in the future could be required to provide financial assistance to Howard Bank should Howard Bank experience financial distress.
- Mortgage loan origination and risk retention. The Dodd-Frank Act contains additional regulatory requirements that may affect our operations and result in increased compliance costs. For example, the Dodd-Frank Act imposes new standards for mortgage loan originations on all lenders, including banks, in an effort to require steps to verify a borrower's ability to repay. In addition, the Dodd-Frank Act generally requires lenders or securitizers to retain an economic interest in the credit risk relating to loans the lender sells or mortgage and other asset-backed securities that the securitizer issues. The risk retention requirement generally will be 5%, but could be increased or decreased by regulation.
- CFPB. The Dodd-Frank Act created a new independent CFPB within the FRB. The CFPB is tasked with establishing and implementing rules and regulations under certain federal consumer protection laws with respect to the conduct of providers of certain consumer financial products and services. The CFPB has rulemaking authority over many of the statutes governing products and services offered to bank consumers. For banking organizations with assets under $10 billion, like Howard Bank, the CFPB has exclusive rule making authority, but the FDIC, as Howard Bank's primary federal regulator, would continue to have enforcement authority under federal consumer financial law. In addition, the Dodd-Frank Act permits states to adopt consumer protection laws and regulations that are stricter than those regulations promulgated by the CFPB. Compliance with any such new regulations would increase our cost of

operations.

- Deposit insurance. The Dodd-Frank Act permanently increased the deposit insurance limit to $250,000 for insured deposits. Amendments to the Federal Deposit Insurance Act also revise the assessment base against which an insured depository institution's deposit insurance premiums paid to the DIF will be calculated. Several of these provisions could increase the FDIC deposit insurance premiums paid by Howard Bank.
- Enhanced lending limits. The Dodd-Frank Act strengthened the limits on a depository institution's credit exposure to one borrower. Federal banking law limits a depository institution's ability to extend credit to one person (or group of related persons) in an amount exceeding certain thresholds. The Dodd-Frank Act expanded the scope of these restrictions to include credit exposure arising from derivative transactions, repurchase agreements, and securities lending and borrowing transactions.

Some of the requirements of the Dodd-Frank Act have been implemented, while others will be implemented over time and most will be subject to regulations implemented over the course of several years. Given the uncertainty associated with the manner in which the provisions of the Dodd-Frank Act will be implemented by the various regulatory agencies and through regulations, the full extent of the impact such requirements will have on our operations is unclear. The changes resulting from the Dodd-Frank Act may impact the profitability of our business activities, require changes to certain of our business practices, impose upon us more stringent capital, liquidity and leverage requirements or otherwise adversely affect our business. These changes may also require us to invest significant management attention and resources to evaluate and make any changes necessary to comply with new statutory and regulatory requirements. Failure to comply with the new requirements may negatively impact our results of operations and financial condition. While we cannot predict what effect any presently contemplated or future changes in the laws or regulations or their interpretations would have on us, these changes could be materially adverse to our investors.

Effect of Governmental Monetary Policies

Our earnings are affected by domestic economic conditions and the monetary and fiscal policies of the United States government and its agencies. The FRB's monetary policies have had, and are likely to continue to have, an important impact on the operating results of commercial banks through its power to implement national monetary policy in order, among other things, to curb inflation or combat a recession. The monetary policies of the FRB affect the levels of bank loans, investments and deposits through the FRB's control over the issuance of United States government securities, its regulation of the discount rate applicable to member banks and its influence over reserve requirements to which member banks are subject. We cannot predict the nature or impact of future changes in monetary and fiscal policies.

Federal and State Securities Laws

Our common stock is registered with the Securities and Exchange Commission under the Securities Exchange Act of 1934 (the "Exchange Act"). As such, we are subject to the information, proxy solicitation, insider trading restrictions and other requirements of the Exchange Act.

Further, if we wish to sell common stock or other securities to raise capital in the future, we will be subject to the registration, anti-fraud, and other applicable provisions of state and federal securities laws. For example, we will have to register the sales of such securities under the Securities Act, the Maryland Securities Act, and the applicable securities laws of each state in which we offer or sell the securities, unless an applicable exemption from registration exists with respect to such sales. Such exemptions may, among other things, limit the number and types of persons we could sell such securities to and the manner in which we could market the securities. We would also be subject to federal and state anti-fraud requirements with respect to any statements we make to potential purchasers in connection with the offer and sale of such securities.

Sarbanes-Oxley Act of 2002

The Sarbanes Oxley Act of 2002 addresses, among other issues, corporate governance, auditing and accounting, executive compensation, and enhanced and timely disclosure of corporate information. We have prepared policies, procedures and systems designed to ensure compliance with the Sarbanes Oxley Act and related regulations.

Item 1A. Risk Factors

You should consider carefully the following risks, along with the other information contained in and incorporated into this annual report. The risks and uncertainties described below are not the only ones that may affect us. Additional risks and uncertainties also may adversely affect our business and operations. If any of the following events actually occur, our business and financial results could be materially adversely affected.

Because our loan portfolio consists largely of commercial business and commercial real estate loans, our portfolio carries a higher degree of risk than would a portfolio composed primarily of residential mortgage loans.

Our loan portfolio is made up largely of commercial business loans and commercial real estate loans, most of which is collateralized by real estate. These types of loans generally expose a lender to a higher degree of credit risk of non-payment and loss than do residential mortgage loans because of several factors, including dependence on the successful operation of a business or a project for repayment, the collateral securing these loans may not be sold as easily as residential real estate, and loan terms with a balloon payment rather than full amortization over the loan term. In addition, commercial real estate and commercial loans typically involve larger loan balances to single borrowers or groups of related borrowers compared to one- to four-family residential mortgage loans. Consequently, an adverse development with respect to one loan or one credit relationship can expose us to a significantly greater risk of loss compared to an adverse development with respect to a one- to four-family residential mortgage loan. Underwriting and portfolio management activities cannot completely eliminate all risks related to these loans. Any significant failure to pay on time by our customers or a significant default by our customers would materially and adversely affect us.

We make both secured and some unsecured commercial and industrial loans. Unsecured loans generally involve a higher degree of risk of loss than do secured loans because, without collateral, repayment is wholly dependent upon the success of the borrowers' businesses. Secured commercial and industrial loans are generally collateralized by accounts receivable, inventory, equipment or other assets owned by the borrower and include a personal guaranty of the business owner. Compared to real estate, that type of collateral is more difficult to monitor, its value is harder to ascertain, it may depreciate more rapidly and it may not be as readily saleable if repossessed. Further, commercial and industrial loans generally will be serviced primarily from the operation of the business, which may not be successful, and commercial real estate loans generally will be serviced from income on the properties securing the loans.

While any declines in the value of our real estate collateral securing loans have been reflected in existing reserves, the discounts and reserves we have taken against our loan portfolio based on our internal review of economic conditions and their impact on real estate values in our market areas may be insufficient. Further deterioration in the real estate market or a prolonged economic recovery could adversely affect the value of the properties securing the loans or revenues from borrowers' businesses, thereby increasing the risk of non-performing loans and increased portfolio losses that could materially and adversely affect us.

In addition, while our commercial borrowers are slowly recovering from the recent economic recession, they have been impacted by the continuing decreased levels of consumer and business spending that began during the recession and its aftermath. Small businesses that make up the majority of our commercial borrowers generally do not have the cash reserves to help cushion them from an economic slowdown to the same extent that large borrowers do and thus may be more heavily impacted by an economic downturn. A continued sluggish economy or another economic slowdown may have a negative effect on the ability of our commercial borrowers to make timely repayments of their loans, which could have an adverse impact on our earnings.

Current market conditions include an over-supply of land, lots and finished homes in many markets, including those where we do business. Construction loans are subject to risks during the construction phase that are not present in standard residential real estate and commercial real estate loans. These risks include:

- the viability of the contractor;
- the value of the project being subject to successful completion;
- the contractor's ability to complete the project, to meet deadlines and time schedules and to stay within cost estimates; and
- concentrations of such loans with a single contractor and its affiliates.

Real estate construction and land loans also present risks of default in the event of declines in property values or volatility in the real estate market during the construction phase. If we are forced to foreclose on a project prior to completion, we may not be able to recover the entire unpaid portion of the loan, may be required to fund additional amounts to complete a project and may have to hold the property for an indeterminate amount of time. If any of these risks were to occur, it could adversely affect our financial condition, results of operations and cash flows.

The federal banking agencies have issued guidance regarding high concentrations of commercial real estate loans within bank loan portfolios. The guidance requires financial institutions that exceed certain levels of commercial real estate lending compared with their total capital to maintain heightened risk management practices that address the following key elements: including board and management oversight and strategic planning, portfolio management, development of underwriting standards, risk assessment and monitoring through market analysis and stress testing, and maintenance of increased capital levels as needed to support the level of commercial real estate lending. If there is any deterioration in our commercial real estate or real estate construction and land portfolios or if our regulators conclude that we have not implemented appropriate risk management practices, it could adversely affect our business

and result in a requirement of increased capital levels, and such capital may not be available at that time.

We are subject to security and operational risks relating to our use of technology that could damage our reputation and our business.

We rely heavily on communications and information systems to conduct our business. System failure or security breaches in our Internet banking activities or other communication and information systems could damage our reputation, result in a loss of customer business, cause us to incur expenses to rectify, subject us to additional regulatory scrutiny or expose us to civil litigation and possible financial liability, any of which could have a material adverse effect on our financial condition and results of operations. We rely on standard Internet and other security systems to provide the security and authentication necessary to effect secure transmission of data. These precautions may not protect our systems from damage or compromises or breaches of our security measures. We continue to monitor developments in this area and consider whether additional protective measures are necessary or appropriate, and we have obtained insurance protection intended to cover losses due to network security breaches; there is no guarantee, however, that such insurance would cover all costs associated with any breach, damage or failure of our computer systems and network infrastructure.

We rely on certain external vendors. Our business is dependent on the use of outside service providers that support our day-to-day operations including data processing and electronic communications.

Our business is dependent on the use of outside service providers that support our day-to-day operations including data processing and electronic communications. Our operations are exposed to the risk that a service provider may not perform in accordance with established performance standards required in our agreements for any number of reasons including equipment or network failure, a change in their senior management, their financial condition, their product line or mix and how they support existing customers, or a simple change in their strategic focus. While we have comprehensive policies and procedures in place to mitigate risk at all phases of service provider management from selection to performance monitoring and renewals, the failure of a service provider to perform in accordance with contractual agreements could be disruptive to our business, which could have a material adverse effect on our financial conditions and results of operations.

Because our loan portfolio includes residential real estate loans, our earnings are sensitive to the credit risks associated with these types of loans.

We originate and retain in our portfolio residential mortgage loans and intend to increase our origination of these types of loans. While residential real estate loans are more diversified than loans to commercial borrowers, and our local real estate market and economy have performed better than many other markets, a downturn could cause higher unemployment, more delinquencies, and could adversely affect the value of properties securing loans in our portfolio. In addition, should values begin to decline again, the real estate market may take longer to recover or not recover to previous levels. These risks increase the probability of an adverse impact on our financial results as fewer borrowers would be eligible to borrow and property values could be below necessary levels required for adequate coverage on the requested loan.

Our residential lending department may not continue to provide us with significant noninterest income.

The residential mortgage business is highly competitive, and highly susceptible to changes in market interest rates, consumer confidence levels, employment statistics, the capacity and willingness of secondary market purchasers to acquire and hold or securitize loans, and other factors beyond our control. Additionally, in many respects, the mortgage origination business is relationship based, and dependent on the services of individual mortgage loan officers. The loss of services of one or more loan officers could have the effect of reducing the level of our mortgage production, or the rate of growth of production. As a result of these factors we cannot be certain that we will not be able to continue to increase the volume or percentage of revenue or net income produced by the residential mortgage business.

Our financial condition, earnings and asset quality could be adversely affected if we are required to repurchase loans originated for sale by our residential lending department.

The Bank originates residential mortgage loans for sale to secondary market investors, subject to contractually specified and limited recourse provisions. Because the loans are intended to be originated within investor guidelines, using designated automated underwriting and product specific requirements as part of the loan application, the loans sold have a limited recourse provision. In general, the Bank may be required to repurchase a previously sold mortgage loan or indemnify the investor if there is non-compliance with defined loan origination or documentation standards, including fraud, negligence, material misstatement in the loan documents or noncompliance with applicable law. In addition, the Bank may have an obligation to repurchase a loan if the mortgagor has defaulted early in the loan term. The potential mortgagor early default repurchase period is up to approximately twelve months after sale of the loan to the investor. The recourse period for fraud, material misstatement, breach of representations and warranties, noncompliance with law, or similar matters could be as long as the term of the loan. Mortgages subject to recourse are collateralized by single-family residential properties, have loan-to-value ratios of 80% or less, or have private mortgage insurance. Our experience to date has been minimal in the case of loan repurchases due to default, fraud, breach of representations, material misstatement, or legal noncompliance. Should repurchases become a material issue, our earnings and asset quality could be adversely impacted, which could adversely impact our share price.

If our allowance for credit losses is not sufficient to cover actual loan losses, our earnings would decrease.

We maintain an allowance for credit losses that we believe is adequate for absorbing any potential losses in our loan portfolio. Management, through a periodic review and consideration of our loan portfolio, determines the amount of the allowance for credit losses. We cannot, however, predict with certainty the amount of probable losses in our portfolio or be sure that our allowance will be adequate in the future. If management’s assumptions and judgments prove to be incorrect and the allowance for credit losses is inadequate to absorb future losses, our losses will increase and our earnings will suffer.

In particular, it is more difficult to estimate loan losses for those types of loans - commercial and commercial real estate - that constitute the majority of our portfolio as compared to, for example, residential mortgage loans. Also, because these types of loans tend to have large loan balances, a loss on a single loan could have a significant adverse effect on our operations.

In determining the amount of the allowance for credit losses, we review our loans and our loss and delinquency experience, and evaluate economic conditions. If our assumptions are incorrect, our allowance for credit losses may not be sufficient to cover future incurred losses in our loan portfolio, resulting in additions to the allowance and a corresponding decrease to earnings. Material additions to the allowance could materially decrease our net income. If delinquencies and defaults continue to increase, we may be required to further increase our provision for loan losses.

In addition, bank regulators periodically review our allowance for credit losses and may require an increase in the provision for loan losses or further loan charge-offs to the allowance for credit losses. Any increase in the allowance for credit losses or loan charge-offs might have a material adverse effect on our financial condition and results of operations.

Our growth strategy may not be successful, may be dilutive and may have other adverse consequences.

As previously mentioned, a key component of our growth strategy is to pursue acquisitions of other financial institutions or branches of other financial institutions. As consolidation of the banking industry continues, the competition for suitable acquisition candidates may increase. We compete with other banking companies for acquisition opportunities, and there are a limited number of candidates that meet our acquisition criteria. Consequently, we may not be able to identify suitable candidates for acquisitions. If we are unable to locate suitable acquisition candidates willing to sell on terms acceptable to us, our net income could decline and we would be required to find other methods to grow our business. We may also open additional branches organically and expand into new markets or offer new products and services. These activities would involve a number of risks, including:

- the time and expense associated with identifying and evaluating potential acquisitions and merger partners;
- using inaccurate estimates and judgments to evaluate credit, operations, management and market risks with respect to the target institution or its branches or assets;
- diluting our existing stockholders in an acquisition;
- the time and expense associated with evaluating new markets for expansion, hiring experienced local management and opening new offices or branches as there may be a substantial time lag between these activities before we generate sufficient assets and deposits to support the costs of the expansion;
- operating in markets in which we have had no or only limited experience;
- taking a significant amount of time negotiating a transaction or working on expansion plans, resulting in management's time and attention being diverted from the operation of our existing business;
- we may not be able to correctly identify profitable or growing markets for new branches;
- the time and expense associated with integrating the operations and personnel of the combined businesses;
- the ability to realize the anticipated benefits of the acquisition;
- creating an adverse short-term effect on our results of operations;
- losing key employees and customers as a result of an acquisition that is poorly received;
- time and costs associated with regulatory approvals;
- lack of information on a target institution or its branches or assets;
- inability to obtain additional financing (including by issuing additional common equity), if necessary, on favorable terms or at all; and
- unforeseen adjustments, write-downs, write-offs or restructuring or other impairment charges.

In addition, we may not be able to integrate successfully or operate profitably any financial institutions we may acquire. We may experience disruption and incur unexpected expenses in integrating acquisitions. Any acquisitions we do make may not enhance our cash flows, business, financial condition, results of operations or prospects and may have an adverse effect on our results of operations, particularly during periods in which the acquisitions are being

integrated into our operations.

Also, the costs to lease and start up new branch facilities or to acquire existing financial institutions or branches, and the additional costs to operate these facilities, may increase our noninterest expense. It also may be difficult to adequately and profitably manage the anticipated growth from the new branches. We can provide no assurance that any new branch sites will successfully attract a sufficient level of deposits and other banking business to offset their operating expenses.

Further, we plan to continue to make investments in our infrastructure in the future. We also currently plan to open additional branches in the areas where we now operate and in other markets over the next few years. We anticipate that this will have the short-term effect of, at least temporarily, increasing our expenses at a faster rate than revenue growth, which will have an adverse effect on net income.

If we grow too quickly and are not able to control costs and maintain asset quality, growth could materially and adversely affect our financial condition and results of operations. Further, we may not be successful in our growth strategy, which would negatively impact our financial condition and results of operations.

Consumers may decide not to use banks to complete their financial transactions.

Technology and other changes are allowing consumers to complete financial transactions through alternative methods that historically have involved banks. For example, consumers can now maintain funds that would have historically been held as bank deposits in brokerage accounts, mutual funds or general-purpose reloadable prepaid cards. Consumers can also complete transactions such as paying bills and transferring funds directly without the assistance of banks. The process of eliminating banks as intermediaries, which may increase as consumers become more comfortable with these new technologies and offerings, could result in the loss of fee income, as well as the loss of customer deposits and the related income generated from those deposits. The loss of these revenue streams and the lower cost of deposits as a source of funds could have a material adverse effect on our financial condition and results of operations.

Strong competition within our market area may limit our growth and profitability.

Competition in the banking and financial services industry is intense. In our market area, we compete with, among others, commercial banks, savings institutions, mortgage brokerage firms, credit unions, mutual funds, and insurance companies operating locally and elsewhere. There are also a number of smaller community-based banks that pursue similar operating strategies as Howard Bank. In addition, some of our competitors have recently offered loans with lower fixed rates and loans on more attractive terms than we have been willing to offer. Our continued profitability depends upon our continued ability to successfully compete in our market area. The greater resources and deposit and loan products offered by our competition may limit our ability to increase our interest earning assets. See “Item 1. Business—Competition” for more information about competition in our market area.

The financial services industry could become even more competitive as a result of legislative, regulatory and technological changes and continued consolidation. Banks, securities firms and insurance companies can merge under the umbrella of a financial holding company, which can offer virtually any type of financial service, including banking, securities underwriting, insurance (both agency and underwriting) and merchant banking. Increased competition among financial services companies due to the recent consolidation of certain competing financial institutions may adversely affect our ability to market our products and services. Also, technology has lowered barriers to entry and made it possible for banks to compete in our market without a retail footprint by offering competitive rates, as well as non-banks to offer products and services traditionally provided by banks. Additionally, due to their size, many competitors may offer a broader range of products and services as well as better pricing for certain products and services than we can, which could affect our ability to grow and remain profitable on a long-term basis. Our profitability depends upon our ability to successfully compete in our market area. If we must raise interest rates paid on deposits or lower interest rates charged on our loans, our net interest margin and profitability could be adversely affected.

We continually encounter technological change.

The financial services industry is continually undergoing rapid technological change with frequent introductions of new technology driven by new or modified products and services. The effective use of technology increases efficiency and enables financial institutions to better serve customers and to reduce costs. Our future success depends, in part, upon our ability to address the needs of our customers by using technology to provide products and services that will satisfy customer demands, as well as to create additional efficiencies in our operations. Many of our competitors have substantially greater resources to invest in technological improvements. We may not be able to effectively implement new technology-driven products and services or be successful in marketing these products and services to our customers. Failure to successfully keep pace with technological change affecting the financial services industry could have a material adverse effect on our business and, in turn, our financial condition and results of operations.

New regulations may negatively impact our mortgage banking business.

The Dodd Frank Act required the regulatory agencies to issue regulations that require securitizers of loans retain “not less than 5% of the credit risk for any asset that is not a qualified residential mortgage.” The rule, issued in 2014, aligns the definition of “qualified residential mortgage” with the definition of “qualified mortgage” as defined by the CFPB for purposes of its regulations. The final rule became effective on February 23, 2015. Compliance with the final rule was required beginning December 24, 2015 with respect to asset-backed securities collateralized by residential mortgages, and is required beginning December 24, 2016 with respect to all other classes of asset-backed securities. The final rule could have a significant effect on the secondary market for loans and the types of loans we originate, and restrict our ability to originate residential mortgage loans.

We must comply with extensive and complex governmental regulation, which could have an adverse effect on our business and our growth strategy, and we may be adversely affected by changes in laws and regulations.

The banking industry is subject to extensive regulation by state and federal banking authorities. Many of these regulations are intended to protect depositors, the public or the FDIC insurance funds, not stockholders. Regulatory requirements affect our lending practices, capital structure, investment practices, dividend policy and many other aspects of our business. These requirements may constrain our operations, and changes in regulations could adversely affect us. The burden imposed by these federal and state regulations may place banks in general, and Howard Bank specifically, at a competitive disadvantage compared to less regulated competitors. In addition, the cost of compliance with regulatory requirements could adversely affect our ability to operate profitably or increase profitability. See "Supervision and Regulation" for more information about applicable banking laws and regulations. Further, if we are not in compliance with such requirements, we could be subject to fines or other regulatory action that could restrict our ability to operate or otherwise have a material adverse effect on our business and financial condition. Although we believe we are material compliance with all applicable regulations, it is possible there are violations of which we are unaware that could be discovered by our regulators in the course of an examination or otherwise, which could trigger such fines or other adverse consequences

Further, regulatory authorities have extensive discretion in their supervisory and enforcement activities, including the imposition of restrictions on our operations, classification of our assets and determination of the level of our allowance for credit losses. If regulators require Howard Bank to charge-off loans or increase its allowance for credit losses, our earnings would suffer. Any change in such regulation and oversight, whether in the form of regulatory policy, regulation, legislation or supervisory action, may have a material impact on our operations. For a further discussion, see "Supervision and Regulation."

In addition, because regulation of financial institutions changes regularly and is the subject of constant legislative debate, we cannot forecast how federal or state regulation of financial institutions may change in the future and impact our operations. Changes in regulation and oversight, including in the form of changes to statutes, regulations or regulatory policies or changes in interpretation or implementation of statutes, regulations or policies, could affect the service and products we offer, increase our operating expenses, increase compliance challenges and otherwise adversely impact our financial performance and condition. In addition, the burden imposed by these federal and state regulations may place banks in general, and Howard Bank specifically, at a competitive disadvantage compared to less regulated competitors.

The Company and the Bank implemented an enhanced organizational structure to ensure that the risk management activities of the Company are scaled to the entire enterprise. The office of strategic risk management, reporting to an executive vice president with direct reporting to the CEO and a dotted line reporting to the full board, is responsible for credit, compliance and operational, physical and IT security, legal, reputational and other on and off balance sheet risks.

Further, as a public company, we incur significant legal, accounting, insurance and other expenses in connection with compliance with rules of the SEC and the rules of The NASDAQ Stock Market LLC.

A worsening of economic conditions could adversely affect our results of operations and financial condition.

We continue to operate in a challenging and uncertain economic environment. Economic growth continues to be slow and uneven. A return to recessionary conditions or prolonged stagnant or deteriorating economic conditions could significantly affect the markets in which we do business, the demand for our products and services, the value of our loans and investments, and our ongoing operations, costs and profitability. Further continuing economic uncertainty, including regarding concerns about U.S. debt levels and related governmental actions, including potential tax increases and cuts in government spending, may negatively impact economic conditions going forward. In addition, an increase in unemployment levels may result in higher than expected loan delinquencies, increases in our nonperforming and criticized classified assets and a decline in demand for our products and services. These events may cause us to incur losses and may adversely affect our financial condition and results of operations.

Furthermore, the FRB, in an attempt to help the overall economy, has among other things kept interest rates low through its targeted federal funds rate and the purchase of U.S. Treasury and mortgage-backed securities. If the FRB increases the federal funds rate in the near term, overall interest rates will likely rise, which may negatively impact the housing markets and the U.S. economic growth. In addition, deflationary pressures, while possibly lowering our operating costs, could have a negative impact on our borrowers, especially our commercial borrowers, and the values of collateral securing our loans, which could negatively affect our financial performance.

Our profitability depends on interest rates, and changes in interest rates could have an adverse impact on our results of operations and financial condition.

Our results of operations will depend to a large extent on our "net interest income," which is the difference between the interest expense incurred in connection with our interest-bearing liabilities, such as interest on deposit accounts, and the interest income received from our interest-earning assets, such as loans and investment securities. Changes in interest rates can increase or decrease our net interest income, because different types of assets and liabilities may react differently, and at different times, to market interest rate changes. When interest bearing liabilities mature or reprice more quickly than interest earning assets in a period, an increase in interest rates could reduce net interest income. Similarly, when interest earning assets mature or reprice more quickly than interest bearing liabilities, falling interest rates could reduce net interest income. Additionally, an increase in interest rates may, among other things, reduce the demand for loans and our ability to originate loans and decrease loan repayment rates. A decrease in the general level of interest rates may affect us through, among other things, increased prepayments on our loan and mortgage-backed securities portfolios and increased competition for deposits. Accordingly, changes in the level of market interest rates affect our net yield on interest earning assets, loan origination volume, loan and mortgage-backed securities portfolios, and our overall results. Fluctuations in interest rates are highly sensitive to many factors that are not predictable or controllable. Therefore, while we attempt to manage our risk from changes in market interest rates by adjusting the rates, maturity, repricing, and balances of the different types of interest-earning assets and interest bearing liabilities, we might not be able to maintain a consistent positive spread between the interest that we receive and the interest that we pay. As a result, a rapid increase or decrease in interest rates could have an adverse effect on our net interest margin and results of operations.

The capital rules that were issued require insured depository institutions and their holding companies to hold more capital. The impact of the new rules on our financial condition and operations is uncertain but could be materially adverse.

In July 2013, the bank regulators adopted a final rule for the Basel III capital framework. These rules apply to all depository institutions, top-tier bank holding companies with total consolidated assets of $1 billion or more and top-tier savings and loan holding companies and substantially amend the regulatory risk-based capital rules applicable to us. The rules phase in over time beginning in 2015 and will become fully effective in 2019. The rules apply to Howard Bank and will apply to Howard Bancorp after it achieves total consolidated assets of $1 billion or more. Beginning in 2015, Howard Bank's minimum risk-based capital requirements are (i) a common equity Tier 1 ratio of 4.5%, (ii) a Tier 1 capital (common Tier 1 capital plus Additional Tier 1 capital) ratio of 6% (up from 4%) and (iii) a total capital ratio of 8% (the current requirement). Our leverage ratio requirement will remain at the 4% level now required. Beginning in 2016, a capital conservation buffer will phase in over three years, ultimately resulting in a requirement of an additional 2.5% of common equity Tier 1 capital on top of the minimum common equity Tier 1, Tier 1 and total capital requirements, resulting in a required common equity Tier 1 ratio of 7%, a required Tier 1 ratio of 8.5%, and a required total capital ratio of 10.5%. Failure to satisfy any of these three capital requirements will result in limits on paying dividends, engaging in share repurchases and paying discretionary bonuses. These limitations will establish a maximum percentage of eligible retained income that could be utilized for such actions.

Monetary policy and general economic conditions will influence our results of operations.

Governmental economic and monetary policy will influence our results of operations. The rates of interest payable on deposits and chargeable on loans are affected by fiscal policy as determined by various governmental and regulatory authorities, in particular the FRB, as well as by national, state and local economic conditions. In addition, adverse general economic conditions may impair the ability of our borrowers to repay loans.

Regulations pursuant to the Dodd Frank Act may adversely impact our results of operations, liquidity or financial condition. The Dodd-Frank Act represents a comprehensive overhaul of the U.S. financial services industry.

The Dodd Frank Act required the CFPB and other federal agencies to issue many new and significant rules and regulations to implement its various provisions. There are a number of regulations under the Dodd Frank Act that have not yet been fully adopted and implemented and we will not know the full impact of the Dodd Frank Act on our business until such regulations are fully implemented. As a result, we cannot predict the full extent to which the Dodd Frank Act will impact our business, operations or financial condition. However, compliance with these new laws and regulations may require us to make changes to our business and operations and will likely result in additional costs and a diversion of management's time from other business activities, any of which may adversely impact our results of operations, liquidity or financial condition.

Because the Bank serves a limited market area, we could be more adversely affected by an economic downturn in our market area than our larger competitors that are more geographically diverse.

Our current primary market area consists of the Greater Baltimore Metropolitan Area. Broad geographic diversification is not currently part of our community bank focus. As a result, if our market areas suffer an economic downturn, our business and financial condition may be more severely affected by such circumstances than are our larger competitors. Factors that adversely affect the economy in our target markets could reduce our deposit base and demand for our services and products and increase our credit losses. Consequently, we may be adversely affected, potentially materially, by adverse changes in economic conditions in and around our market areas. Our larger bank competitors, for example, serve more geographically diverse market areas, parts of which may not be affected by the same economic conditions that may exist in our market areas.

Further, unexpected changes in the national and local economy may adversely affect our ability to attract deposits and to make loans. In particular, due to the proximity of our primary and secondary market areas to Washington, D.C., decreases in spending by the Federal government, could impact us more than banks that serve a larger or a different geographical area. Such risks are beyond our control and may have a material adverse effect on our financial condition and results of operations and, in turn, the value of our common stock.

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The small to medium-sized businesses that the Bank lends to may have fewer resources to weather a downturn in the economy, which may impair a borrower's ability to repay a loan to the Bank that could materially harm our operating results.

The Bank targets its business development and marketing strategy primarily to serve the banking and financial services needs of small to medium-sized businesses. These small to medium-sized businesses frequently have smaller market share than their competition, may be more vulnerable to economic downturns, often need substantial additional capital to expand or compete and may experience significant volatility in operating results. Any one or more of these factors may impair the borrower's ability to repay a loan. In addition, the success of a small to medium-sized business often depends on the management talents and efforts of one or two persons or a small group of persons, and the death, disability or resignation of one or more of these persons could have a material adverse impact on the business and its ability to repay a loan. Economic downturns and other events that negatively impact our market areas could cause the Bank to incur substantial credit losses that could negatively affect our results of operations and financial condition.

We depend heavily on five key employees, Mary Ann Scully, Robert A. Altieri, Dennis E. Finnegan, Charles E. Schwabe and George C. Coffman, to continue the implementation of our long-term business strategy and the loss of their services could disrupt our operations and result in reduced earnings.

Ms. Scully is our President and Chief Executive Officer, Mr. Altieri is an Executive Vice President, President of our Mortgage Banking Division and our Chief Specialty Lending Officer, Mr. Finnegan is an Executive Vice President and our Chief Deposit Officer, Mr. Schwabe is an Executive Vice President and our Secretary, Chief Administrative Officer, and Chief Risk Officer, and Mr. Coffman is an Executive Vice President and our Chief Financial Officer. We believe that our continued growth and future success will depend in large part on the skills of our senior management team. We believe our senior management team possesses valuable knowledge about and experience in the banking industry and that their knowledge and relationships would be difficult to replicate. We have entered into an employment agreement with each of Ms. Scully, Mr. Altieri, Mr. Finnegan, Mr. Schwabe and Mr. Coffman and acquired key-person life insurance on each such executive officer, but the existence of such agreements and insurance does not assure that we will be able to retain their services or recover losses associated with the loss of their services. The unexpected loss of the services of Ms. Scully, Mr. Altieri, Mr. Finnegan, Mr. Schwabe or Mr. Coffman could have a material adverse effect on our business, operations, financial condition and operating results, as well as the value of our common stock.

Federal and state banking agencies periodically conduct examinations of our business, including compliance with laws and regulations, and our failure to comply with any supervisory actions to which we are or become subject as a result of such examinations may adversely affect us.

State and federal banking agencies, including the FDIC and the Maryland Office of the Commissioner of Financial Regulation, periodically conduct examinations of our business, including compliance with laws and regulations. If, as

a result of an examination, a state or federal banking agency were to determine that our financial condition, capital resources, asset quality, earnings prospects, management, liquidity or other aspects of any of our operations had become unsatisfactory, or that we or our management was in violation of any law or regulation, it may take a number of different remedial actions as it deems appropriate. These actions include the power to enjoin “unsafe or unsound” practices, to require affirmative actions to correct any conditions resulting from any violation or practice, to issue an administrative order that can be judicially enforced, to direct an increase in our capital, to restrict our growth, to assess civil monetary penalties against our officers or directors, to remove officers and directors and, if it is concluded that such conditions cannot be corrected or there is an imminent risk of loss to depositors, to terminate the Bank’s deposit insurance. If we become subject to such regulatory actions, our business, results of operations and reputation may be negatively impacted.

Many of our new activities and expansion plans require regulatory approvals, and failure to obtain them may restrict our growth.

We intend to complement and expand our business by continuing to pursue strategic acquisitions of banks and other financial institutions. We must generally receive regulatory approval before we can acquire an institution or business. Such regulatory approvals may not be granted on terms that are acceptable to us, or at all. We may also be required to sell branches as a condition to receiving regulatory approval, which condition may not be acceptable to us or, if acceptable to us, may reduce the benefit of any acquisition.

In addition to the acquisition of existing financial institutions, as opportunities arise, we plan to continue de novo branching as a part of our internal growth strategy and possibly enter into new markets through de novo branching. De novo branching and any acquisition carries with it numerous risks, including the inability to obtain all required regulatory approvals. The failure to obtain these regulatory approvals for potential future strategic acquisitions and de novo branches may impact our business plans and restrict our growth.

Failure to pay dividends on our Series AA Preferred Stock may have negative consequences, including external involvement in our board of directors.

If dividends on the Series AA Preferred Stock are not paid in full for six quarterly dividend periods, whether or not consecutive, and if the aggregate liquidation preference amount of the then-outstanding shares of Series AA Preferred Stock is at least $25.0 million, the total number of positions on our board of directors will automatically increase by two and the holders of the Series AA Preferred Stock, acting as a single class, will have the right to elect two individuals to serve in the new director positions. This right and the terms of such directors will end when we have paid full dividends for at least four consecutive quarterly dividend periods. If full dividends have not been paid on the Series AA Preferred Stock for five or more quarterly dividend periods, whether or not consecutive, we must invite a representative selected by the holders of a majority of the outstanding shares of Series AA Preferred Stock, voting as a single class, to attend all meetings of our board of directors in a nonvoting observer capacity. Any such representative would not be obligated to attend any board meeting to which he or she is invited, and this right will end when we have paid full dividends for at least four consecutive dividend periods.

Our preferred shares impact net income available to our common stockholders and our earnings per share.

The dividends declared on the Series AA Preferred Stock reduce net income available to common shareholders and our earnings per common share. The Series AA Preferred Stock will also receive preferential treatment in the event of liquidation, dissolution or winding up of the Company.

We may be required to raise additional capital in the future, but that capital may not be available when it is needed on attractive terms, or at all.

We are required by regulatory authorities to maintain adequate levels of capital to support our operations. Our capital requirements for the foreseeable future are currently satisfied. We may at some point, however, need to raise additional capital to support our continued growth, or if our liquidity is adversely affected by external factors such as worsening economic conditions or continued economic uncertainty. Our ability to raise additional capital, if needed, will depend in part on conditions in the capital markets at that time, which are outside our control. Accordingly, we cannot assure you of our ability to raise additional capital, if needed, on terms acceptable to us. If we cannot raise additional capital when needed, our ability to further expand our operations could be materially impaired, or the failure to raise additional capital could have a material adverse effect on our liquidity, financial condition or results of operations. In addition, if we decide to raise additional equity capital, your interest in Howard Bancorp could be diluted. Furthermore, if we raise additional capital through the issuance of debt securities, there can be no assurance that sufficient revenues or cash flow will exist to service such debt.

The market value of our investments could negatively impact stockholders' equity.

All of our securities investment portfolio as of December 31, 2015 has been designated as available for sale pursuant to Statement of Financial Accounting Standards, Accounting Standards Codification ("ASC") Topic 320 – "Investments. ASC Topic 320 requires that unrealized gains and losses in the estimated value of the available for sale portfolio be "marked to market" and reflected as a separate item in stockholders' equity, net of tax. If the market value of the investment portfolio declines, this could cause a corresponding decline in stockholders' equity.

Our lending limit may limit our growth.

We are limited in the amount we can loan to a single borrower by the amount of our capital. Generally, under current law, we may lend up to 15% of our unimpaired capital and surplus to any one borrower. Based upon our current capital levels, the amount we may lend is significantly less than that of many of our competitors and may discourage potential borrowers who have credit needs in excess of our lending limit from doing business with us. We accommodate larger loans by selling participations in those loans to other financial institutions, but this strategy may not always be available.

We are a community bank and our ability to maintain our reputation is critical to the success of our business and the failure to do so may materially adversely affect our performance.

We are a community bank, and our reputation is one of the most valuable components of our business. As such, we strive to conduct our business in a manner that enhances our reputation. This is done, in part, by recruiting, hiring and retaining employees who share our core values of being an integral part of the communities we serve, delivering superior service to our customers and caring about our customers and associates. If our reputation is negatively affected, by the actions of our employees or otherwise, our business and, therefore, our operating results may be materially adversely affected.

Anti-takeover provisions in our corporate documents and in Maryland corporate law may make it difficult and expensive to remove current management.

Anti-takeover provisions in our corporate documents and in Maryland law may render the removal of our existing board of directors and management more difficult. Consequently, it may be difficult and expensive for our stockholders to remove current management, even if current management is not performing adequately.

Our articles of incorporation limit the liability of our directors and officers.

Our articles of incorporation provide that, to the full extent permitted by Maryland law, no director or officer of Howard Bancorp will be liable to us or our stockholders for money damages. This limitation could impair the ability of us and our stockholders to recover for damages resulting from acts or omissions of our directors and officers.

The market price for our common stock may be volatile.

The market price of our common stock could be subject to significant fluctuations due to changes in sentiment in the market regarding our operations or business prospects. Factors that may affect market sentiment include:

- operating results that vary from the expectations of our management or of securities analysts and investors;
- developments in our business or in the financial service sector generally;
- regulatory or legislative changes affecting our industry generally or our business and operations in particular;
- operating and securities price performance of companies that investors consider to be comparable to us;
- changes in estimates or recommendations by securities analysts;
- announcements of strategic developments, acquisitions, dispositions, financings and other material events by us or our competitors; and
- changes in financial markets and national and local economies and general market conditions, such as interest rates and stock, commodity, credit or asset valuations or volatility.

While the U.S. and other governments continue efforts to restore confidence in financial markets and promote economic growth, market and economic turmoil could still occur in the near- or long-term, negatively affecting our business, financial condition and results of operations, as well as the price, trading volume and volatility of our common stock.

We can sell additional shares of common stock without consulting stockholders and without offering shares to existing stockholders, which would result in dilution of stockholders' interests in Howard Bancorp and could depress our stock price.

Our articles of incorporation currently authorize an aggregate of 10 million shares of common stock, 6,964,918 of which are outstanding as of the date of this report, 137,463 of which are reserved for issuance pursuant to outstanding options granted under our stock incentive plans and employment agreements and 608,399 of which are reserved for issuance pursuant to future grants under our stock incentive plans. Our board of directors has the authority to amend our articles of incorporation, without stockholder approval, to increase or decrease the aggregate number of shares of stock or the number of shares of any class of stock that we have the authority to issue. The board of directors is further authorized to issue additional shares of common stock and preferred stock, at such times and for such consideration as it may determine, without stockholder action. The ability of the board of directors to increase our authorized shares of capital stock, and the existence of authorized but unissued shares of common stock and preferred stock, could have the effect of rendering more difficult or discouraging hostile takeover attempts, or of facilitating a negotiated acquisition and could affect the market for and price of our common stock. Because our common stockholders do not have preemptive rights to purchase shares of our capital stock (that is, the right to purchase a stockholder's pro rata share of any securities issued by Howard Bancorp), any future offering of capital stock could have a dilutive effect on holders of our common stock.

Item 1B. Unresolved Staff Comments

Not applicable

Item 2. Properties

Our headquarters are located in Ellicott City, Maryland. The Bank owns nine full-service branches and leased the remaining branches. See Note 9 to the Notes to the Consolidated Financial Statements for additional information.

We own the following properties, which had a book value of $15.3 million at December 31, 2015:

Branch Locations	Address	Description
Maple Lawn (1)	10985 Johns Hopkins Road Laurel, MD 20723	Full service branch with drive-thru
Centennial	10161 Baltimore National Pike Ellicott City, MD 21042	Full service branch with drive-thru
Aberdeen	3 West Bel Air Aberdeen, MD 21001	Full service branch with drive-thru
Rising Sun	6 Pearl Street Rising Sun, MD 21911	Full service branch with drive-thru
Elkton (1)	305 Augustine Herman Highway Elkton, MD 21921	Full service branch with drive-thru
Dublin	3535 Conowingo Rd. Street, MD 21154	Full service branch with drive-thru
Dundalk	1301 Merritt Blvd. Dundalk, MD 21222	Full service branch with drive-thru
Parkville (1)	2028 E. Joppa Road Parkville, MD 21234	Full service branch with drive-thru
Hampden	821 W. 36th Street Baltimore, MD 21211	Full service branch

Office Locations	Address	Description
Innovation Center	10163 Baltimore National Pike Ellicott City, MD 21042	Information Technology and other support functions

(1) The premises are owned, but are subject to a ground lease.

We lease the following branches:

Branch Locations	Address	Description
Snowden River	6011 University Blvd Suite 150 Ellicott City, MD 21043	Full service branch with drive-thru
Defense Highway	116 Defense Highway Annapolis, MD 21401	Full service branch with drive-thru
Towson	22 West Pennsylvania Avenue Baltimore, MD 21204	Full service branch with drive-thru
Bel Air	101 North Main Street Bel Air, MD 21014	Full service branch with drive-thru

Havre de Grace	800 Revolution Street Havre de Grace, MD 21078	Full service branch with drive-thru
Penn Hill	2006 Lancaster Pike Peach Bottom, PA 17563	Full service branch with drive-thru
Glen Arm	12128 Long Green Pike Glen Arm, MD 21057	Full service branch with drive-thru

We lease the following facilities unless otherwise noted:

Office Locations	**Address**	**Description**
Corporate Office	6011 University Blvd Suite 370 Ellicott City, MD 21043	Corporate Headquarters
Towson Office	22 West Pennsylvania Avenue Suite 102 Baltimore, MD 21204	Regional Banking Office
Annapolis Office	1997 Annapolis Exchange Pkwy Suite 140 Annapolis, MD 21401	Regional Banking Office and Regional Mortgage Banking Office
Columbia Mortgage Office	8820 Columbia 100 Parkway Columbia, MD 21045	Regional Mortgage Banking Office
Timonium Mortgage Office	1954 Greenspring Drive Suite 165 Timonium, MD 21093	Regional Mortgage Banking Office
Dundalk	1301 Merritt Blvd. Dundalk, MD 21222	Deposit Operation Services

Parkville (1) (2)	2028 E. Joppa Road Parkville, MD 21234	Loan Operation Services

(1) The premise is owned, but subject to a ground lease.

Item 3. Legal Proceedings

From time to time, we may be involved in litigation relating to claims arising out of our normal course of business. As of the date of this report, we are not aware of any material pending litigation matters.

Item 4. Mine Safety Disclosures

Not applicable

Part II

Item 5. Market for the Registrant's Common Equity, Related Stockholder Matters and Issuer Purchase of Equity Securities

Our common stock is listed on The NASDAQ Stock Market under the symbol "HBMD."

The following table reflects the high and low sale prices for the periods presented. Quotations are based on NASDAQ listings and reflect inter-dealer prices, without retail mark-up, mark-down or commission and may not represent actual transactions.

	2015		2014	
	Stock price range		Stock price range	
Quarter	High	Low	High	Low
First	$ 14.90	$ 10.75	$ 19.99	$ 9.25
Second	14.75	12.01	11.30	9.50
Third	15.15	13.03	11.20	9.25
Fourth	14.90	12.51	12.00	9.84

At February 29, 2016, we had 470 stockholders of record.

Dividends

We have not paid any dividends on our common stock since our inception and we presently do not intend to pay any dividends in the foreseeable future. We expect that we will retain all earnings, if any, for operating capital. Our ability to pay dividends is dependent upon, among other things, restrictions imposed by the reserve and capital requirements of Maryland and federal law and regulations, our income and financial condition, tax considerations, and general business conditions. In addition, there are restrictions on our ability to pay dividends on our common stock if we are in arrears in the required dividend payment on our Series AA Preferred Stock.

Item 6. Selected Financial Data

	Year ended December 31,				
(in thousands, except per share data.)	2015	2014	2013	2012	2011
Statements of Operations data:					
Interest income	$33,349	$23,360	$17,711	$15,537	$14,640
Interest expense	3,072	2,402	1,901	2,005	2,017
Provision for credit losses	1,836	3,255	950	718	1,164
Noninterest income	11,927	23,256	1,324	768	1,137
Noninterest expense	38,253	23,694	13,239	10,823	10,148
Federal and state income tax expense	973	6,853	984	1,138	1,063
Net income	1,142	10,412	1,961	1,621	1,385
Dividends	126	126	165	616	451
Net income (loss) available to common shareholder	1,016	10,286	1,796	1,005	934
Per share data and shares outstanding:					
Net income per common share, basic	$0.16	$2.53	$0.44	$0.31	$0.35
Net income per common share, diluted	$0.16	$2.48	$0.44	$0.31	$0.35
Book value per common share at period end	$11.54	$11.36	$8.80	$8.45	$9.12
Average common shares outstanding	6,160,005	4,073,077	4,036,291	3,269,835	2,638,443
Diluted average common shares outstanding	6,261,561	4,154,280	4,076,470	3,269,835	2,638,443
Shares outstanding at period end	6,962,139	4,145,547	4,095,650	4,040,471	2,640,264
Financial Condition data:					
Total assets	$946,759	$691,416	$499,918	$401,675	$323,082
Loans receivable (gross)	760,002	552,917	403,875	322,218	276,531
Allowance for credit losses	4,869	3,602	2,506	2,764	3,433
Other interest-earning assets	135,137	99,261	60,481	38,972	15,614
Total deposits	747,408	554,039	388,949	314,858	262,642
Borrowings	98,828	67,628	61,658	38,987	22,984
Total stockholders’ equity	92,899	59,643	48,624	46,721	36,630
Common equity	80,337	47,081	36,062	34,159	24,068
Average assets	782,441	557,602	428,961	356,355	306,567
Average stockholders' equity	76,143	50,674	47,717	41,338	31,749
Average common stockholders' equity	63,581	38,112	35,155	28,776	23,737
Selected performance ratios:					
Return on average assets	0.15 %	1.87 %	0.46 %	0.45 %	0.45 %
Return on average common equity	1.80 %	27.32 %	5.58 %	5.63 %	5.83 %
Net interest margin[(1)]	4.08 %	3.97 %	3.93 %	3.98 %	4.37 %
Efficiency ratio[(2)]	90.64 %	53.59 %	77.27 %	75.69 %	73.75 %
Asset quality ratios:					
Nonperforming loans to gross loans	1.36 %	0.77 %	0.79 %	0.75 %	2.13 %

Allowance for credit losses to loans	0.64	%	0.65	%	0.62	%	0.86	%	1.24	%
Allowance for credit losses to nonperforming loans	46.95	%	84.69	%	78.76	%	115.12	%	58.40	%
Nonperforming assets to loans and other real estate	1.67	%	1.21	%	1.37	%	1.63	%	2.79	%
Nonperforming assets to total assets	1.35	%	0.97	%	1.11	%	1.32	%	2.40	%
Capital ratios:										
Leverage ratio	9.90	%	8.60	%	9.93	%	12.34	%	11.52	%
Tier I risk-based capital ratio	11.47	%	10.11	%	11.45	%	14.18	%	13.14	%
Total risk-based capital ratio	12.09	%	10.73	%	12.05	%	15.02	%	14.36	%
Average equity to average assets	9.73	%	9.09	%	11.12	%	11.60	%	10.36	%

(1) Net interest margin is net interest income divided by average earning assets.

(2) Efficiency ratio is noninterest expense divided by the sum of net interest income and noninterest income.

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

This section is intended to help current and potential investors understand our financial performance through a discussion of the factors affecting our consolidated financial condition at December 31, 2015 and 2014 and our consolidated results of operations for the years ended December 31, 2015, 2014 and 2013. This section should be read in conjunction with the Consolidated Financial Statements and notes to the consolidated financial statements that appear elsewhere in this report.

Overview

Howard Bancorp, Inc. is the holding company for Howard Bank. Howard Bank is a trust company chartered under Subtitle 2 of Title 3 of the Financial Institutions Article of the Annotated Code of Maryland. The Bank was formed in March 2004 and commenced banking operations on August 9, 2004. Howard Bank does not exercise trust powers, and our regulatory structure is the same as a Maryland-chartered commercial bank. As such, our business has consisted primarily of originating both commercial and real estate loans secured by property in our market area. Typically, commercial real estate and business loans involve a higher degree of risk and carry a higher yield than one-to four-family residential loans. Although we plan to continue to focus on commercial customers, we intend to increase our originations of one- to four-family residential mortgage loans going forward, increasing our portfolio of mortgage lending and also selling select loans into the secondary markets.

We are headquartered in Ellicott City, Maryland and we consider our primary market area to be The Greater Baltimore Metropolitan Area. We engage in a general commercial banking business, making various types of loans and accepting deposits. We market our financial services to small to medium sized businesses and their owners, professionals and executives, and high-net-worth individuals. Our loans are primarily funded by core deposits of customers in our market.

Our core business strategy is to deliver superior customer service that is supported by an extremely high level of banking sophistication. Our specialized community banking focus on both local markets and small business related market segments is combined with a broad array of products, new technology and seasoned banking professionals which positions the Bank differently than most competitors. Our experienced executives establish a relationship with each client and bring value to all phases of a client's business and personal banking needs.

Our results of operations depend mainly on our net interest income, which is the difference between the interest income we earn on our loan and investment portfolios and the interest expense we pay on deposits and borrowings. Results of operations are also affected by provisions for credit losses, noninterest income and noninterest expense. Our noninterest expense consists primarily of compensation and employee benefits, as well as office occupancy,

deposit insurance and general administrative and data processing expenses. Our operations are significantly affected by general economic and competitive conditions, particularly with respect to changes in interest rates, government policies and actions of regulatory authorities. Future changes in applicable laws, regulations or government policies may materially affect our financial condition and results of operations.

In August 2014 Howard Bank purchased from NBRS Financial Bank its branch located at 800 Revolution Street, Havre de Grace, Maryland. Pursuant to the branch purchase, Howard Bank acquired $16.1 million in loans and $18.7 million in deposits. In connection with its purchase of the branch, Howard Bank made a net cash payment of $2.4 million, including a premium of approximately $384,000. This transaction was recorded as an asset acquisition rather than as a business combination.

In October 2014 Howard Bank acquired the assets and deposits of a failed institution from the FDIC with branch locations in Harford and Cecil Counties in Maryland and Lancaster County in Pennsylvania. This added $135.6 million in assets and generated a bargain purchase gain of $16.1 million before tax and expanded our geographic reach.

As discussed in “Item 1. Business—Recent Developments,” on June 2, 2015, we sold 2,173,913 shares of our common stock for an aggregate of $25 million to certain institutional accredited investors in a private placement offering.

Also as discussed in “Item 1. Business—Recent Developments,” on August 28, 2015, we completed our acquisition of Patapsco Bancorp, the parent company of The Patapsco Bank, through the merger of Patapsco Bancorp with and into the Company, immediately followed by the merger of Patapsco Bank with and into the Bank. The merger was consummated pursuant to the Agreement and Plan of Merger dated as of March 2, 2015, as amended, by and between the Company and Patapsco Bancorp.

For the year ended December 31, 2015, we reported net income of $1.1 million compared to net income of $10.4 million in 2014. The primary reason for this dramatic decrease in earnings was that 2014 included a $16.1 million pretax bargain purchase gain on the FDIC-assisted acquisition of NBRS reflected in noninterest income in the fourth quarter of 2014, while 2015 included over $4.0 million in merger-related expenses incurred in connection with the Patapsco Bancorp acquisition. Please see Note 2 to the consolidated financial statements for additional details of merger-related activities. Resulting primarily from our balance sheet growth, net interest income for 2015 was $30.3 million, representing an increase of $9.3 million, or 44%, compared to the $21.0 million recorded for 2014. Partially offsetting the increase in net interest income were an increase in noninterest expenses and a decrease in noninterest income as a result of the impact of the bargain purchase gain in 2014. Total noninterest expenses were $38.3 million for 2015 compared to $23.7 million for 2014, an increase of $14.6 million, or 62%. These include merger and restructuring charges of over $4.3 million for 2015 versus only $455 thousand for 2014.

Our nonperforming assets totaled $12.7 million, or 1.35% of total assets, at December 31, 2015, compared to $6.7 million, or 0.97% of total assets, at December 31, 2014 and $5.6 million, or 1.11% of total assets, at December 31, 2013. We had loans totaling $1.8 million delinquent more than 90 days and still accruing at December 31, 2015 compared to $1.2 million of such delinquencies at December 31, 2014. In addition, we provided $1.8 million for credit losses for the year ended December 31, 2015 compared to $3.3 million for credit losses during the year ended December 31, 2014 and $950 thousand during the year ended December 31, 2013. The 2015 provision was for the most part reflective of the overall growth experienced in our loan portfolio. 2014 included a nearly $2.0 million provision due to a loan loss incurred on one commercial customer.

Critical Accounting Policies

Our accounting and financial reporting policies conform to the accounting principles generally accepted in the United States of America ("GAAP") and general practice within the banking industry. Accordingly, preparation of the financial statements require management to exercise significant judgment or discretion and make significant assumptions and estimates based on the information available that have, or could have, a material impact on the carrying value of certain assets or on income. These estimates and assumptions affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of income and expenses during the periods presented. In reviewing and understanding financial information for us, you are encouraged to read and understand the significant accounting policies used in preparing our financial statements. The accounting policies we view as critical are those relating to the allowance for credit losses, income taxes and share based compensation.

Allowance for credit losses

The allowance for credit losses is established through a provision for credit losses charged against income. Loans are charged against the allowance for credit losses when management believes that the collectability of the principal is unlikely. Subsequent recoveries are added to the allowance. The allowance is an amount that represents the amount of probable and reasonably estimable known and inherent losses in the loan portfolio, based on evaluations of the collectability of loans. The evaluations take into consideration such factors as changes in the types and amount of loans in the loan portfolio, historical loss experience, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral, estimated losses relating to specifically identified loans, and current economic conditions. This evaluation is inherently subjective as it requires material estimates including, among others, exposure at default, the amount and timing of expected future cash flows on impaired loans, value of collateral, estimated losses on our loan portfolios as well as consideration of general loss experience. Based on our estimate of the level of allowance for credit losses required, we record a provision for credit losses to maintain the allowance for credit losses at an appropriate level.

We cannot predict with certainty the amount of loan charge-offs that we will incur. We do not currently determine a range of loss with respect to the allowance for credit losses. In addition, our regulatory agencies, as an integral part of

their examination processes, periodically review our allowance for credit losses. Such agencies may require that we recognize additions to the allowance for credit losses based on their judgments about information available to them at the time of their examination. To the extent that actual outcomes differ from management's estimates, additional provisions to the allowance for credit losses may be required that would adversely impact earnings in future periods.

Goodwill and Other Intangible Assets

Goodwill represents the excess of the purchase price over the sum of the estimated fair values of tangible and identifiable intangible assets acquired less the estimated fair value of the liabilities assumed. Core deposit intangibles represent the estimated value of long-term deposit relationships acquired in a business combination. The core deposit intangible is amortized over the estimated useful lives of the acquired long-term deposits acquired, and the remaining amounts of the core deposit intangible are periodically reviewed for reasonableness.

Goodwill has an indefinite useful life and is evaluated for impairment annually or more frequently if events and circumstances indicate that the asset might be impaired. An impairment loss is recognized to the extent that the carrying amount exceeds the asset's fair value. The goodwill impairment analysis is a two-step test. The first step, used to identify potential impairment, involves comparing the reporting unit's estimated fair value to its carrying value, including goodwill. If the estimated fair value of a reporting unit exceeds its carrying value, goodwill assigned to that reporting unit is considered not to be impaired. If the carrying value exceeds estimated fair value, there is an indication of potential impairment and the second step is performed to measure the amount of impairment of goodwill assigned to that reporting unit.

If required, the second step involves calculating an implied fair value of goodwill for each reporting unit for which the first step indicated impairment. The implied fair value of goodwill is determined in a manner similar to the amount of goodwill calculated in a business combination, by measuring the excess of the estimated fair value of the reporting unit, as determined in the first step, over the aggregate estimated fair values of the individual assets, liabilities and identifiable intangibles as if the reporting unit was being acquired in a business combination. If the implied fair value of goodwill exceeds the carrying value of goodwill assigned to the reporting unit, there is no impairment. If the carrying value of goodwill assigned to a reporting unit exceeds the implied fair value of the goodwill, an impairment charge is recorded for the excess. An impairment loss cannot exceed the carrying value of goodwill assigned to a reporting unit, and the loss establishes a new basis in the goodwill. Subsequent reversal of goodwill impairment losses is not permitted. We have determined that Howard Bancorp has one reporting unit.

We may engage an external valuation specialist to assist us in the goodwill assessment, which we anticipate will be performed as of September 30th each year, which would be our annual test date.

Business Combinations

GAAP requires that the acquisition method of accounting, formerly referred to as purchase method, be used for all business combinations and that an acquirer be identified for each business combination. Under GAAP, the acquirer is the entity that obtains control of one or more businesses in the business combination, and the acquisition date is the date the acquirer achieves control. GAAP requires that the acquirer recognize the fair value of assets acquired, liabilities assumed, and any non-controlling interest in the acquired entity at the acquisition date.

Income taxes

We account for income taxes under the asset/liability method. We recognize deferred tax assets for the future consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases, as well as operating loss and tax credit carry-forwards. We measure deferred tax assets and liabilities using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. We recognize the effect on deferred tax assets and liabilities of a change in tax rates in income in the period indicated by the enactment date. We establish a valuation allowance for deferred tax assets when, in the judgment of management, it is more likely than not that such deferred tax assets will not become realizable. The judgment about the level of future taxable income is dependent to a great extent on matters that may, at least in part, be beyond our control. It is at least reasonably possible that management’s judgment about the need for a valuation allowance for deferred tax assets could change in the near term.

Share based compensation

We follow the provisions of ASC Topic 718 “Compensation – Stock Compensation” which requires the expense recognition over the respective service period for the fair value of share based compensation awards, such as stock options, restricted stock, and performance based shares. This standard allows management to establish modeling assumptions as to expected stock price volatility, option terms, forfeiture rates and dividend rates which directly impact estimated fair value. The accounting standard also allows for the use of alternative option pricing models which may impact fair value as determined. Our practice is to utilize reasonable and supportable assumptions which are reviewed with the appropriate board Committee.

Balance Sheet Analysis and Comparison of Financial Condition

A comparison between December 31, 2015 and December 31, 2014 balance sheets is presented below.

Assets

Total assets increased $255.3 million, or 36.9%, to $946.8 million at December 31, 2015 compared to $691.4 million at December 31, 2014. This increase in assets includes $170 million in assets associated with the Patapsco Bancorp acquisition. Complementing this acquired growth, the Bank had organic growth of total assets of $86 million and organic loan growth of $55 million during 2015. The primary source of funding for the asset growth was an increase in deposit levels. Customer deposits increased from $554.0 million at December 31, 2014 to $747.4 million at December 31, 2015, an increase of $193.4 million or 34.9%, of which $170 million, or 31% growth, is attributable to the Patapsco Bancorp transaction, and $24 million, or 4%, is attributable to organic growth. Supplementing the deposit growth, borrowed funds increased by $31.2 million or 46.1% during 2015. In addition, our total capital levels increased $32.3 million or 55.8% year over year, primarily due to the proceeds of $25 million additional capital from the private placement offering in 2015.

Securities Available for Sale

We currently hold U.S. agency securities, mortgage backed securities, stock in another small financial institution and mutual fund investments in our securities portfolio, all of which are categorized as available for sale. The investment in a mutual fund is a supplement to our community reinvestment program activities. We use our securities portfolio to provide the required collateral for funding via commercial customer repurchase agreements as well as to provide sufficient liquidity to fund our loans and provide funds for withdrawals of deposited funds. At December 31, 2015 and December 31, 2014 we held an investment in stock of the FHLB of $4.2 million and $2.6 million, respectively. This investment is required for continued FHLB membership and is based partially upon the amount of borrowings outstanding from the FHLB. These investments are carried at cost.

The following table sets forth the composition of our investment securities portfolio at the dates indicated.

	December 31,					
(in thousands)	2015		2014		2013	
	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
U.S. Government Agencies	$48,467	$ 48,422	$37,010	$ 36,981	$28,522	$ 28,521
Treasuries	-	-	4,000	3,997	-	-
Mortgage-backed	54	57	95	101	157	167
Other investments	1,100	1,094	-	-	-	
	$49,621	$ 49,573	$41,105	$ 41,079	$28,679	$ 28,688

We had securities available for sale of $49.6 million and $41.1 million at December 31, 2015 and December 31, 2014, respectively, which were recorded at fair value. This represents an increase of $8.5 million, or 20.1%, for the year ended December, 2015 from the prior year end. We did not record any gains or losses on the sales or calls of securities in 2015, even though we did liquidate the entire investment portfolio acquired in the Patapsco Bancorp acquisition, because we sold the securities in the acquired portfolio within days of the closing of the transaction. In the fourth quarter of 2014, the Bank both acquired and sold nearly $31.7 million in securities associated with NBRS, which resulted in a net loss on the sale of the securities of $228 thousand.

With respect to our portfolio of securities available for sale, the portfolio contained 19 securities with unrealized losses of $51 thousand and 14 securities with an unrealized losses of $32 thousand at December 31, 2015 and 2014, respectively. Changes in the fair value of these securities resulted primarily from interest rate fluctuations. We do not intend to sell these securities nor is it more likely than not that we would be required to sell these securities before their anticipated recovery, and we believe the collection of the investment and related interest is probable. Based on this analysis, we do not consider any of the unrealized losses to be other than temporary impairment losses.

Portfolio Maturities and Yields

The composition and maturities of the investment securities portfolio (with respect to those securities that have a fixed maturity date) at December 31, 2015 is summarized in the following table. Maturities are based on the final contractual payment dates, and do not reflect the impact of prepayments or early redemptions that may occur.

	As of December 31, 2015											
(in thousands)	One year or less		After one through five years		After five through ten years		After ten years		Total			
	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield		
U.S. Government Agencies	$43,465	0.28 %	$5,002	0.91 %	$-	- %	$-	- %	$48,467	0.34 %		
Mortgage-backed	-	-	-	-	54	4.82	-	-	54	4.82		
	$43,465	0.28 %	$5,002	0.91 %	$54	4.82 %	$-	- %	$48,521	0.35 %		

Loan and Lease Portfolio

Total loans and leases increased by $207.1 million or 37.5%, to $760.0 million at December 31, 2015 from $552.9 million at December 31, 2014. Included in loans and leases at December 31, 2015 is $152 million in loans associated with the Patapsco Bancorp acquisition. At December 31, 2015, total loans were 80.3% of total assets compared to 80.0% of total assets at December 31, 2014. The composition of loans acquired in the Patapsco Bancorp acquisition consisted of the following at December 31, 2015:

- $4 million in construction and land.
- $79 million in residential first lien.
- $4 million in residential junior lien.
- $37 million in commercial real estate.
- $27 million in commercial and industrial.
- $1 million in consumer credit.

The following table sets forth the composition of our loan portfolio at the dates indicated. In addition to the loans we hold in our portfolio, we had loans held for sale of $49.7 million at December 31, 2015 and $42.9 million at December 31, 2014.

(dollars in thousands)	December 31, 2015		2014		2013		2012		2011	
	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percen
Real Estate										
Construction and land	$69,385	9.1 %	$64,158	11.6 %	$50,884	12.6 %	$37,963	11.8 %	$39,268	14.2
Residential - first lien	182,988	24.1	88,293	16.0	39,249	9.7	29,826	9.3	22,087	8.0
Residential - junior lien	27,477	3.6	19,301	3.5	8,266	2.0	7,983	2.5	9,242	3.3
Total residential real estate	210,465	27.7	107,594	19.5	47,515	11.7	37,809	11.7	31,329	11.3
Commercial - owner occupied	131,114	17.3	112,826	20.4	90,333	22.4	61,119	19.0	46,588	16.8
Commercial - non-owner occupied	181,361	23.9	123,958	22.4	113,559	28.1	96,223	29.9	76,880	27.8
Total commercial real estate	312,475	41.1	236,784	42.8	203,892	50.5	157,342	48.8	123,468	44.6
Total real estate loans	592,325	77.9	408,536	73.9	302,291	74.8	233,114	72.3	194,065	70.2
Commercial loans and leases	163,424	21.4	139,669	25.2	100,410	24.9	87,844	27.3	81,243	29.4
Consumer loans	4,253	0.6	4,712	0.9	1,174	0.3	1,260	0.4	1,223	0.4
Total loans and leases	$760,002	100.0%	$552,917	100.0%	$403,875	100.0%	$322,218	100.0%	$276,531	100.0

We have historically focused primarily on lending to businesses for commercial financing as well as commercial real estate lending. Our business model has always been to focus on the needs of small to mid-sized businesses and their owners. While this focus continues, with the commencement of our mortgage banking activities in 2014, we expect to see continued growth in our residential real estate lending.

Loan Portfolio Maturities

The following table summarizes the scheduled repayments of our loan portfolio and sets forth the scheduled repayments of fixed and adjustable rate loans in our portfolio at December 31, 2015.

	As of December 31, 2015			
(dollars in thousands)	One year or less	After one through five years	After five years	Total
Real Estate				
Construction and land	$23,828	$ 34,282	$ 11,275	$69,385
Residential - first lien	861	6,028	176,099	182,988
Residential - junior lien	15	2,432	25,030	27,477
Total residential real estate	876	8,460	201,129	210,465
Commercial - owner occupied	9,914	79,564	41,636	131,114
Commercial - non-owner occupied	18,340	105,216	57,805	181,361
Total commercial real estate	28,254	184,780	99,441	312,475
Total real estate loans	52,958	227,522	311,845	592,325
Commercial loans and leases	21,137	68,631	73,656	163,424
Consumer loans	564	1,432	2,257	4,253
Total	$74,659	$ 297,585	$ 387,758	$760,002
Rate terms:				
Fixed rate	$37,970	$ 227,209	$ 176,856	$442,035
Adjustable rate	36,689	70,376	210,902	317,967
Total	$74,659	$ 297,585	$ 387,758	$760,002

Deposits

We accept deposits primarily from the areas in which our branches and offices are located. We have consistently focused on building broader customer relationships and targeting small business customers to increase our core deposits. We also rely on our customer service to attract and retain deposits. We offer a variety of deposit accounts with a range of interest rates and terms. Customer deposits have historically provided us with a sizeable source of relatively stable and low-cost funds to support asset growth. Our deposit accounts consist of commercial and retail checking accounts, savings accounts, certificates of deposit, money market accounts, and individual retirement accounts. We do not currently accept brokered deposits other than those obtained under Promontory Interfinancial Network's certificate of deposit account registry service ("CDARS") program.

We review and update interest rates paid, maturity terms, service fees and withdrawal penalties on a periodic basis. Deposit rates and terms are based primarily on current operating strategies and market interest rates, liquidity requirements, anticipated short term loan demand and our deposit growth goals.

Our deposits increased from $554.0 million at December 31, 2014 to $747.4 million at December 31, 2015, an increase of $193.4 million or 34.9%. As detailed in the table below, all categories of deposits reflected growth in 2015. Included in the 2015 deposits figure are $170 million in deposits associated with the Patapsco Bancorp acquisition, which consisted of the following at December 31, 2015:

- $22 million in noninterest-bearing demand accounts.
- $10 million in interest-bearing demand accounts.
- $75 million in money market accounts.
- $18 million in saving accounts.
- $45 million in certificate of deposit accounts.

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The following table sets forth the distribution of total deposit accounts, by account type, at the dates indicated

(dollars in thousands)	December 31, 2015			2014			2013		
	Amount	% of Total	Weighted Average Rate	Amount	% of Total	Weighted Average Rate	Amount	% of Total	Weighted Average Rate
Noninterest-bearing demand	$173,689	23 %	- %	$142,727	26 %	- %	$89,759	23 %	- %
Interest-bearing checking	54,014	7	0.21	49,988	9	0.24	31,443	8	0.27
Money market accounts	230,661	31	0.47	140,426	25	0.47	96,365	25	0.40
Savings	51,989	7	0.18	31,354	6	0.19	12,496	3	0.34
Certificates of deposit $100,000 and over	142,599	19	-	108,904	19	1.20	110,516	29	1.20
Certificates of deposit under $100,000	94,456	13	-	80,640	15	0.52	48,370	12	0.72
Total deposits	$747,408	100 %	0.55 %	$554,039	100 %	0.61 %	$388,949	100 %	0.67 %

As of December 31, 2015 and 2014, the aggregate amount of outstanding certificates of deposit in amounts greater than or equal to $100,000 was $142.6 million and $108.9 million, respectively. The following table sets forth the maturity of those certificates at December 31, 2015

(in thousands)	
Three months or less	$36,906
Over three to six months	39,697
Over six to twelve months	27,102
Over twelve months	38,894
	$142,599

Borrowings

Customer deposits remain the primary source we utilize to meet funding needs, but we supplement this with short-term and long-term borrowings. Borrowings consist of overnight unsecured master notes, overnight securities sold under agreement to repurchase (“repurchase agreements”), FHLB advances, and a junior subordinated debenture assumed in the Patapsco Bancorp acquisition.

As a part of the Patapsco Bancorp acquisition, Howard Bancorp assumed debt originally issued by Patapsco Bancorp. In 2005 Patapsco Statutory Trust I, a Connecticut statutory business trust and an unconsolidated wholly-owned

subsidiary of Patapsco Bancorp and now of the Company, issued $5 million of capital trust pass-through securities to investors. The interest rate currently adjusts on a quarterly basis at the rate of the three month LIBOR plus 1.48%. Patapsco Statutory Trust I purchased $5,155,000 of junior subordinated deferrable interest debentures from Patapsco Bancorp. The debentures are the sole asset of the Trust. Patapsco Bancorp also fully and unconditionally guaranteed the obligations of the Trust under the capital securities, which guarantee became an obligation of the Company upon our acquisition of Patapsco Bancorp. The capital securities are redeemable by the Company at par. The capital securities must be redeemed upon final maturity of the subordinated debentures on December 31, 2035.

Our borrowings totaled $98.8 million at December 31, 2015 and $67.6 million at December 31, 2014. Short-term borrowings are summarized in the following table:

	December 31,					
	2015		2014		2013	
(dollars in thousands)	Amount	Rate	Amount	Rate	Amount	Rate
Securities Sold Under Agreement to Repurchase & Master Notes						
At period end	$16,621	0.12%	$24,628	0.12%	$21,658	0.12%
Average for the year	$19,434	0.12%	$17,142	0.12%	$15,697	0.27%
Maximum month-end balance	$23,694		$24,628		$24,644	
Federal Funds Purchased and Short-term Borrowed Funds						
At period end	$52,500	0.55%	$24,000	0.26%	$24,000	0.43%
Average for the year	$27,459	0.47%	$22,184	0.38%	$12,762	0.57%
Maximum month-end balance	$52,500		$31,000		$24,000	

Short-term borrowing totaled $69.1 million at December 31, 2015 and $48.6 million at December 31, 2014. Securities sold under agreements to repurchase, totaling $15.7 million at December 21, 2015, consist of overnight electronic sweep products that move customer excess funds from non-interest bearing deposit accounts to an interest bearing repurchase agreement, which is considered a borrowing. Master notes, totaling $0.9 million at December 31, 2015, similarly sweep funds from the Bank's customer accounts to the Company but do not require pledged collateral. Repurchase agreements sweep funds within the Bank and are secured primarily by pledges of U.S. Government Agency securities, based upon their fair value, as collateral for 100% of the principal and accrued interest of its repurchase agreements. At December 31, 2015 advances under borrowing from the FHLB consisted of ten short-term advances outstanding totaling $52.5 million, of which $17 million were federal funds purchased. At December 31, 2014 we had seven advances outstanding totaling $24.0 million, of which $11 million were federal funds purchased.

Total Shareholders' Equity

Total shareholders' equity increased by $33.3 million or 55.8% from $59.6 million at December 31, 2014 to $92.9 million at December 31, 2015. The increase in shareholders' equity is primarily the result of the proceeds from our private placement of 2,173,913 shares of common stock in June 2015, which added over $23.1 million to equity, and the Patapsco Bancorp acquisition pursuant to which we issued 560,891 shares of common stock representing additional common equity of over $8.0 million. Total shareholders' equity at December 31, 2015 represents a capital to asset ratio of 9.8%, while the total shareholders' equity at December 31, 2014 represents a capital to asset ratio of 8.6%.

Average Balance and Yields

The following tables set forth average balance sheets, average yields and costs, and certain other information for the periods indicated. No tax-equivalent yield adjustments were made, as the effect thereof was not material. All average balances are daily average balances. Non-accrual loans were included in the computation of average balances, and have been reflected in the table as loans carrying a zero yield. The yields set forth below include the effect of deferred fees, discounts and premiums that are amortized or accreted to interest income or expense.

	December 31, 2015			2014			2013		
(dollars in thousands)	Average Balance	Income / Expense	Yield / Rate	Average Balance	Income / Expense	Yield / Rate	Average Balance	Income / Expense	Yield / Rate
Earning assets									
Loans and leases: [1]									
Commercial loans and leases	$145,697	$7,128	4.89 %	$108,151	$5,173	4.78 %	$92,595	$4,532	4.89
Commercial real estate	269,412	14,422	5.35	211,674	10,773	5.09	179,023	8,834	4.93
Construction and land	65,508	3,121	4.76	58,889	2,947	5.00	44,276	2,284	5.16
Residential real estate	144,743	6,382	4.41	70,025	3,141	4.49	40,664	1,838	4.52
Consumer	4,257	258	6.07	1,778	142	7.97	1,097	59	5.33
Total loans and leases	629,617	31,311	4.97	450,517	22,176	4.92	357,655	17,546	4.91
Loans held for sale [2]	47,691	1,706	3.58	23,711	880	3.71	958	33	3.44
Federal funds sold	24,365	63	0.26	25,914	54	0.21	25,338	54	0.21
Securities: [2]									
U.S. Treasury	2,071	12	0.58	1,074	-		-	-	
U.S Gov agencies	33,989	117	0.34	20,198	20	0.10	16,725	26	0.16
Mortgage-backed	1,275	3	0.26	4,408	133	3.02	245	11	4.56
Other investments	3,534	137	3.89	2,499	97	3.88	1,825	40	2.20
Total securities	40,869	269	0.66	28,179	250	0.89	18,795	78	0.41
Total earning assets	742,542	33,349	4.49	528,321	23,360	4.42	402,747	17,711	4.40
Cash and due from banks	7,342			6,231			4,861		
Bank premises and equipment, net	16,145			11,466			9,855		
Other assets	20,329			16,391			14,484		
Less: allowance for credit losses	(3,917)			(4,807)			(2,986)		
Total assets	$782,441			$557,602			$428,961		
Interest-bearing liabilities									
Deposits:									
Interest-bearing demand accounts	$48,465	101	0.21 %	$35,065	$83	0.24 %	$25,866	$69	0.27

Money market	172,492	807	0.47	116,010	550	0.47	81,345	327	0.40
Savings	40,369	73	0.18	16,535	31	0.19	12,270	42	0.34
Time deposits	215,846	1,630	0.75	172,436	1,415	0.82	129,082	1,218	0.94
Total interest-bearing deposits	477,172	2,611	0.55	340,046	2,079	0.61	248,563	1,656	0.67
Short-term borrowings	47,893	154	0.32	39,326	106	0.27	28,459	114	0.40
Long-term borrowings	22,881	307	1.34	19,927	217	1.09	16,521	131	0.79
Total interest-bearing funds	547,946	3,072	0.56	399,299	2,402	0.60	293,543	1,901	0.65
Noninterest-bearing deposits	150,848			105,361			86,727		
Other liabilities and accrued expenses	7,505			2,268			974		
Total liabilities	706,299			506,928			381,244		
Shareholders' equity	76,142			50,674			47,717		
Total liabilities & shareholders' equity	$782,441			$557,602			$428,961		
Net interest rate spread [3]		$30,277	3.93 %		$20,958	3.82 %		$15,810	3.75 %
Effect of noninterest-bearing funds			0.14			0.15			0.18
Net interest margin on earning assets [4]			4.08 %			3.97 %			3.93 %

(1) Loan fee income is included in the interest income calculation, and non-accrual loans are included in the average loan base upon which the interest rate earned on loans is calculated.

(2) Available for sale securities and loans held for sale are presented at fair value

(3) Net interest rate spread represents the difference between the yield on average interest-earning assets and the cost of average interest-bearing liabilities.

(4) Net interest margin represents net interest income divided by average total interest-earning assets.

Rate/Volume Analysis

The following table presents the effects of changing rates and volumes on our net interest income for the periods indicated. The rate column shows the effects attributable to changes in rate (changes in rate multiplied by prior volume). The volume column shows the effects attributable to changes in volume (changes in volume multiplied by prior rate

	For the year ended December 31,					
	2015 vs. 2014			2014 vs. 2013		
	Due to variances in			Due to variances in		
(in thousands)	Total	Rates	Volumes [1]	Total	Rates	Volumes [1]
Interest earned on:						
Loans and leases:						
Commercial loans and leases	$1,955	$118	$ 1,837	641	$(103)	$ 744
Commercial real estate	3,649	558	3,091	1,940	277	1,663
Construction and land	174	(142)	316	663	(68)	731
Residential real estate	3,241	(53)	3,294	1,303	(14)	1,317
Consumer	116	(34)	150	83	29	54
Loans held for sale	826	(32)	858	847	3	844
Taxable securities	19	(64)	83	172	90	82
Federal funds sold	9	12	(3)	0	(2)	2
Total interest income	9,989	363	9,626	5,649	212	5,437
Interest paid on:						
Savings deposits	42	(1)	43	(10)	(18)	8
Interest bearing checking	18	(10)	28	13	(9)	22
Money market accounts	257	(7)	264	224	59	165
Time deposits	215	(113)	328	197	(139)	336
Short-term borrowings	48	20	28	(8)	(37)	29
Long-term borrowings	90	51	39	85	48	37
Total interest expense	670	(60)	730	501	(96)	597
Net interest earned	$9,319	$423	$ 8,896	$5,148	$308	$ 4,840

(1) Change attributed to mix (rate and volume) are included in volume variance.

Comparison of Results of Operations

A comparison of the results of operations for the years ended December 31, 2015 and December 31, 2014 is presented below.

General

Net income available to common shareholders decreased $9.3 million, to $1.0 million for the year ended December 31, 2015 compared to $10.3 million for the year ended December 31, 2014. The decrease in net income available to common shareholders was primarily due to a $16.1 million pretax bargain purchase gain associated with the NBRS acquisition recorded in 2014, while 2015 was impacted by $4.3 million in merger and restructuring expenses. Positively affecting 2015 versus 2014 net income were increases in net interest income totaling $9.3 million and increased revenues from mortgage banking activities (including gains on sale of loans and loan fee income) of $4.0 million. Offsetting these improvements was a $14.6 million increase in noninterest expenses. Included in noninterest expenses are merger and restructuring expenses that increased to $4.3 million in 2015 from $455 thousand in 2014.

Interest Income

Interest income and fees on loans increased $10.0 million, or 42.8%, to $33.3 million for the year ended December 31, 2015 compared to $23.4 million during the year ended December 31, 2014. The increase was due almost entirely to a $10.0 million, or 43.2%, increase in interest income and fees on loans. The increase in interest income and fees was for the most part a result of an increase in interest income on loans, which was mainly due to a $203.0 million increase in average loans outstanding for 2015 versus 2014. Included is this average loan growth is a $24.0 million increase in the average balance of loans held for sale. The average yield on loans and leases increased to 4.97% from 4.92% year over year, while the average yield on loans held for sale decreased to 3.58% from 3.71% reflective of current residential loan market conditions. In addition, interest income earned on investment securities and other interest earning assets increased $29 thousand primarily as a result of growth in their average balances, partially offset by a decrease in the average yield on investment securities. The average yield on investment securities decreased to 0.66% from 0.89% primarily as a result of changes in the portfolio mix, while the average yield from other earning asset increased to 0.26% from 0.21% year over year.

Interest Expense

Interest expense increased $670 thousand, or 27.9%, to $3.1 million during the year ended December 31, 2015 from $2.4 million during the prior year. Interest expense increased primarily due to an increase in the average balance of interest bearing funds from $399.3 million for 2014 to $547.9 million for 2015, representing a $148.6 million or 37.2% increase in the average balance of interest bearing funds. Interest expense benefitted in 2015 from a $45.5 million, or 43.2%, increase in the average balance of noninterest-bearing deposits, without which we would have had to rely on other sources of funding and interest expense would have been significantly higher. Partially mitigating the increase in interest expense due to the growth in the average balance of interest-bearing funds was a decrease in the overall cost of funds for 2015 versus 2014 of four basis points. In addition, interest expense increased $138 thousand as a result of an $11.5 million increase in the average balance of borrowings and a ten basis point increase in the average rate of short-term and long-term borrowings, which was 0.65% during the year ended December 31, 2015.

Net Interest Income

Net interest income is our largest source of operating revenue. Net interest income is affected by various factors including changes in interest rates and the composition of interest-earning assets and interest-bearing liabilities and maturities. Net interest income is determined by the interest rate spread (i.e., the difference between the yields earned on interest-earning assets and the rates paid on interest-bearing liabilities) and the relative amounts of interest-earning assets and interest-bearing liabilities. Net interest income increased $9.3 million, or 44.5%, during the year ended December 31, 2015 compared to the year ended December 31, 2014. The increase in net interest income was primarily due to an increase in interest income driven by our continued balance sheet growth. As noted above, the increase in net interest income was primarily due to increased interest income of $10.0 million, or 42.8%, year over year, while interest expense increased less than $1 million, even with the sizable growth in deposits and borrowings.

Provision for Credit Losses

We establish a provision for credit losses, which is a charge to earnings, in order to maintain the allowance for credit losses at a level we consider adequate to absorb credit losses incurred in the loan portfolio that are both probable and reasonably estimable at the balance sheet date. In determining the level of the allowance for credit losses, management considers past and current loss experience, evaluations of real estate collateral, current economic conditions, volume and type of lending, adverse situations that may affect a borrower’s ability to repay a loan and the levels of nonperforming loans. The amount of the allowance is based on estimates and actual losses may vary from such estimates as more information becomes available or economic conditions change. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as circumstances change or more information becomes available. The allowance for credit losses is assessed on at least a quarterly basis and provisions are made for credit losses as required in order to maintain the allowance.

Based on management's evaluation of the above factors, we had a provision for credit losses of $1.8 million for 2015 compared to $3.3 million during 2014, a decrease of $1.43 million. The substantial provision for credit losses during the 2014 period resulted primarily from one large commercial customer that closed its business during the third quarter of 2014 and did not fulfill its commitments under existing contracts. The provision for the 2015 period reflects general provisions on loans that are collectively evaluated given the continued growth in the size of our loan portfolio, as well as any specific provisions required on loans that are individually evaluated and deemed to be impaired. One of the Bank's primary measures of asset quality is the ratio of non-accrual loans, troubled debt restructured loans and other real estate owned ("OREO") as a percentage of total assets. This asset quality measure for 2015 was 1.35% at December 31, 2015 compared to 0.97% at the end of 2014, primarily as a result of an increase of $6.1 million in non-performing loans.

Management analyzes the allowance for credit losses as described in the section entitled "Allowance for Credit Losses." The provision that is recorded is sufficient, in management's judgment, to bring the allowance for credit losses to a level that reflects the losses inherent in our loan portfolio relative to loan mix, economic conditions and historical loss experience. Management believes, to the best of its knowledge, that all known losses as of the balance sheet dates have been recorded. However, although management uses the best information available to make determinations with respect to the provisions for credit losses, additional provisions for credit losses may be required to be established in the future should economic or other conditions change substantially. In addition, as an integral part of their examination process, the Maryland Office of the Commissioner of Financial Regulation and the FDIC will periodically review the allowance for credit losses. The Maryland Office of the Commissioner of Financial Regulation and the FDIC may require us to recognize additions to the allowance based on their analysis of information available to them at the time of their examination.

Noninterest Income

Noninterest income was $11.9 million for the year ended December 31, 2015 compared to $23.3 million for the year ended December 31, 2014. The primary reason for the decrease in noninterest income was the bargain purchase gain resulting from the NBRS acquisition totaling $16.1 million recorded in 2014. Excluding this one-time gain, noninterest income increased $4.8 million or 66.4% year over year. Our focus on building a mortgage banking platform commenced in 2014 and continued through 2015. Throughout 2015, our mortgage loan originations increased each quarter, with total loans originated with the intent to sell to secondary investors reaching nearly $600 million for 2015 compared to approximately $300 million in 2014. As a result of the origination and subsequent sales of residential mortgage loans in 2015, revenue derived from mortgage banking activities was $7.0 million for 2015 compared to $4.3 million in 2014. Complementing the gains on sale of mortgage loans was loan fee income derived from mortgage banking processing and underwriting as well as other portfolio loan fees. The loan fees realized in 2015 were $2.9 million compared to $1.6 million for 2014.

Service charges on deposit accounts, which consist of account activity fees such as overdraft fees and other traditional banking fees, increased $176 thousand or 19.5% during 2015. This increase was due mainly to a $100 thousand increase in overdraft or non-sufficient fees as well as a $37 thousand increase in account activity fees due to the growth in deposit accounts.

Noninterest income for 2014 was negatively impacted by a $228 thousand loss on the sale of investment securities. As a part of the acquisition of NBRS in the fourth quarter of 2014, we acquired their investment portfolio, and after a review of the composition of the acquired portfolio, it was determined that the longer term securities held exposed the Company to increased interest rate risk and were not a good fit with the legacy approach toward maintaining a shorter duration portfolio, and we liquidated the portfolio at a $228 thousand loss. Similarly in 2015, we evaluated the Patapsco Bancorp investment portfolio and chose to liquidate the entire portfolio, but did not recognize a gain or loss on the sale of this portfolio in 2015 because we sold the securities we acquired in the Patapsco Bancorp acquisition within days of the closing of the transaction.

Other operating income, which consists mainly of non-depository account fees such as wire, merchant card and ATM services, increased $326 thousand in 2015 compared to the same period of 2014 due to our larger customer base.

Noninterest Expenses

Noninterest expenses increased $14.6 million, or 61.44%, to $38.3 million for the year ended December 31, 2015 compared to $23.7 million for the year ended December 31, 2014. Throughout 2015, the Bank continued to expand into the greater Baltimore market, adding operational staff, facilities and equipment needed to support these initiatives

and these growth-related costs are reflected in the overall increases in various categories of noninterest expense. Merger and restructuring costs associated with the Patapsco Bancorp acquisition as well as system integration costs relating to the late 2014 NBRS acquisition were $4.3 million in 2015 compared to $455 thousand in 2014. For the Patapsco Bancorp acquisition, these costs represent legal and investment banking fees, as well as compensation costs for severance and other payments provided for in employment agreements between Patapsco Bank and its former executive officers. In addition to the Patapsco Bancorp-related costs, we also incurred data processing and conversion-related expenses as we integrated the former NBRS data platform into our systems in April 2015.

Compensation and benefits expenses increases represent our investment in growth initiatives. As we have grown our balance sheet and geographic footprint, we have also increased our business development, customer service and infrastructure staffing to ensure appropriate support levels, risk oversight, information technology platforms, and human resources. Compensation and benefits expenses grew by $3.8 million or 28.0% for 2015 versus 2014. 2015 compensation and benefits reflect the full complement of mortgage banking personnel that generated nearly $600 million in mortgage loans for resale into the secondary market and revenues of $7.0 million and increases in staffing at new locations via acquisitions and support staff. We had 257 full time equivalent employees (FTE) at December 31, 2015 compared to 214 FTE at the end of 2014, representing an increase of 43 FTE or 20%.

Occupancy and equipment related costs increased by $1.4 million or 55.0% during 2015 compared to 2014, primarily as the result of the previously discussed expansion resulting from both organic and acquired growth. We have altered the mix of owned versus leased locations to better manage this expense component and will continue to evaluate facility and branch utilization, efficiencies and opportunities. We plan to open our Little Patuxent branch in Howard County, Maryland in the first quarter of 2017. Along with continued expansion, general increases in the operational and maintenance upkeep we expect to see these costs continue to moderately increase going forward.

Marketing and business development expenses increased to $2.9 million during 2015, representing an increase of $1.2 million or 71.0% from the prior year, in order to support sales and growth initiatives in conjunction with ongoing organic and acquisition growth activities. Approximately $1.6 million of the $2.9 million in marketing and business expenses during 2015 was incurred in connection with mortgage banking activities to generate the higher origination levels achieved.

We recorded a valuation write-down of $736 thousand in 2015 related to OREO properties that we currently hold. No such valuation adjustments were recorded in 2014.

Other operating expenses consists mainly of loan-related expenses (including collection costs associated with non-performing assets) and a variety of general expenses such as telephone and data lines, supplies and postage and courier services. In aggregate, these expenses increased $1.3 million year over year. Supporting our expanding infrastructure increased insurance cost $83 thousand, supplies $142 thousand, phone and data lines $66 thousand, bank security and armor carrier $48 thousand and software licenses and maintenance $480 thousand.

Income Tax Expense

Taking into consideration the above-stated changes in net interest income, the provision for credit losses, and our noninterest income (particularly the bargain purchase gain in 2014) and noninterest expense levels, pretax income decreased by $15.23 million from $17.3 million in 2014 to $2.1 million in 2015.

Income tax expense amounted to $973 thousand for year ended December 31, 2015 and $6.9 million for the year ended December 31, 2014, resulting in effective tax rates of 46.0% and 39.7%, respectively. The effective tax rate is influenced by sources of non-taxable income, such as the income from our BOLI program, and also by certain non-deductible expense items. Certain merger and acquisition cost are deemed not deductible for income tax purposes, which resulted in the high effective tax rate for 2015.

A comparison of the results of operations for the years ended December 31, 2014 and December 31, 2013 is presented below.

General

Net income available to common shareholders increased $8.5 million, or 472.8%, to $10.3 million for the year ended December 31, 2014 compared to of $1.8 million for the year ended December 31, 2013. The increase in net income available to common shareholders was primarily due to a $16.1 million pretax bargain purchase gain associated with the NBRS acquisition, partially offset by increases in non-interest expenses and an increase in the provision for credit losses. For 2014, the dividends paid on preferred stock decreased slightly due to a reduction in the dividend rate in mid-year 2013.

Interest Income

Interest income increased $5.6 million, or 31.9%, to $23.4 million for the year ended December 31, 2014 compared to $17.7 million during the year ended December 31, 2013. The increase was due primarily to a $5.5 million, or 31.2%, increase in interest income on loans. In addition, interest income earned on investment securities increased $172 thousand primarily as a result of balance sheet growth. Income derived from federal funds sold remained unchanged for 2014 versus 2013. The increase in interest income on loans was due to a $92.9 million increase in average loans outstanding for 2014 versus 2013. The yield earned on the loan portfolio remained relatively unchanged, as the average yield on loans was 4.92% for 2014 compared to 4.91% during 2013.

Interest Expense

Interest expense increased $501 thousand, or 26.4%, to $2.4 million during the year ended December 31, 2014 from $1.9 million during the prior year. The interest expense increased primarily due to an increase in average interest bearing funds from $293.5 million for 2013 to $399.3 million for 2014, representing an increase in the average interest bearing funds of $105.7 million or 36%. Mitigating the increase in interest expense due to the growth in funds was a decrease in the overall cost of funds for 2014 versus 2013 of five basis points.

Net Interest Income

Net interest income increased $5.1 million, or 32.6%, during the year ended December 31, 2014 compared to the year ended December 31, 2013. The increase in net interest income was primarily due to an increase in interest income driven by our continued balance sheet growth. As noted above, the increase in net interest income was primarily due to increased interest income of $5.6 million, or 31.9%, year over year, while interest expense increased less than $1 million, even with the sizable growth in deposits and borrowings.

Provision for Credit Losses

Based on management's evaluation of the factors outlined in the comparison of the results of operations for the years ended December 31, 2015 and December 31, 2014, we had a provision for credit losses of $3.3 million for 2014 compared to $1.0 million during 2013, an increase of $2.3 million. The $3.3 million provision during 2014 includes both specific amounts for loans that are individually evaluated for impairment as well as additional general provisions for loans that are collectively evaluated, and are influenced by our continued growth in the size of the loan portfolio. The increased provision for 2014 is a result of the growth in the loan portfolio during 2014 and from one large commercial customer that closed their business during the third quarter of 2014 and notified their customers that any remaining commitments under existing contracts would not be completed. While the Bank is pursuing multiple remedies, management deemed it prudent to absorb the full loss. The ratio of nonperforming loans to gross loans decreased from 0.79% at December 31, 2013 to 0.77% at December 31, 2014. The ratio of non-accrual loans, troubled debt restructured loans and OREO as a percentage of total assets was 0.97% at December 31, 2014 compared to 1.11% at the end of 2013. Even though nonperforming assets increased to $6.7 million at the end of 2014 compared to $5.6 million at December 31, 2013, the ratio of nonperforming assets to total assets declined given the large asset growth encountered during 2014.

Noninterest Income

Noninterest income was $23.3 million for the year ended December 31, 2014 compared to $1.3 million for the year ended December 31, 2013. The two primary reasons for the increase in noninterest income were the bargain purchase gain resulting from the NBRS acquisition and higher mortgage banking revenues due to gains on the sales of residential loans. For further information on the $16.1 million bargain purchase gain see Note 2 to our consolidated financial statements. Our focus on building a mortgage banking platform commenced in late 2013, and continued through the first quarter of 2014. Throughout 2014, our mortgage loan originations increased each quarter, with total loans originated with the intent to sell to secondary investors exceeding $300 million for the year. As a result of the origination and subsequent sales of residential mortgage loans in 2014, revenue derived from mortgage banking activities was $4.3 million for 2014 compared to $215 thousand in 2013. Complementing the gains on sale of mortgage loans were loan fees associated with mortgage banking activities, which are included in loan related income. The loan fees realized in 2014 were $1.5 million compared to less than $100 thousand for 2013.

Service charges on deposit accounts increased $210 thousand or 54.3% during 2014. This increase was due mainly to growth in deposit balances and an increase in overdraft or non-sufficient fees as more customer checks were presented where the funds were insufficient to cover the amount of the check.

The additional amounts under policies added to our BOLI program in December 2013 generated an increase of $95 thousand in income from bank owned life insurance, to $377 thousand during 2014 compared to $282 thousand during 2013.

As discussed above in the comparison of the results of operations for the years ended December 31, 2015 and December 31, 2014, noninterest income for 2014 was also impacted by a $228 thousand loss on the sale of investment securities resulting from our sale of the securities acquired in the NBRS acquisition. We did not sell any investment securities in 2013.

Noninterest Expenses

Noninterest expenses increased $10.5 million, or 79.0%, to $23.7 million for the year ended December 31, 2014 compared to the $13.2 million for the year ended December 31, 2013. Late in 2013 and throughout 2014, the Bank expanded its mortgage banking division, expanded into the greater Baltimore, Harford and Cecil County markets and added operational staff, facilities and equipment needed to support these initiatives, and these growth-related costs are reflected in the overall increases in various categories of noninterest expense. More than half of this increase in expenditures was in compensation and benefits expenses, which increased by $6.0 million or 81.7% for 2014 versus 2013. 2014 compensation and benefits reflect the full complement of mortgage banking personnel that generated over $300 million in mortgage loans for resale into the secondary market and revenues of $4.3 million, increases in staffing from our organic expansion, and additional staff introduced via acquisitions. We had 216 FTE at December 31, 2014 compared to 96 FTE at the end of 2013, representing an increase of 120 FTE or 125%. Compensation costs increased $3.4 million while taxes and benefits increased $2.6 million year over year.

As would be expected given our balance sheet growth and increases in staffing, we have also increased the number of locations that we utilize, and have experienced a sizable increase in our occupancy costs. Occupancy and equipment expenses during 2014 increased $870 thousand or 54.6% from the prior year due to both the incremental costs of operating additional locations as we continue to expand our presence in the markets we serve and minor increases in rental payments for our existing facilities.

Marketing and business development expenses during 2014 increased $922 thousand or 122.7% over the prior year to support sales growth and research initiatives in conjunction with ongoing organic and acquisition growth activities and also our strategic growth initiatives. Approximately $700 thousand of this increase was incurred in connection with mortgage banking activities to generate the origination levels achieved.

Professional fees, which consist primarily of legal, accounting and consulting expenses, increased $618 thousand or 70.0% during 2014 compared to the prior year. This increase was primarily from legal and investment banking fees for the branch acquisition and the FDIC-assisted acquisitions consummated in 2014, as well as ongoing strategic growth initiatives.

Other operating expenses increased $1.8 million during 2014 compared to the prior year, nearly $1.0 million of which was related to the development of the mortgage banking infrastructure and operations. Credit reports and appraisals, which are a component of loan-related expenses, increased by approximately $700 thousand when comparing 2014 to 2013. Most of the remainder of the increase in operating cost was due to the dramatic increase in staff and locations, and the resulting increases in expenses such as telephone and data lines, postage, software and physical security costs.

Nonperforming and Problem Assets

Management performs reviews of all delinquent loans and our loan officers contact customers to attempt to resolve potential credit issues in a timely manner. When in the best interests of Howard Bank and the customer, we will do a troubled debt restructure with respect to a particular loan. When not possible, we seek to aggressively move loans through the legal and foreclosure process within applicable legal constraints.

Loans are placed on non-accrual status when payment of principal or interest is 90 days or more past due and the value of the collateral securing the loan, if any, is less than the outstanding balance of the loan. Loans are also placed on non-accrual status if management has serious doubt about further collectability of principal or interest on the loan, even though the loan is currently performing. When loans are placed on a non-accrual status, unpaid accrued interest is fully reversed, and further income, if any, is recognized only to the extent received. The loan may be returned to accrual status if the loan is brought current, has performed in accordance with the contractual terms for a reasonable period of time and ultimate collectability of the total contractual principal and interest is no longer in doubt.

The table below sets forth the amounts and categories of our nonperforming assets, which consist of non-accrual loans, troubled debt restructurings and OREO (which includes real estate acquired through, or in lieu of, foreclosure), at the dates indicated

	December 31,				
(in thousands)	2015	2014	2013	2012	2011
Non-accrual loans:					
Real estate loans:					
Construction and land	$-	$1,144	$-	$432	$-
Residential - First Lien	693	719	331	442	368
Residential - Junior Lien	63	57	-	-	44
Commercial	1,148	-	258	384	1,988
Commercial and leases	5,935	2,015	2,593	1,143	3,229
Consumer	150	92	-	-	9
Total non-accrual loans	7,989	4,027	3,182	2,401	5,638
Accruing troubled debt restructured loans:					
Real estate loans:					
Construction and land	-	-	-	-	-
Residential - First Lien	301	-	-	-	240
Residential - Junior Lien	-	-	-	-	-
Commercial	2,073	226	-	-	-
Commercial and leases	7	-	-	-	-
Consumer	-	-	-	-	-
Total accruing troubled debt restructured loans	2,381	226	-	-	240
Total non-performing loans	10,370	4,253	3,182	2,401	5,878
Other real estate owned:					
Land	964	595	595	595	595
Commercial	1,405	1,877	1,782	2,130	1,084
Residential	-	-	-	178	206
Total other real estate owned	2,369	2,472	2,377	2,903	1,885
Total non-performing assets	$12,739	$6,725	$5,559	$5,304	$7,763
Ratios:					
Non-performing loans to total gross loans	1.36 %	0.77 %	0.79 %	0.75 %	2.13 %
Non-performing assets to total assets	1.35 %	0.97 %	1.11 %	1.32 %	2.40 %

Of the $8.0 million in non-accrual loans shown for 2015, approximately $5.4 million was from legacy loans, while the additional $2.6 million resulted from acquired loans. The performing (accruing) troubled debt restructured loans (“TDRs”) of $2.4 million are legacy loans and represent only three separate credit relationships.

Included in total non-accrual loans at December 31, 2015 above are two TDRs totaling $744 thousand that were not performing in accordance with their modified terms, and the accrual of interest has ceased. These TDRs consist of one commercial loan and one commercial real estate loan. Loans 90 days or more past due and still accruing interest at December 31, 2015 totaled $1.8 million and consisted of legacy loans totaling $460 thousand and acquired loans

totaling $1.3 million

Interest income that would have been recorded during the year ended December 31, 2015, 2014 and 2013 if non-accrual loans had been current and in accordance with their original terms was $198 thousand, $126 thousand and $116 thousand, respectively. No interest income was recorded on such loans during these periods.

Under GAAP we are required to account for certain loan modifications or restructurings as TDRs. In general, the modification or restructuring of a debt constitutes a TDR if Howard Bank, for economic or legal reasons related to the borrower's financial difficulties, grants a concession, such as a reduction in the effective interest rate, to the borrower that we would not otherwise consider. However, all debt restructurings or loan modifications for a borrower do not necessarily constitute troubled debt restructurings.

Nonperforming assets amounted to $12.7 million or 1.35% of total assets at December 31, 2015 compared to $6.7 million or 0.97% of total assets at December 31, 2014 and $5.6 million or 1.11% of total assets at December 31, 2013. Total nonperforming assets increased by $6.0 million during 2015 due to a $3.9 million increase in non-accrual loans, a $2.2 million increase in current TDRs and a decrease in OREO of $103 thousand. There was one new land loan totaling $625 thousand added to OREO property in 2015. Additionally, the Bank recorded a valuation allowance in non-interest expense totaling $736 thousand on three existing properties held in OREO in 2015.

The composition of our nonperforming loans is further described below:

Non-Accrual Loans:

- Six residential first lien loans totaling $693 thousand, consisting of three acquired from NBRS and one acquired from Patapsco Bank.
- One residential junior lien in the amount of $63 thousand.
- Ten commercial real estate loans totaling $1.1 million, two acquired from NBRS and two from Patapsco Bank. Five of these loans totaling $171 thousand represent one relationship
- 32 commercial loans totaling $5.9 million, consisting of nine acquired loans representing seven relationships and 23 legacy loans representing 11 relationships. Of the 23 legacy loans, four have SBA guarantees, and we expect to receive repayment with respect to the guaranteed amounts once we submit claims to the SBA. Specific reserves of $1.2 million have been taken against two of these loans.
- One consumer loan for $150 thousand. A $75 thousand specific reserve has been recorded against this loan.

Accruing Trouble Debt Restructure Loans:

- One residential first lien for $326 thousand.
- One commercial real estate loan for $2.1 million.
- One commercial loan for $1 thousand.

Other Real Estate Owned

Real estate we acquire as a result of foreclosure is classified as OREO. When property is acquired it is recorded at the lower of cost, which is the unpaid balance of the loan less estimated foreclosure costs, or fair value at the date of foreclosure. If there is a subsequent decline in the value of real estate owned, we provide an additional allowance to reduce real estate acquired through foreclosure to its fair value less estimated disposal costs. Costs relating to holding such real estate are charged against income in the current period while costs relating to improving such real estate are capitalized until a saleable condition is reached up to the property's net realizable value, then such costs would be charged against income in the current period. We had foreclosed real estate of $2.4 million at December 31, 2015, $2.5 million at December 31, 2014 and $2.4 million at December 31, 2013. Foreclosed real estate at December 31, 2015 consisted of two office condominiums in Prince George's County, Maryland, several parcels of unimproved land in Baltimore County, Maryland, a commercial building in Carroll County, Maryland, one commercial building in

Sussex County, Delaware, and several lots of non-residential property in Anne Arundel County, Maryland.

Classification of Loans

Our policies, consistent with regulatory guidelines, provide for the classification of loans and other assets that are considered to be of lesser quality as Substandard, Doubtful, or Loss assets. An asset is considered Substandard if it is inadequately protected by the current net worth and paying capacity of the obligor or by the collateral pledged, if any. Substandard assets include those assets characterized by the distinct possibility that we will sustain some loss if the deficiencies are not corrected. Assets classified as Doubtful have all of the weaknesses inherent in those classified Substandard with the added characteristic that the weaknesses present make collection or liquidation in full, on the basis of currently existing facts, conditions and values, highly questionable and improbable. Assets (or portions of assets) classified as loss are those considered uncollectible and of such little value that their continuance as assets is not warranted. Assets that do not expose us to risk sufficient to warrant classification in one of the aforementioned categories, but which possess potential weaknesses that deserve our close attention, are required to be designated as Special Mention.

We maintain an allowance for credit losses at an amount estimated to equal all credit losses incurred in our loan portfolio that are both probable and reasonable to estimate at a balance sheet date. Our determination as to the classification of our assets is subject to review by the Maryland Commissioner of Financial Regulation and the FDIC. We regularly review our asset portfolio to determine whether any assets require classification in accordance with applicable regulations.

The following table sets forth our amounts of classified loans and criticized loans (classified loans and loans designated as Special Mention) at the dates indicated.

	December 31,		
(in thousands)	2015	2014	2013
Classified loans:			
Substandard	$3,009	$7,037	$3,182
Doubtful	6,496	966	-
Total classified loans	9,505	8,003	3,182
Special mention	614	-	-
Total criticized loans	$10,119	$8,003	$3,182

At December 31, 2015, total classified loans of $10.1 million consisted of non-accrual loans totaling $8.0 million and accruing TDR loans totaling $2.0 million. At December 31, 2014, total classified loans of $8.0 million consisted of non-accrual loans totaling $4.3 million and accruing TDR loans totaling $226 thousand.

Allowance for Credit Losses

We provide for credit losses based upon the consistent application of our documented allowance for credit loss methodology. All credit losses are charged to the allowance for credit losses and all recoveries are credited to it. Additions to the allowance for credit losses are provided by charges to income based on various factors which, in our judgment, deserve current recognition in estimating probable losses. We regularly review the loan portfolio and make provisions for credit losses in order to maintain the allowance for credit losses in accordance with GAAP. The allowance for credit losses consists primarily of two components:

1) Specific allowances are established for loans classified as Substandard or Doubtful. For loans classified as impaired, the allowance is established when the net realizable value (collateral value less costs to sell) of the impaired loan is lower than the carrying amount of the loan. The amount of impairment provided for as a specific allowance is represented by the deficiency, if any, between the underlying collateral value and the carrying value of the loan. Impaired loans for which the estimated fair value of the loan, or the loan's observable market price or the fair value of the underlying collateral, if the loan is collateral dependent, exceeds the carrying value of the loan are not considered in establishing specific allowances for credit losses; and

2) General allowances established for credit losses on a portfolio basis for loans that do not meet the definition of impaired loans. The portfolio is grouped into similar risk characteristics, primarily loan type and regulatory classification. We apply an estimated loss rate to each loan group. The loss rates applied are based upon our loss experience adjusted, as appropriate, for the qualitative factors discussed below. This evaluation is inherently subjective, as it requires material estimates that may be susceptible to significant revisions based upon changes in

economic and real estate market conditions.

The allowance for credit losses is maintained at a level to provide for losses that are probable and can be reasonably estimated. Management's periodic evaluation of the adequacy of the allowance is based on Howard Bank's past credit loss experience, known and inherent losses in the portfolio, adverse situations that may affect the borrower's ability to repay, the estimated value of any underlying collateral, composition of the loan portfolio, current economic conditions and other relevant factors. This evaluation is inherently subjective as it requires material estimates that may be susceptible to significant change, including the amounts and timing of future cash flows expected to be received on impaired loans.

A loan is considered past due or delinquent when a contractual payment is not paid on the day it is due. A loan is considered impaired when, based on current information and events, it is probable that Howard Bank will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record and the amount of the shortfall in relation to the principal and interest owed. The impairment of a loan may be 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, Howard Bank's impairment on such loans is measured by reference to the fair value of the collateral. Interest income on impaired loans is recognized on the cash basis.

Our loan policies state that after all collection efforts have been exhausted, and the loan is deemed to be a loss, then the remaining loan balance will be charged to the established allowance for credit losses. All loans are evaluated for loss potential once it has been determined by the Watch Committee that the likelihood of repayment is in doubt. When a loan is past due for at least 90 days or a deterioration in debt service coverage ratio, guarantor liquidity, or loan-to-value ratio has occurred that would cause concern regarding the likelihood of the full repayment of principal and interest, and the loan is deemed not to be well secured, the loan should be moved to non-accrual status and a specific reserve is established if the net realizable value is less than the principal value of the loan balance(s). Once the actual loss value has been determined a charge-off against the allowance for credit losses for the amount of the loss is taken. Each loss is evaluated on its specific facts regarding the appropriate timing to recognize the loss.

The adjustments to historical loss experience are based on our evaluation of several qualitative factors, including:

- changes in lending policies, procedures, practices or personnel;
- changes in the level and composition of construction portfolio and related risks;
- changes and migration of classified assets;
- changes in exposure to subordinate collateral lien positions;
- levels and composition of existing guarantees on loans by SBA or other agencies;
- changes in national, state and local economic trends and business conditions;
- changes and trends in levels of loan payment delinquencies; and
- any other factors that management considers relevant to the quality or performance of the loan portfolio.

We evaluate the allowance for credit losses based upon the combined total of the specific and general components. Generally when the loan portfolio increases, absent other factors, the allowance for credit loss methodology results in a higher dollar amount of estimated probable losses than would be the case without the increase. Generally when the loan portfolio decreases, absent other factors, the allowance for credit loss methodology results in a lower dollar amount of estimated probable losses than would be the case without the decrease.

Commercial and commercial real estate loans generally have greater credit risks compared to the one- to four-family residential mortgage loans we originate, as they typically involve larger loan balances concentrated with single borrowers or groups of related borrowers. In addition, the payment experience on loans secured by income-producing properties typically depends on the successful operation of the related business and thus may be subject to a greater extent to adverse conditions in the real estate market and in the general economy. Actual credit losses may be significantly more than the allowance for credit losses we have established, which could have a material negative effect on our financial results.

Generally, we underwrite commercial loans based on cash flow and business history and receive personal guarantees from the borrowers where appropriate. We generally underwrite commercial real estate loans and residential real estate loans at a loan-to-value ratio of 85% or less. Accordingly, in the event that a loan becomes past due and, randomly with respect to performing loans, we will conduct visual inspections of collateral properties and/or review

publicly available information, such as online databases, to ascertain property values. We will also obtain formal appraisals on a regular basis even if we are not considering liquidation of the property to repay a loan. It is our practice to obtain updated appraisals if there is a material change in market conditions or if we become aware of new or additional facts that indicate a potential material reduction in the value of any individual property collateral.

For impaired loans, we utilize the appraised value in determining the appropriate specific allowance for credit losses attributable to a loan. In addition, changes in the appraised value of multiple properties securing our loans may result in an increase or decrease in our general allowance for credit losses as an adjustment to our historical loss experience due to qualitative and environmental factors, as described above.

As of December 31, 2015 and 2014, nonperforming loans amounted to $10.4 million and $4.3 million, respectively. The amount of nonperforming loans requiring specific reserves totaled $1.4 million and $1.1 million, respectively, and the amount of nonperforming loans with no specific valuation allowance totaled $9.0 million and $3.2 million, respectively, at December 31, 2015 and December 31, 2014.

Nonperforming loans are evaluated and valued at the time the loan is identified as impaired on a case by case basis, at the lower of cost or market value. Market value is measured based on the value of the collateral securing the loan. The value of real estate collateral is determined based on an appraisal by qualified licensed appraisers hired by us. Appraised values may be discounted based on management’s historical experience, changes in market conditions from the time of valuation, and/or management’s expertise and knowledge of the client and the client’s business. The difference between the appraised value and the principal balance of the loan will determine the specific allowance valuation required for the loan, if any. Nonperforming loans are reviewed and evaluated on at least a quarterly basis for additional impairment and adjusted accordingly.

We evaluate the loan portfolio on at least a quarterly basis, more frequently if conditions warrant, and the allowance is adjusted accordingly. While we use the best information available to make evaluations, future adjustments to the allowance may be necessary if conditions differ substantially from the information used in making the evaluations. In addition, as an integral part of their examination process, the Maryland Office of the Commissioner of Financial Regulation and the FDIC will periodically review the allowance for credit losses. The Maryland Office of the Commissioner of Financial Regulation and the FDIC may require us to recognize additions to the allowance based on their analysis of information available to them at the time of their examination.

The following table sets forth activity in our allowance for credit losses for the twelve months ended:

	December 31,				
(in thousands)	2015	2014	2013	2012	2011
Balance at beginning of year	$3,602	$2,506	$2,764	$3,433	$3,523
Charge-offs:					
Real estate					
Construction and land loans	-	-	-	-	-
Residential first lien loans	(23)	-	(183)	(79)	-
Residential junior lien loans	(12)	-	-	(44)	-
Commercial owner occupied loans	-	-	-	-	(1,033)
Commercial non-owner occupied loans	(82)	(160)	(375)	(268)	-
Commercial loans and leases	(825)	(2,054)	(759)	(1,129)	(562)
Consumer loans	(5)	(5)	-	(15)	(21)
	(947)	(2,219)	(1,317)	(1,535)	(1,616)
Recoveries:					
Real estate					
Construction and land loans	-	-	-	-	-
Residential first lien loans	3	1	-	-	-
Residential junior lien loans	1	-	-	-	-
Commercial owner occupied loans	-	-	-	-	-
Commercial non-owner occupied loans	318	4	29	63	-
Commercial loans and leases	52	55	80	80	361
Consumer loans	4	-	-	5	1
	378	60	109	148	362
Net charge-offs	(569)	(2,159)	(1,208)	(1,387)	(1,254)
Provision for credit losses	1,836	3,255	950	718	1,164
Balance at end of year	$4,869	$3,602	$2,506	$2,764	$3,433
Net charge-offs to average loans and leases	0.09 %	0.48 %	0.34 %	0.48 %	0.48 %

Allocation of Allowance for Credit Losses

The following tables set forth the allowance for credit losses allocated by loan category and the percent of loans in each category to total loans at the dates indicated. The allowance for credit losses allocated to each category is not necessarily indicative of future losses in any particular category and does not restrict the use of the allowance to absorb losses in other categories.

	December 31,				
	2015	2014	2013	2012	2011
(dollars in thousands)	Amount	Amount	Amount	Amount	Amount

		Percent [1]		Percent [1]		Percent [1]		Percent [1]		Percent [1]
Real estate										
Construction and land loans	$265	9.1 %	$174	11.6 %	$122	12.6 %	$127	11.8 %	$174	14.2 %
Residential first lien loans	300	24.1	272	16.0	200	9.7	204	9.2	111	8.0
Residential junior lien loans	47	3.6	55	3.5	34	2.0	22	2.5	64	3.3
Commercial owner occupied loans	309	17.3	160	20.4	131	22.4	650	19.0	611	16.8
Commercial non-owner occupied loans	728	23.9	562	22.4	541	28.1	505	29.8	197	27.8
Commercial loans and leases	3,094	21.5	2,366	25.2	1,464	24.9	1,227	27.3	2,233	29.4
Consumer loans	126	0.6	13	0.9	14	0.3	29	0.4	43	0.5
Total	$4,869	100.0 %	$3,602	100.0 %	$2,506	100.0 %	$2,764	100.0 %	$3,433	100.0 %

(1) Represents the percent of loans in each category to total loans

We measure the historic loss performance based upon the levels of losses incurred in each preceding 24-month period. As is shown in table above, reflecting the amount of charge-offs per segment, commercial loans has been the category with the most credit losses over the last five years, and thus the allocation of the total allowance at December 31, 2015 reflects this historic loss experience.

Liquidity and Capital Resources

Liquidity is the ability to meet current and future financial obligations. Our primary sources of funds consist of deposit inflows, loan repayments, advances from the FHLB, principal repayments and the sale of securities available for sale. While maturities and scheduled amortization of loans and securities are predictable sources of funds, deposit flows and loan prepayments are greatly influenced by general interest rates, economic conditions and competition. Our Asset/Liability Committee is responsible for establishing and monitoring our liquidity targets and strategies in order to ensure that sufficient liquidity exists for meeting the borrowing needs and deposit withdrawals of our customers as well as unanticipated contingencies. We believe that we have enough sources of liquidity to satisfy our short- and long-term liquidity needs as of December 31, 2015 and December 31, 2014.

We regularly monitor and adjust our investments in liquid assets based upon our assessment of:

- Expected loan demand;
- Expected deposit flows and borrowing maturities;
- Yields available on interest-earning deposits and securities; and
- The objectives of our asset/liability management program.

Excess liquid assets are invested generally in interest-earning deposits and short-term securities.

The most liquid of all assets are cash and cash equivalents. The level of these assets is dependent on our operating, financing, lending and investing activities during any given period. At December 31, 2015 and 2014, cash and cash equivalents totaled $38.3 million and $24.5 million, respectively. The increase for 2015 primarily resulted from growth in our deposits and other funding sources, and proceeds from the sale of shares of our common stock. We used cash and cash equivalents to provide additional funds needed to fund these assets.

Our cash flows are derived from operating activities, investing activities and financing activities as reported in our statements of cash flows included in our financial statements.

At December 31, 2015 and 2014, we had $167.7 million and $115.3 million, respectively, in loan commitments outstanding, including commitments issued to originate loans of $95.0 million and $64.4 million at December 31, 2015 and 2014, respectively, and $72.7 million and $50.9 million in unused lines of credit to borrowers at December 31, 2015 and 2014, respectively. In addition to commitments to originate loans and unused lines of credit we had $7.8 million and $12.4 million in letters of credit at December 31, 2015 and 2014, respectively. Certificates of deposit due within one year totaled $157.2 million, or 21.0% of total deposits, and $105.9 million, or $19.1% of total deposits, at

December 31, 2015 and 2014, respectively. If we do not retain these deposits, we may be required to seek other sources of funds, including loan and securities sales, and FHLB advances. Depending on market conditions, we may be required to pay higher rates on our deposits or other borrowings than we currently pay on the certificates of deposit due on or before December 31, 2016. We believe, however, based on historical experience and current market interest rates that we will retain upon maturity a large portion of our certificates of deposit with maturities of one year or less as of December 31, 2015.

Our primary investing activity is originating loans. During the years ended December 31, 2015 and December 31, 2014, cash used to fund net loan growth was $53.7 million and $48.8 million, respectively. During these periods, we purchased $42.8 million and $26.5 million of securities, respectively. Additionally, in 2015 we purchased an additional $1.8 million of bank owned life insurance.

Financing activities consist primarily of activity in deposit accounts, FHLB advances and related FHLB stock activity. We experienced a net increase in cash provided from deposits of $18.0 million and $2.1 million, respectively, during the years ended December 31, 2015 and 2014. Deposit flows are affected by the overall level of interest rates, the interest rates and products offered by us and our local competitors, and by other factors. Further impacting total cash provided by financing activities was the impact of the issuance of 2,173,913 shares of common stock via private placement for net proceeds $23.8 million.

Liquidity management is both a daily and long-term function of business management. If we require funds beyond our ability to generate them internally, borrowing agreements exist with the FHLB, which provide an additional source of funds. FHLB advances increased to $78.5 million at December 31, 2015 compared to $43.0 million at December 31, 2014. At December 31, 2015, we had the ability to borrow up to a total of $203.5 million based upon our credit availability at the FHLB, subject to collateral requirements.

The Bank is subject to various regulatory capital requirements, including a risk-based capital measure. The risk-based capital guidelines include both a definition of capital and a framework for calculating risk-weighted assets by assigning balance sheet assets and off-balance sheet items to broad risk categories. At December 31, 2015 and 2014, the Bank exceeded all regulatory capital requirements. The Bank is considered “well capitalized” under regulatory guidelines. See— “Item 1. Business—Supervision and Regulation—Howard Bank—Capital Requirements” and the Notes to o
Financial Statements.

Commitments, Contingent Liabilities, and Off-Balance Sheet Arrangements

We are party to financial instruments with off-balance sheet risk in the normal course of business to meet the financial needs of our customers. These financial instruments are limited to commitments to originate loans and involve, to varying degrees, elements of credit, interest rate, and liquidity risk. These do not represent unusual risks, and management does not anticipate any losses that would have a material effect on us.

Outstanding loan commitments and lines of credit at December 31, 2015 and December 31, 2014 are as follows:

	December 31,	
(in thousands)	2015	2014
Unfunded loan commitments	$95,009	$64,375
Unused lines of credit	72,664	50,889
Letters of credit	7,848	12,397

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. We generally require collateral to support financial instruments with credit risk on the same basis as we do for balance sheet instruments. Management generally bases the collateral required on the credit evaluation of the counterparty. Commitments generally have interest rates at current market rates, expiration dates or other termination clauses and may require payment of a fee. Available credit lines represent the unused portion of lines of credit previously extended and available to the customer so long as there is no violation of any contractual condition. These lines generally have variable interest rates. Since we expect many of the commitments to expire without being drawn upon, and since it is unlikely that all customers will draw upon their lines of credit in full at any one time, the total commitment amount or line of credit amount does not necessarily represent future cash requirements. We evaluate each customer’s credit-worthiness on a case-by-case basis. Because we conservatively underwrite these facilities at inception, we have not had to withdraw any commitments. We are not aware of any loss that we would incur by funding our commitments, lines of credit or letters of credit.

The credit risk involved in these financial instruments is essentially the same as that involved in extending loan facilities to customers. No amount has been recognized in the statement of financial condition at December 31, 2015, December 31, 2014 or December 31, 2013 as a liability for credit loss related to these commitments.

Impact of Inflation and Changing Prices

Our financial statements and related notes have been prepared in accordance with U.S. GAAP. U.S. GAAP generally requires the measurement of financial position and operating results in terms of historical dollars without consideration of changes in the relative purchasing power of money over time due to inflation. The impact of inflation is reflected in the increased cost of our operations. Unlike industrial companies, our assets and liabilities are primarily monetary in nature. As a result, changes in market interest rates have a greater impact on performance than the effects of inflation.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk

Not required as the Company is a smaller reporting company.

Part II

Item 8. Financial Statements and Supplementary Data

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Shareholders and Board of Directors
Howard Bancorp, Inc.

Ellicott City, Maryland

We have audited the accompanying consolidated balance sheets of Howard Bancorp, Inc., (the "Company") as of December 31, 2015 and 2014, and the related consolidated statements of operations, comprehensive income, changes in shareholders' equity, and cash flows for each of the years in the three-year period ended December 31, 2015. The Company's management is responsible for these consolidated financial statements. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of their internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing 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 over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Howard Bancorp, Inc. as of December 31, 2015 and 2014, and the results of its operations and its cash flows for each of the years in the three-year period ended December 31, 2015, in conformity with accounting

principles generally accepted in the United States of America.

Baltimore, Maryland

March 29, 2016

Suite 200, 809 Glen Eagles Court Baltimore, Maryland 21286 410-823-8000 1-800-686-3883 Fax: 410-296-4815
www.stegman.com

Members of

Howard Bancorp, Inc. and Subsidiary

Consolidated Balance Sheets

(in thousands)	December 31, 2015	2014
ASSETS		
Cash and due from banks	$31,818	$23,598
Federal funds sold	6,522	919
Total cash and cash equivalents	38,340	24,517
Securities available-for-sale, at fair value	49,573	41,079
Nonmarketable equity securities	4,163	2,571
Loans held for sale, at fair value	49,677	42,881
Loans and leases, net of unearned income	760,002	552,917
Allowance for credit losses	(4,869)	(3,602)
Net loans and leases	755,133	549,315
Bank premises and equipment, net	20,765	12,122
Goodwill	603	-
Core deposit intangible	2,903	1,391
Bank owned life insurance	18,548	11,659
Other real estate owned	2,369	2,472
Interest receivable and other assets	4,685	3,409
Total assets	$946,759	$691,416
LIABILITIES		
Noninterest-bearing deposits	$173,689	$142,727
Interest-bearing deposits	573,719	411,312
Total deposits	747,408	554,039
Short-term borrowings	69,121	48,628
Long-term borrowings	29,707	19,000
Deferred tax liability	1,667	4,686
Accrued expenses and other liabilities	5,957	5,420
Total liabilities	853,860	631,773
COMMITMENTS AND CONTINGENCIES		
SHAREHOLDERS' EQUITY		
Preferred stock—par value $0.01 (liquidation preference of $1,000 per share) authorized 5,000,000; shares issued and outstanding 12,562 series AA at December 31, 2015 and December 31, 2014	12,562	12,562
Common stock - par value of $0.01 authorized 10,000,000 shares; issued and outstanding 6,962,139 shares at December 31, 2015 and 4,145,547 at December 31, 2014	70	41
Capital surplus	70,587	38,360
Retained earnings	9,712	8,696
Accumulated other comprehensive loss	(32)	(16)
Total shareholders’ equity	92,899	59,643
Total liabilities and shareholders’equity	$946,759	$691,416

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

Consolidated Statements of Operations

	December 31,		
(in thousands)	2015	2014	2013
INTEREST INCOME			
Interest and fees on loans	$33,017	$23,056	$17,579
Interest and dividends on securities	269	250	78
Other interest income	63	54	54
Total interest income	33,349	23,360	17,711
INTEREST EXPENSE			
Deposits	2,611	2,079	1,656
Short-term borrowings	154	106	114
Long-term borrowings	307	217	131
Total interest expense	3,072	2,402	1,901
NET INTEREST INCOME	30,277	20,958	15,810
Provision for credit losses	1,836	3,255	950
Net interest income after provision for credit losses	28,441	17,703	14,860
NONINTEREST INCOME			
Service charges on deposit accounts	773	597	387
Realized and unrealized gains on mortgage banking activity	6,971	4,341	215
Bargain purchase gain	-	16,090	-
Loss on the sale of securities	-	(228)	-
Loss on the sale of other real estate owned	(8)	-	(37)
Income from bank owned life insurance	408	377	282
Loan fee income	2,979	1,601	115
Other operating income	804	478	362
Total noninterest income	11,927	23,256	1,324
NONINTEREST EXPENSE			
Compensation and benefits	17,196	13,434	7,397
Occupancy and equipment	3,816	2,462	1,592
Amortization of core deposit intangible	462	111	34
Marketing and business development	2,861	1,674	752
Professional fees	1,478	1,046	883
Data processing fees	1,353	866	529
Merger and restructuring	4,344	455	-
FDIC Assessment	453	442	327
Provision for other real estate owned	736	-	347
Loan production expense	2,223	1,170	248
Other operating expense	3,331	2,034	1,130
Total noninterest expense	38,253	23,694	13,239
INCOME BEFORE INCOME TAXES	2,115	17,265	2,945
Income tax expense	973	6,853	984
NET INCOME	$1,142	$10,412	$1,961
Preferred stock dividends	126	126	165
Net income available to common shareholders	$1,016	$10,286	$1,796
NET INCOME PER COMMON SHARE			

Basic	$0.16	$2.53	$0.44
Diluted	$0.16	$2.48	$0.44

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

Consolidated Statements of Comprehensive Income

	December 31,		
(in thousands)	2015	2014	2013
Net Income	$1,142	$10,412	$1,961
Other comprehensive income			
Investments available-for-sale:			
Reclassification adjustment for losses	-	228	-
Related income tax benefit	-	(90)	-
Unrealized holding losses	(22)	(262)	(27)
Related income tax benefit	6	104	10
Comprehensive income	$1,126	$10,392	$1,944

Consolidated Statements of Changes in Shareholders' Equity

(dollars in thousands, except share data)	Preferred stock	Number of shares	Common stock	Capital Surplus	Retained Earnings / (Accumulated deficit)	Accumulated other comprehensive income/(loss)	Total
Balances at January 1, 2013	$12,562	4,040,471	$ 40	$37,484	$ (3,386)	$ 21	$46,721
Net income	-	-	-	-	1,961	-	1,961
Net unrealized loss on securities	-	-	-	-	-	(17)	(17)
Dividends paid on preferred stock	-	-	-	-	(165)	-	(165)
Issuance of common stock:							
Stock awards	-	5,179	-	37	-	-	37
Stock-based compensation	-	50,000	1	86	-	-	87
Balances at December 31, 2013	12,562	4,095,650	41	37,607	(1,590)	4	48,624
Net income	-	-	-	-	10,412	-	10,412
Net unrealized loss on securities	-	-	-	-	-	(20)	(20)
Dividends paid on preferred stock	-	-	-	-	(126)	-	(126)
Forfeited restricted shares	-	(6,668)	-	(34)	-	-	(34)
Issuance of common stock:							
Exercise of options and warrants	-	51,207	-	507	-	-	507
Stock awards	-	5,358	-	54	-	-	54
Stock-based compensation	-	-	-	226	-	-	226
Balances at December 31, 2014	12,562	4,145,547	41	38,360	8,696	(16)	59,643
Net income	-	-	-	-	1,142	-	1,142
Net unrealized loss on securities	-	-	-	-	-	(16)	(16)
Dividends paid on preferred stock	-	-	-	-	(126)	-	(126)
Forfeited stock awards	-	(6,664)	-	(34)	-	-	(34)

Issuance of common stock:							
Stock offering	-	2,173,913	22	23,096	-	-	23,118
Stock awards	-	7,163	-	95	-	-	95
Exercise of options	-	62,287	1	652	-	-	653
Acquisition of Patapsco Bancorp	-	560,891	6	8,043			8,049
Stock-based compensation	-	19,002	-	375	-	-	375
Balances at December 31, 2015	$12,562	6,962,139	$ 70	$70,587	$ 9,712	$ (32)	$92,899

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

Consolidated Statements of Cash Flows

	Year Ended December 31,		
(in thousands)	2015	2014	2013
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net income	$1,142	$10,412	$1,961
Adjustments to reconcile net income to net cash from operating activities:			
Provision for credit losses	1,836	3,255	950
Deferred income (benefit) taxes	(3,019)	5,825	45
Provision for other real estate owned	736	-	347
Depreciation	1,008	734	599
Stock-based compensation	436	246	124
Net (amortization) accretion of investment securities	(13)	7	17
Bargain purchase gain	-	(16,090)	-
Loss on sales of securities	-	228	-
Net amortization of intangible asset	462	111	34
Loans originated for sale	(591,422)	(309,404)	(14,119)
Proceeds from sale of loans originated for sale	591,597	274,162	12,674
Realized and unrealized gains on mortgage banking activity	(6,971)	(4,341)	(215)
Loss on sales of other real estate owned, net	8	-	37
Cash surrender value of BOLI	(408)	(377)	(282)
Decrease in interest receivable	(356)	(542)	(29)
Increase in interest payable	90	56	21
(Increase) decrease in other assets	(368)	159	(981)
(Decrease) increase in other liabilities	(2,190)	4,447	(443)
Net cash (used in) provided by operating activities	(7,432)	(31,112)	740
CASH FLOWS FROM INVESTING ACTIVITIES:			
Purchases of investment securities available-for-sale	(42,880)	(26,544)	(50,513)
Proceeds from maturities of investment securities available-for-sale	61,043	48,810	48,658
Net increase in loans and leases outstanding	(53,749)	(48,765)	(45,679)
Purchase of bank owned life insurance	(1,800)	-	(11,000)
Proceeds from the sale of other real estate owned	12	-	141
Purchase of premises and equipment	(5,273)	(2,010)	(1,033)
Cash and cash equivalents of acquisition	10,899	13,426	-
Cash received (paid) in acquisition	(2,015)	26,496	(3,195)
Net cash (used in) provided by investing activities	(33,763)	11,413	(62,621)
CASH FLOWS FROM FINANCING ACTIVITIES:			
Net increase (decrease) in noninterest-bearing deposits	18,513	24,488	(6,115)
Net (decrease) increase in interest-bearing deposits	(547)	(22,360)	44,866
Net increase in short-term borrowings	15,493	2,971	18,670
Proceeds from issuance of long-term debt	6,914	12,000	12,000
Repayment of long-term debt	(9,000)	(9,000)	(8,000)
Net proceeds from issuance of common stock, net of cost	23,771	507	-
Cash dividends on preferred stock	(126)	(126)	(165)
Net cash provided by financing activities	55,018	8,480	61,256

Net increase (decrease) in cash and cash equivalents	13,823	(11,219)	(625)
Cash and cash equivalents at beginning of period	24,517	35,736	36,361
Cash and cash equivalents at end of period	$38,340	$24,517	$35,736
SUPPLEMENTAL INFORMATION			
Cash payments for interest	$2,982	$2,345	$1,879
Cash payments for income taxes	2,890	495	707
Transferred from loans to other real estate owned	625	95	0
Fair value of assets and liabilities from acquisitions			
Tangible assets acquired	211,901	134,892	
Intangible assets acquired	2,577	677	
Liabilities assumed	(204,414)	(143,990)	
Total merger consideration	$10,064	$(8,421)	$-

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

Notes to Consolidated Financial Statements

Note 1: Summary of Significant Accounting Policies

Nature of Operations

On December 15, 2005, Howard Bancorp, Inc. (“Bancorp”) acquired all of the stock and became the holding company of Howard Bank (the “Bank”) pursuant to the Plan of Reorganization approved by the shareholders of the Bank and by federal and state regulatory agencies. Each share of the Bank’s common stock was converted into two shares of Bancorp common stock effected by the filing of Articles of Exchange on that date, and the shareholders of the Bank became the shareholders of Bancorp. The Bank has four subsidiaries, three of which hold foreclosed real estate and the other owns and manages real estate that is used as a branch location and has office and retail space. The accompanying consolidated financial statements of Bancorp and its wholly-owned subsidiary bank (collectively the “Company”) have been prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”).

Bancorp was incorporated in April of 2005 under the laws of the State of Maryland and is a bank holding company registered under the Bank Holding Company Act of 1956. Bancorp is a single bank holding company with one subsidiary, Howard Bank, which operates as a state trust company with commercial banking powers regulated by the Maryland Division of Financial Regulation.

On October 17, 2014, the Bank acquired certain assets and assumed substantially all deposits and certain other liabilities of NBRS Financial Bank (“NBRS”), which was closed on October 17, 2014 by the Maryland Office of the Commissioner of Financial Regulation (the “NBRS Acquisition”). The NBRS Acquisition was completed in accordance with the terms of the Purchase and Assumption Agreement with the Federal Deposit Insurance Corporation (the “FDIC”). The Bank did not acquire any of NBRS’s other real estate owned. See Note 2 for further information regarding the NBRS Acquisition.

On August 28, 2015, Bancorp completed its acquisition of Patapsco Bancorp through the merger of Patapsco Bancorp, the parent company of The Patapsco Bank, with and into Bancorp pursuant to the Agreement and Plan of Merger dated as of March 2, 2015, as amended, by and between the Company and Patapsco Bancorp. As a result of the merger, each share of common stock of Patapsco Bancorp was converted into the right to receive, at the holder’s election, $5.09 in cash or 0.3547 shares of Bancorp common stock, provided that (i) cash was paid in lieu of any fractional shares of Bancorp common stock and (ii) 20% of the shares of common stock of Patapsco Bancorp outstanding at the time of the merger were exchanged for cash in the merger, with the remaining shares of Patapsco Bancorp common stock exchanged for 560,891 shares of Bancorp common stock. The aggregate merger consideration

was $10.064 million. In connection with the merger, immediately thereafter Patapsco Bank was merged with and into the Bank, with the Bank the surviving bank.

The Company is a diversified financial services company providing commercial banking, mortgage banking and consumer finance through banking branches, the internet and other distribution channels to businesses, business owners, professionals and other consumers located primarily in the Greater Baltimore Metropolitan Area.

The following is a description of the Company's significant accounting policies.

Principles of Consolidation

The consolidated financial statements include the accounts of Bancorp, its subsidiary bank and the Bank's subsidiaries. All significant intercompany accounts and transactions have been eliminated. The parent company only financial statements report investments in the subsidiary bank under the equity method. Certain reclassifications may have been made to the prior year's consolidated financial statements to conform to current period presentation.

Use of Estimates

The preparation of financial statements in conformity with GAAP 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. Material estimates that are particularly susceptible to significant changes in the near-term relate to the determination of the allowance for credit losses, other-than-temporary impairment of investment securities and the fair value of loans held for sale.

Segment Information

The Company has one reportable segment, “Community Banking.” All of the Company’s activities are interrelated, and each activity is dependent and assessed based on how each of the activities of the Company supports the others. For example, lending is dependent upon the ability of the Bank to fund itself with deposits and other borrowings and manage interest rate and credit risk. Accordingly, all significant operating decisions are based upon analysis of the Company as one segment or unit.

Cash and Cash Equivalents

Cash and cash equivalents include cash on hand, amounts due from banks, cash items in the process of clearing, federal funds sold, and interest-bearing deposits with banks with original maturities of less than 90 days. Generally, federal funds are sold as overnight investments.

Investment Securities

Marketable equity securities and debt securities not classified as held-to-maturity are classified as available-for-sale. Securities available-for-sale are acquired as part of the Bank's asset/liability management strategy and may be sold in response to changes in interest rates, loan demand, changes in prepayment risk and other factors. Securities available-for-sale are carried at estimated fair value, with unrealized gains or losses based on the difference between amortized cost and fair value reported as accumulated other comprehensive income (loss), net of deferred taxes, a separate component of shareholders’ equity, when appropriate. Realized gains and losses, using the specific identification method, are included as a separate component of noninterest income. Related interest and dividends are included in interest income. Declines in the fair value of individual available-for-sale securities below their amortized cost that are other than temporary result in write-downs of the individual securities to their fair value. Factors affecting the determination of whether an other-than-temporary impairment has occurred include a downgrading of the security by a rating agency, a significant deterioration in the financial condition of the issuer, or that management would not have the intent and ability to hold a security for a period of time sufficient to allow for any anticipated recovery in fair value or that management would be required to sell the security before recovery in fair value.

Nonmarketable Equity Securities

Nonmarketable equity securities include equity securities that are not publicly traded or are held to meet regulatory requirements such as Federal Home Loan Bank stock. These securities are accounted for at cost.

Loans Held-For-Sale

During the quarter ended September 30, 2014 the Company elected to apply the fair value option under Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") 825-10 *"Recognition and Measurement of Financial Assets and Financial Liabilities"* to loans held for sale. As such, mortgage loans originated and intended for sale into the secondary market are carried at fair value. Fair value is determined based on outstanding investor commitments, and in the absence of such commitments, on current investor yield requirements or third party pricing models. This election was made in order to better align the timing and recognition of the revenues generated with the related costs associated with mortgage loans originated with the intent to sell at the measurement date. Prior to this election, loans were originated and recorded at cost as of the measurement date, and related gains or losses were not recorded until the loan was sold.

The Company sells its mortgage loans to third party investors servicing released. Upon sale and delivery, loans are legally isolated from the Company and the Company has no ability to restrict or constrain the ability of third party investors to pledge or exchange the mortgage loans. The Company does not have the entitlement or ability to repurchase the mortgage loans or unilaterally cause third party investors to put the mortgage loans back to the Company. Unrealized and realized gains on loan sales are determined using the specific identification method and are recognized through mortgage banking activity in the Consolidated Statement of Operations.

The Company engages in sales of residential mortgage loans originated by the Bank. Loans held for sale are carried at fair value. Fair value is based on outstanding investor commitments or, in absent of such commitments, based on current investor yield requirements based on third party models. Gains and losses on sales of these loans are recorded as a component of noninterest income in the Consolidated Statements of Operations. The Company's current practice is to sell residential mortgage loans on a servicing released basis, and, therefore, it has no intangible asset recorded for the value of such servicing.

The Company enters into commitments to originate residential mortgage loans whereby the interest rate on the loan is determined prior to funding (i.e. rate lock commitment). Such rate lock commitments on mortgage loans to be sold in the secondary market are considered to be derivatives. The period of time between issuance of a loan commitment and closing and sale of the loan generally ranges from 15 to 60 days. The Company protects itself from changes in interest rates through the use of best efforts forward delivery commitments, whereby the Company commits to sell a loan at a premium at the time the borrower commits to an interest rate with the intent that the buyer has assumed interest rate risk on the loan.

For purposes of calculating fair value of rate lock commitments, we estimate loan closing and investor delivery rate based on historical experience. The measurement of the estimated fair value of the rate lock commitments is presented as realized and unrealized gains from mortgage banking activities.

Loans and Leases

Loans are stated at their principal balance outstanding, plus deferred origination costs, less unearned discounts and deferred origination fees. Interest on loans is credited to income based on the principal amounts outstanding. Origination fees and costs are amortized to income over the contractual life of the related loans. Generally, accrual of interest on a loan is discontinued when the loan is delinquent more than 90 days unless the collateral securing the loan is sufficient to liquidate the loan. All interest accrued but not collected for loans that are placed on non-accrual or charged-off is reversed against interest income. Interest on these loans is accounted for on the cash-basis or cost-recovery method, until qualifying for return to accrual. Loans are returned to accrual status when all principal and interest amounts contractually due are brought current and future payments are reasonably assured.

Management considers loans impaired when, based on current information, it is probable that the Company will not collect all principal and interest payments according to contractual terms. Loans are tested for impairment no later than when principal or interest payments become 90 days or more past due and they are placed on non-accrual. Management also considers the financial condition of the borrower, cash flows of the loan and the value of the related collateral. Impaired loans do not include large groups of smaller balance homogeneous loans such as residential real estate and consumer installment loans which are evaluated collectively for impairment. Loans specifically reviewed for impairment are not considered impaired during periods of “minimal delay” in payment (90 days or less) provided eventual collection of all amounts due is expected. The impairment of a loan may be 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 Company’s impairment on such loans is measured by reference to the fair value of the collateral. Interest income on impaired loans is recognized on the cash basis.

The segments of the Company’s loan portfolio are disaggregated to a level that allows management to monitor risk and performance. The commercial real estate (“CRE”) loan segment is further disaggregated into two classes; owner occupied loans and non-owner occupied loans. Non-owner occupied CRE loans, which include loans secured by non-owner occupied nonfarm nonresidential properties, generally have a greater risk profile than owner occupied CRE loans. The residential mortgage loan segment is further disaggregated into two classes: first lien mortgages and second or junior lien mortgages.

Allowance for Credit Losses

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

The allowance for credit losses consists of a specific component and a nonspecific component. The components of the allowance for credit losses represent an estimation done pursuant to either the Financial Accounting Standards Board's ("FASB") Accounting Standards Codification ("ASC") Topic 450 *Contingencies* or ASC Topic 310 *Receivables*. The specific component of the allowance for credit losses reflects expected losses resulting from analysis developed through credit allocations for individual loans. The credit allocations are based on a regular analysis of all loans over a fixed-dollar amount where the internal credit rating is at or below a predetermined classification. The specific component of the allowance for credit losses also includes management's determination of the amounts necessary given concentrations and changes in portfolio mix and volume.

The nonspecific portion of the allowance is determined based on management's assessment of general economic conditions, as well as economic factors in the individual markets in which the Company operates including the strength and timing of economic cycles and concerns over the effects of a prolonged economic downturn in the current cycle. This determination inherently involves a higher risk of uncertainty and considers current risk factors that may not have yet manifested themselves in the Bank's historical loss factors used to determine the nonspecific component of the allowance, and it recognizes knowledge of the portfolio may be incomplete. The Bank's historic loss factors are based upon actual losses incurred by portfolio segment over the preceding 24-month period. In portfolio segments where no actual losses have been incurred within the most recent 24-month period, industry loss data for that portfolio segment, as provided by the FDIC, are utilized. In addition to historic loss factors, the Bank's methodology for the allowance for credit losses also incorporates other risk factors that may be inherent within the portfolio segments. For each portfolio segment, in addition to the historic loss experience experienced, the other factors that are measured and monitored in the overall determination of the allowance include:

- changes in lending policies, procedures, practices or personnel;
- changes in the level and composition of construction portfolio and related risks;
- changes and migration of classified assets;
- changes in exposure to subordinate collateral lien positions;
- levels and composition of existing guarantees on loans by SBA or other agencies;
- changes in national, state and local economic trends and business conditions;
- changes and trends in levels of loan payment delinquencies; and
- any other factors that management considers relevant to the quality or performance of the loan portfolio.

Each of these qualitative risk factors is measured based upon data generated either internally, or in the case of economic conditions utilizing independently provided data on items such as unemployment rates, commercial real estate vacancy rates, or other market data deemed relevant to the business conditions within the markets served.

The Company's loan policies state that after all collection efforts have been exhausted, and the loan is deemed to be a loss, then the remaining loan balance will be charged to the Company's established allowance for credit losses. All loans are evaluated for loss potential once it has been determined by the Watch Committee that the likelihood of repayment is in doubt. When a loan is past due for at least 90 days or a deterioration in debt service coverage ratio, guarantor liquidity, or loan-to-value ratio has occurred that would cause concern regarding the likelihood of the full repayment of principal and interest, and the loan is deemed not to be well secured, the loan should be moved to non-accrual status and a specific reserve is established if the net realizable value is less than the principal value of the loan balance(s). Once the actual loss value has been determined a charge-off against the allowance for credit losses for the amount of the loss is taken. Each loss is evaluated on its specific facts regarding the appropriate timing to recognize the loss.

Goodwill and Other Intangible Assets

Goodwill represents the excess of the purchase price over the sum of the estimated fair values of tangible and identifiable intangible assets acquired less the estimated fair value of the liabilities assumed. Core deposit intangibles represent the estimated value of long-term deposit relationships acquired in a business combination. The core deposit intangible is amortized over the estimated useful lives of the acquired long-term deposits acquired, and the remaining amounts of the core deposit intangible are periodically reviewed for reasonableness.

Goodwill has an indefinite useful life and is evaluated for impairment annually or more frequently if events and circumstances indicate that the asset might be impaired. An impairment loss is recognized to the extent that the carrying amount exceeds the asset's fair value. The goodwill impairment analysis is a two-step test. The first step, used to identify potential impairment, involves comparing the reporting unit's estimated fair value to its carrying value, including goodwill. If the estimated fair value of a reporting unit exceeds its carrying value, goodwill assigned to that reporting unit is considered not to be impaired. If the carrying value exceeds estimated fair value, there is an indication of potential impairment and the second step is performed to measure the amount of impairment of goodwill assigned to that reporting unit.

If required, the second step involves calculating an implied fair value of goodwill for each reporting unit for which the first step indicated impairment. The implied fair value of goodwill is determined in a manner similar to the amount of goodwill calculated in a business combination, by measuring the excess of the estimated fair value of the reporting unit, as determined in the first step, over the aggregate estimated fair values of the individual assets, liabilities and identifiable intangibles as if the reporting unit was being acquired in a business combination. If the implied fair value of goodwill exceeds the carrying value of goodwill assigned to the reporting unit, there is no impairment. If the carrying value of goodwill assigned to a reporting unit exceeds the implied fair value of the goodwill, an impairment charge is recorded for the excess. An impairment loss cannot exceed the carrying value of goodwill assigned to a reporting unit, and the loss establishes a new basis in the goodwill. Subsequent reversal of goodwill impairment losses is not permitted. We have determined that Howard Bancorp has one reporting unit.

We may engage an external valuation specialist to assist us in the goodwill assessment, which we anticipate will be performed as of September 30th each year, which would be our annual test date.

Business Combinations

Accounting principles generally accepted in the United States (U.S. GAAP) requires that the acquisition method of accounting, formerly referred to as purchase method, be used for all business combinations and that an acquirer be identified for each business combination. Under U.S. GAAP, the acquirer is the entity that obtains control of one or more businesses in the business combination, and the acquisition date is the date the acquirer achieves control. U.S. GAAP requires that the acquirer recognize the fair value of assets acquired, liabilities assumed, and any non-controlling interest in the acquired entity at the acquisition date.

Other Real Estate Owned

Other real estate acquired through, or in lieu of, foreclosure is initially recorded at the lower of book value or fair value less estimated cost to sell at the date of acquisition, establishing a new cost basis. Revenues and expenses from operations are included in noninterest income. Additions to the valuation allowance are included in noninterest expense. Subsequent to foreclosure, valuations are periodically performed by management and an allowance for losses is established, if necessary, by a charge to operations if the carrying value of a property exceeds its estimated fair value less estimated costs to sell.

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, which generally range from 3 to 10 years for furniture, fixtures and equipment and 3 to 5 years for computer software and hardware. Leasehold improvements are amortized over the terms of the respective leases or the estimated useful lives of the improvements, whichever is shorter. The costs of major renewals and betterments are capitalized, while the costs of ordinary maintenance and repairs are included in noninterest expense.

Income Taxes

The Company uses the liability method of accounting for income taxes. Under the liability method, deferred tax assets and liabilities are determined based on differences between the financial statement carrying amounts and the tax bases of existing assets and liabilities (i.e., temporary differences) and are measured at the enacted rates that will be in effect when these differences reverse.

As changes in tax laws or rates are enacted, deferred tax assets and liabilities are adjusted through the provision for income taxes. In addition, deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or the entire deferred tax asset will not be realized.

The Company does not have uncertain tax positions that are deemed material, and did not recognize any adjustments for unrecognized tax benefits. The Company's policy is to recognize interest and penalties on income taxes in other non-interest expenses.

Net Income Per Common Share

Basic net income per common share is computed by dividing net income available to common shareholders by the weighted average number of common shares outstanding during the year. Diluted net income per common share is computed by dividing net income available to common shareholders by the weighted average number of common shares outstanding during the year including any potential dilutive effects of common stock equivalents, such as options and warrants.

Share-Based Compensation

Compensation cost is recognized for stock options issued to directors and employees. Compensation cost is measured as the fair value of these awards on their date of grant. A Black-Scholes model is utilized to estimate the fair value of stock options. Compensation cost is recognized over the required service period, generally defined as the vesting period for stock option awards. For awards with graded vesting, compensation cost is recognized on a straight-line basis over the requisite service period for the entire award. When an award is granted to an employee who is retirement eligible, the compensation cost of these awards is recognized over the period up to when the director or employee first becomes eligible to retire.

Compensation expense for non-vested common stock awards is based on the fair value of the awards, which is generally the market price of the common stock on the measurement date, which, for the Company, is the date of grant, and is recognized ratably over the service period of the award.

Off-Balance Sheet Financial Instruments

In the ordinary course of business, the Company has entered into off-balance sheet financial instruments consisting of commitments to extend credit. Such financial instruments are recorded in the consolidated balance sheet when they are funded.

Comprehensive Income

Accounting principles generally require that recognized revenue, expenses, gains and losses be included in net income. Certain changes in assets and liabilities, such as unrealized gains and losses on securities available for sale,

are reported as a separate component of the equity section of the consolidated balance sheets, such items, along with net income, are components of comprehensive income.

Transfer of Financial Assets

Transfers of financial assets are accounted for as sales, when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when (1) the assets have been isolated from the Company, (2) the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets, and (3) the Company does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity. In certain cases, the recourse to the Bank to repurchase assets may exist but is deemed immaterial based on the specific facts and circumstances.

Reclassifications

Certain reclassifications to 2014 and 2013 financial presentation were made to conform to the 2015 presentation. These reclassifications did not affect previous reported net income or total shareholders' equity.

New Accounting Pronouncements

The FASB issued ASU 2016-02, *Leases (Topic 842).* The new guidance requires lessees to recognize lease assets and lease liabilities related to certain operating leases on the balance sheet by lessees and disclose key information about leasing arrangements. This guidance is effective for fiscal years beginning after December 15, 2018 and interim periods within those fiscal years. The Company is currently evaluating this guidance to determine the impact on its consolidated financial statements.

The FASB issued ASU No. 2016-01, *Financial Instruments – Recognition and Measurement of Financial Assets and Liabilities*. ASU No. 2016-01 requires equity investments to be measured at fair value with changes in fair value recognized in net income, excluding equity investments that are consolidated or accounted for under the equity method of accounting. The amendment allows equity investments without readily determinable fair values to be measured at cost minus impairment, with a qualitative assessment required to identify impairment. The amendment also requires public companies to use exit prices to measure the fair value of financial instruments purposes; requiring separate presentation of financial assets and financial liabilities by measurement category and form of financial asset on the balance sheet or the accompanying notes to the financial statement; it eliminates the disclosure requirements related to measurement assumptions for the fair value of instruments measured at amortized cost. In addition, for liabilities measured at fair value under the fair value option, to present in other comprehensive income changes in fair value due to changes in instrument-specific credit risk. ASU No. 2016-01 is effective for fiscal years beginning after December 15, 2017 and interim periods within those fiscal years. The Company is currently evaluating the impact of

adopting the new guidance on its consolidated financial statements.

The FASB issued ASU No. 2015-16, *Business Combinations (Topic 805): Simplifying the Accounting for Measurement-Period Adjustments.* This update eliminates the requirement to retrospectively adjust the provisional amounts recognized at the acquisition date with a corresponding adjustment to goodwill. These adjustments are required when new information is obtained about facts and circumstances that existed as of the acquisition date that, if known, would have affected the measurement of the amounts initially recognized or would have resulted in the recognition of additional assets or liabilities. The update also requires the nature of and reason for the business combination, to be disclosed in the consolidated financial statements. ASU 2015-16 is effective for fiscal years beginning after December 15, 2015, and interim periods within those fiscal years. The Company will evaluate this amendment but does not believe it will have an impact on its financial position or results of operations.

The FASB issued ASU No. 2014-14, *Receivables—Troubled Debt Restructurings by Creditors (Subtopic 310-40): Classification of Certain Government-Guaranteed Mortgage Loans upon Foreclosure.* This update clarifies how creditors classify certain government-sponsored mortgage loans to borrowers with a guarantee that entitles the creditor to recover all or a portion of the unpaid principal balance from the government if the borrower defaults. The amendments in this update require that a mortgage loan be derecognized and that a separate other receivable be recognized upon foreclosure if the following conditions are met:

1. The loan has a government guarantee that is not separable from the loan before foreclosure.
2. At the time of foreclosure, the creditor has the intent to convey the real estate property to the guarantor and make a claim on the guarantee, and the creditor has the ability to recover under that claim.
3. At the time of foreclosure, any amount of the claim that is determined on the basis of the fair value of the real estate is fixed. Upon foreclosure, the separate other receivable should be measured based on the amount of the loan balance (principal and interest) expected to be recovered from the guarantor.

Adoption of the amendments in this update can be either a prospective transition method or a modified retrospective transition method. For prospective transition, an entity should apply the amendments in this update to foreclosures that occur after the date of adoption. For modified retrospective transition, an entity should apply the amendments in this update by means of a cumulative effect adjustment (through a reclassification to a separate other receivable) as of the beginning of the annual period of adoption. ASU 2015-14 was effective for interim and annual periods beginning after December 15, 2014 and did not have a significant impact on the Company’s financial statements.

The FASB issued ASU No. 2014-12, *Compensation—Stock Compensation (Topic 718): Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period.* The amendments require that a performance target that affects vesting and that could be achieved after the requisite service period be treated as a performance condition. Guidance in Topic 718 as it relates to awards with performance conditions that affect vesting should be applied to account for such awards. As such, the performance target should not be reflected in estimating the grant-date fair value of the award. Compensation cost should be recognized in the period in which it becomes probable that the performance target will be achieved and should represent the compensation cost attributable to the period(s) for which the requisite service has already been rendered. If the performance target becomes probable of being achieved before the end of the requisite service period, the remaining unrecognized compensation cost should be recognized prospectively over the remaining requisite service

period. The total amount of compensation cost recognized during and after the requisite service period should reflect the number of awards that are expected to vest and should be adjusted to reflect those awards that ultimately vest. The requisite service period ends when the employee can cease rendering service and still be eligible to vest in the award if the performance target is achieved. As indicated in the definition of vest, the stated vesting period (which includes the period in which the performance target could be achieved) may differ from the requisite service period. The amendments of ASU 2014-12 are effective for interim and annual periods beginning after December 15, 2015. The Company will evaluate this amendment but does not believe it will have an impact on its financial position or results of operations.

The FASB issued Update ASU No. 2014-09, *Revenue from Contracts with Customers* (Topic 606): The guidance requires an entity to recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The amendments in this update are effective for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period. Early adoption is permitted, but not before the original effective date of December 15, 2016. The Company will evaluate the amendments in this update but does not believe they will have an impact on its financial position or results of operations.

The FASB issued ASU No. 2014-04, *Receivables –Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans upon Foreclosure.* The guidance clarifies when an "in substance repossession or foreclosure" occurs, that is, when a creditor should be considered to have received physical possession of residential real estate property collateralizing a consumer mortgage loan, such that all or a portion of the loan should be derecognized and the real estate property recognized. ASU 2014-04 states that a creditor is considered to have received physical possession of residential real estate property collateralizing a consumer mortgage loan, upon either the creditor obtaining legal title to the residential real estate property upon completion of a foreclosure, or the borrower conveying all interest in the residential real estate property to the creditor to satisfy that loan through completion of a deed in lieu of foreclosure or through a similar legal agreement. The amendments of ASU 2014-04 also require interim and annual disclosure of both the amount of foreclosed residential real estate property held by the creditor and the recorded investment in consumer mortgage loans collateralized by residential real estate property that are in the process of foreclosure. The amendments of ASU 2014-04 are effective for interim and annual periods beginning after December 15, 2014, and may be applied using either a modified retrospective transition method or a prospective transition method as described in ASU 2014-04. ASU 2014-04 did not have a significant impact on the Company's financial statements.

Note 2: Business Combinations

Patapsco Acquisition

On August 28, 2015, Bancorp completed its acquisition of Patapsco Bancorp through the merger of Patapsco Bancorp, the parent company of The Patapsco Bank, with and into Bancorp pursuant to the Agreement and Plan of Merger dated as of March 2, 2015, as amended, by and between the Company and Patapsco Bancorp. As a result of the merger, each share of common stock of Patapsco Bancorp was converted into the right to receive, at the holder's election, $5.09 in cash or 0.3547 shares of Bancorp common stock, provided that (i) cash was paid in lieu of any fractional shares of Bancorp common stock and (ii) 20% of the shares of common stock of Patapsco Bancorp outstanding at the time of the merger were exchanged for cash in the merger, with the remaining shares of Patapsco Bancorp common stock exchanged for 560,891 shares of Bancorp common stock. The aggregate merger consideration was $10.064 million. In connection with the merger, immediately thereafter Patapsco Bank was merged with and into the Bank, with the Bank the surviving bank.

The Company has accounted for the merger under the acquisition method of accounting in accordance with FASB ASC Topic 805, "*Business Combinations*," whereby the acquired assets and assumed liabilities were recorded by Bancorp at their estimated fair values as of their acquisition date. Fair value estimates for loans and deposits were based on management's acceptance of a fair market valuation analysis performed by an independent third party firm.

The acquired assets and assumed liabilities of Patapsco Bancorp were measured at estimated fair value. Management made significant estimates and exercised significant judgment in accounting for the acquisition of Patapsco Bancorp. Management judgmentally assigned risk ratings to loans based on appraisals and estimated collateral values, expected

cash flows, prepayment speeds and estimated loss factors to measure fair values for loans. Deposits and borrowings were valued based upon interest rates, original and remaining terms and maturities, as well as current rates for similar funds in the same markets. Premises and equipment was valued based on recent appraised values. Management used quoted or current market prices to determine the fair value of investment securities.

The following table provides the purchase price as of the acquisition date, the identifiable assets acquired and liabilities assumed at their estimated fair values, and the resulting goodwill of $603 thousand recorded from the acquisition:

(in thousands)

Purchase Price Consideration		
Cash consideration	$	2,015
Purchase price assigned to shares exchanged for stock		8,049
Total purchase price for Patapsco acquisition	$	10,064

Assets acquired at fair value:		
Cash and cash equivalents	$	19,047
Investment securities available for sale		26,255
Loans		156,907
Accrued interest receivable		602
Other assets		9,090
Core deposit intangible		1,974
Total fair value of assets acquired	$	213,875
Liabilities assumed at fair value:		
Deposits		175,083
Borrowings		17,737
Accrued expenses and other liabilities		11,594
Total fair value of liabilities assumed	$	204,414
Net assets acquired at fair value:		$ 9,461
Transaction consideration paid to Patapsco Bancorp		10,064
Amount of goodwill recorded from Patapsco acquisition		$ 603

Acquired loans

The following table outlines the contractually required payments receivable, cash flows we expect to receive, non-accretable credit adjustments and the accretable yield for all Patapsco Bancorp loans as of the acquisition date.

	Contractually Required	Non-Accretable Credit	Cash Flows Expected To Be	Accretable FMV Adjustments	Carrying Value of Loans

	Payments Receivable	Adjustments	Collected		Receivable
Performing Loans Acquired	$ 156,393	$ -	$ 156,393	$ 866	$ 155,527
Impaired Loans Acquired	3,465	1,713	1,752	372	1,380
Total	$ 159,858	$ 1,713	$ 158,145	$ 1,238	$ 156,907

At our acquisition of Patapsco Bancorp, we recorded all loans acquired at the estimated fair value on the purchase date with no carryover of the related allowance for loan losses. On the acquisition date, we segregated the loan portfolio into two loan pools, performing and non-performing loans to be retained in our portfolio.

We had an independent third party determine the net discounted value of cash flows on approximately 1,000 performing loans totaling $156.4 million. The valuation took into consideration the loans' underlying characteristics, including account types, remaining terms, annual interest rates, interest types, past delinquencies, timing of principal and interest payments, current market rates, loan-to-value ratios, loss exposures, and remaining balances. These performing loans were segregated into pools based on loan and payment type and in some cases, risk grade. The effect of this fair valuation process was a net accretable discount adjustment of $866 thousand at acquisition.

We also individually evaluated 13 impaired loans totaling $3.5 million to determine the fair value as of the August 28, 2015 measurement date. In determining the fair value for each individually evaluated impaired loan, we considered a number of factors including the remaining life of the acquired loan, estimated prepayments, estimated loss ratios, estimated value of the underlying collateral and net present value of cash flows we expect to receive, among others.

We established a credit risk related non-accretable difference of $1.7 million relating to these acquired, credit impaired loans, reflected in the recorded net fair value. We further estimated the timing and amount of expected cash flows in excess of the estimated fair value and established an accretable discount adjustment of $372 thousand at acquisition relating to these impaired loans.

Pro forma financial information is not provided because amounts are not meaningful to the Company's financial statements.

NBRS Acquisition

Upon receipt of information from the FDIC, the Company pursued the FDIC assisted acquisition of NBRS Financial Bank as it was deemed a strategic opportunity to acquire assets and assume the liabilities of an institution that operated in counties contiguous to the Company's then current market. The Company has accounted for the NBRS Acquisition under the acquisition method of accounting in accordance with FASB ASC Topic 805, "*Business Combinations*," whereby the acquired assets and assumed liabilities were recorded by the Company at their estimated fair values as of their acquisition date. Fair value estimates were based on management's acceptance of a fair market valuation analysis performed by an independent third party firm.

In October of 2014 the Bank submitted a bid to the FDIC which included a bid based upon acquiring loans at a discounted amount, and also assuming the deposits of NBRS at a slight deposit premium. The Bank was notified that is was the winning bidder in this process, and the net asset discount accepted by the FDIC was $24.5 million. Immediately after the closing of this transaction, the FDIC remitted these funds to the Bank.

The acquired assets and assumed liabilities of NBRS were measured at estimated fair value. Management made significant estimates and exercised significant judgment in accounting for the acquisition of NBRS. Management judgmentally assigned risk ratings to loans based on appraisals and estimated collateral values, expected cash flows, prepayment speeds and estimated loss factors to measure fair values for loans. Premises and equipment was valued based on recent appraised values. Management used quoted or current market prices to determine the fair value of investment securities.

The following table summarizes the acquired assets and assumed liabilities in the NBRS Acquisition as of the acquisition date, and the pre-tax bargain purchase gain of $16.1 million recognized on the transaction:

(in thousands)		
Assets acquired at fair value:		
Cash and cash equivalents	$12,647	
Investment securities available for sale	31,738	
Loans	89,368	
Accrued interest receivable	280	
Other assets	859	
Core deposit intangible	677	
Total fair value of assets acquired	$135,569	
Liabilities assumed at fair value:		
Deposits	143,833	
Accrued expenses and other liabilities	157	
Total fair value of liabilities assumed	$143,990	
Net liabilities assumed at fair value:		$(8,421)
Transaction cash consideration received from the FDIC		24,511
Bargain purchase gain, before tax		$16,090

Acquired Loans

The following table outlines the contractually required payments receivable, cash flows we expect to receive, non-accretable credit adjustments and the accretable yield for all NBRS loans as of the acquisition date.

	Contractually Required Payments Receivable	Non-Accretable Credit Adjustments	Cash Flows Expected To Be Collected	Accretable FMV Adjustments	Carrying Value of Loans Receivable
Performing Loans Acquired	$ 83,536	$ -	$ 83,536	$ 1,721	$ 81,815
Impaired Loans Acquired	2,466	1,125	1,341	285	1,056
Loans under contract to sell	14,489	7,992	6,497	-	6,497
Total	$ 100,490	$ 9,116	$ 91,374	$ 2,006	$ 89,368

At our acquisition of NBRS, we recorded all loans acquired at the estimated fair value on the purchase date with no carryover of the related allowance for loan losses. On the acquisition date, we segregated the loan portfolio into three loan pools, performing and non-performing loans to be retained in our portfolio, and a third category of loans which upon acquisition had pre-arranged agreements to sell within 30 days of acquisition.

We had an independent third party determine the net discounted value of cash flows on approximately 700 performing loans totaling $83.5 million. The valuation took into consideration the loans' underlying characteristics, including account types, remaining terms, annual interest rates, interest types, past delinquencies, timing of principal and interest payments, current market rates, loan to value ratios, loss exposures, and remaining balances. These performing loans were segregated into pools based on loan and payment type and in some cases, risk grade. The effect of this fair valuation process was a net accretable discount adjustment of $1.7 million at acquisition.

We also individually evaluated 13 impaired loans totaling $2.5 million to determine the fair value as of the October 17, 2014 measurement date. In determining the fair value for each individually evaluated impaired loan, we considered a number of factors including the remaining life of the acquired loans, estimated prepayments, estimated loss ratios, estimated value of the underlying collateral and net present value of cash flows we expect to receive, among others.

We established a credit risk related non-accretable difference of $1.1 million relating to these acquired, credit impaired loans, reflected in the recorded net fair value. We further estimated the timing and amount of expected cash flows in excess of the estimated fair value and established an accretable discount adjustment of $285 thousand at acquisition relating to these impaired loans.

During our due diligence, which was conducted as a component of the FDIC bidding process, we invited a third party firm to participate in the onsite loan review in order to allow them to bid upon the majority of the non-accrual and troubled loans held by NBRS. After their review, we entered into a binding agreement where they would purchase specific loans at predetermined amounts, if the Company were the successful bidder in the FDIC process. Because the loans and the pricing was pre-determined, the agreed upon purchase price was deemed to be the fair market value, and these loans were not part of the valuation process utilized on the remaining portfolio loans. These loans were sold to this third party in November 2014 at the fair market value previously determined, and no subsequent gains or losses were recorded upon the sale.

Pro forma financial information is not provided because amounts are not meaningful to the Company’s financial statements.

Note 3: Cash and Due from Banks

Regulation D of the Federal Reserve Act requires that banks maintain reserve balances with the Federal Reserve Bank based principally on the type and amount of their deposits. During 2015 and 2014, the Company maintained balances at the Federal Reserve (in addition to vault cash) to meet the reserve requirements as well as balances to partially compensate for services. Additionally, the Company maintained balances with the Federal Home Loan Bank and two domestic correspondents as partial compensation for services they provided to the Company.

Note 4: Investments Securities

The amortized cost and estimated fair values of investments available for sale are as follows:

(in thousands)	December 31, 2015				2014			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
U.S. Government Agencies	$48,467	$ -	$ 45	$ 48,422	$37,010	$ -	$ 29	$ 36,981
Treasuries	-	-	-	-	4,000	-	3	3,997
Mortgage-backed	54	3	-	57	95	6	-	101
Other investments	1,100	-	6	1,094	-	-	-	-
	$49,621	$ 3	$ 51	$ 49,573	$41,105	$ 6	$ 32	$ 41,079

There have not been any individual securities with an unrealized loss position for a period greater than one year as of either December 31, 2015 or December 31, 2014. Gross unrealized losses and fair value by investment category and length of time the individual securities have been in a continuous unrealized loss position at December 31, 2015 and 2014 is as follows:

December 31, 2015 (in thousands)	Less than 12 months		12 months or more		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
U.S. Government Agencies	$ 39,431	$ 45	$ -	$ -	$39,431	$ 45
Treasuries	-	-	-	-	-	-
Mortgage-backed	-	-	-	-	-	-
Other investments	1,000	6	-	-	1,000	6
	$ 40,431	$ 51	$ -	$ -	$40,431	$ 51

December 31, 2014 (in thousands)	Less than 12 months		12 months or more		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
U.S. Government Agencies	$ 26,477	$ 29	$ -	$ -	$26,477	$ 29

Treasuries	3,997	3	-	-	3,997	3
Mortgage-backed	-	-	-	-	-	-
	$ 30,474	$ 32	$ -	$ -	$30,474	$ 32

The unrealized losses that existed were a result of market changes in interest rates since the original purchase. Management systematically evaluates investment securities for other-than-temporary declines in fair value on a quarterly basis. This analysis requires management to consider various factors, which include (1) duration and magnitude of the decline in value, (2) the financial condition of the issuer or issuers and (3) structure of the security.

An impairment loss is recognized in earnings if any of the following are true: (1) the Company intends to sell the debt security; (2) it is more likely than not that the Company will be required to sell the security before recovery of its amortized cost basis; or (3) the Company does not expect to recover the entire amortized cost basis of the security. In situations where the Company intends to sell or when it is more likely than not that the Company will be required to sell the security, the entire impairment loss must be recognized in earnings. In all other situations, only the portion of the impairment loss representing the credit loss must be recognized in earnings, with the remaining portion being recognized in shareholders' equity as a component of other comprehensive income, net of deferred tax.

The amortized cost and estimated fair values of investments available for sale by contractual maturity are shown below:

(in thousands)	December 31, 2015		2014	
	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
Amounts maturing:				
One year or less	$43,465	$ 43,425	$33,516	$ 33,506
After one through five years	5,002	4,997	7,508	7,487
After five through ten years	54	57	81	86
After ten years	1,100	1,094	-	-
	$49,621	$ 49,573	$41,105	$ 41,079

Because of the composition of the securities portfolios acquired in the Patapsco Bancorp and NBRS acquisitions, management deemed it prudent for interest rate risk management purposes to liquidate both of the acquired portfolios. Thus, in the third quarter of 2015, the Bank both acquired and sold nearly $26.3 million in securities, with no gains or losses incurred upon the liquidation, as the sales were executed within days of the Patapsco Bancorp acquisition. Similarly in the fourth quarter of 2014, the Bank both acquired and sold nearly $31.7 million in securities, which resulted in a net loss on the sale of the securities of $228 thousand. There were no sales of investment securities during 2013.

At December 31, 2015 and December 31, 2014, $22.8 million and $23.8 million fair value of securities were pledged as collateral for repurchase agreements, respectively. No single issuer of securities, except for U.S. Government and U.S. Government agency securities had outstanding balances that exceeded ten percent of shareholders' equity at December 31, 2015.

Note 5: Nonmarketable Equity Securities

At December 31, 2015 and December 31, 2014, the Company's investment in nonmarketable equity securities consisted of Federal Home Loan Bank of Atlanta ("FHLB") stock, which is required for continued membership, of $4.2 million and $2.6 million, respectively. These investments are carried at cost.

Note 6: Loans and Leases

The Company makes loans and leases to customers primarily in the Greater Baltimore Maryland metropolitan area, and surrounding communities. A substantial portion of the Company’s loan portfolio consists of loans to businesses secured by real estate and/or other business assets.

The loan portfolio segment balances at December 31, 2015 and December 31, 2014 are presented in the following table:

	December 31,					
	2015			2014		
(in thousands)	Legacy	Acquired	Total	Legacy	Acquired	Total
Real estate						
Construction and land	$63,085	$6,300	$69,385	$56,490	$7,668	$64,158
Residential - first lien	89,649	93,339	182,988	58,904	29,389	88,293
Residential - junior lien	15,098	12,379	27,477	11,006	8,295	19,301
Total residential real estate	104,747	105,718	210,465	69,910	37,684	107,594
Commercial - owner occupied	94,393	36,722	131,114	85,824	27,002	112,826
Commercial - non-owner occupied	122,304	59,057	181,361	100,589	23,369	123,958
Total commercial real estate	216,696	95,779	312,475	186,413	50,371	236,784
Total real estate loans	384,528	207,797	592,325	312,813	95,723	408,536
Commercial loans and leases	124,981	38,443	163,424	113,176	26,493	139,669
Consumer	1,302	2,951	4,253	1,485	3,227	4,712
Total loans	$510,811	$249,191	$760,002	$427,474	$125,443	$552,917

There were $49.7 million and $42.9 million in loans held for sale at December 31, 2015 and December 31, 2014, respectively.

Portfolio Segments

The Company currently manages its credit products and the respective exposure to credit losses (credit risk) by the following specific portfolio segments (classes) which are levels at which the Company develops and documents its systematic methodology to determine the allowance for credit losses attributable to each respective portfolio segment. These segments are:

- **Commercial business loans & leases** – Commercial loans are made to provide funds for equipment and general corporate needs. Repayment of a loan primarily uses the funds obtained from the operation of the borrower's business. Commercial loans also include lines of credit that are utilized to finance a borrower's short-term credit needs and/or to finance a percentage of eligible receivables and inventory. The Company's loan portfolio also includes a small portfolio of equipment leases, which consists of leases for essential commercial equipment used by small to medium sized businesses.
- **Construction and land loans** – Commercial acquisition, development and construction loans are intended to finance the construction of commercial and residential properties and include loans for the acquisition and development of land. Construction loans represent a higher degree of risk than permanent real estate loans and may be affected by a variety of factors such as the borrower's ability to control costs and adhere to time schedules and the risk that

constructed units may not be absorbed by the market within the anticipated time frame or at the anticipated price. The loan commitment on these loans often includes an interest reserve that allows the lender to periodically advance loan funds to pay interest charges on the outstanding balance of the loan.

- **Commercial owner occupied real estate loans** – Commercial owned-occupied real estate loans consist of commercial mortgage loans secured by owner occupied properties where an established banking relationship exists and involves a variety of property types to conduct the borrower's operations. The primary source of repayment for this type of loan is the cash flow from the business and is based upon the borrower's financial health and the ability of the borrower and the business to repay.
- **Commercial non-owner occupied real estate loans** – Commercial non-owner occupied loans consist of properties where an established banking relationship exists and involves investment properties for warehouse, retail, and office space with a history of occupancy and cash flow. This commercial real estate category contains mortgage loans to the developers and owners of commercial real estate where the borrower intends to operate or sell the property at a profit and use the income stream or proceeds from the sale(s) to repay the loan.
- **Consumer loans** – This category of loans includes primarily installment loans and personal lines of credit. Consumer loans include installment loans used by customers to purchase automobiles, boats and recreational vehicles.
- **Residential first lien mortgage loans** – The residential real estate category contains permanent mortgage loans principally to consumers secured by residential real estate. Residential real estate loans are evaluated for the adequacy of repayment sources at the time of approval, based upon measures including credit scores, debt-to-income ratios, and collateral values. Loans may be either conforming or non-conforming.
- **Residential junior lien mortgage loans** – This category of loans includes primarily home equity loans and lines. The home equity category consists mainly of revolving lines of credit to consumers which are secured by residential real estate. These loans are typically secured with second mortgages on the homes.

Note 7: Credit Quality Assessment

Allowance for Credit Losses

Credit risk can vary significantly as losses, as a percentage of outstanding loans, can vary widely during economic cycles and are sensitive to changing economic conditions. The amount of loss in any particular type of loan can vary depending on the purpose of the loan and the underlying collateral securing the loan. Collateral securing commercial loans can range from accounts receivable to equipment to improved or unimproved real estate depending on the purpose of the loan. Home mortgage and home equity loans and lines are typically secured by first or second liens on residential real estate. Consumer loans may be secured by personal property, such as auto loans or they may be unsecured loan products.

To control and manage credit risk, management has an internal credit process in place to determine whether credit standards are maintained along with an in-house loan administration accompanied by oversight and review procedures. The primary purpose of loan underwriting is the evaluation of specific lending risks that involves the analysis of the borrower's ability to service the debt as well as the assessment of the value of the underlying collateral. Oversight and review procedures include the monitoring of the portfolio credit quality, early identification of potential problem credits and the management of the problem credits. As part of the oversight and review process, the Company maintains an allowance for credit losses (the "allowance") to absorb estimated and probable losses in the loan and lease portfolio. The allowance is based on consistent, continuous review and evaluation of the loan and lease portfolio, along with ongoing assessments of the probable losses and problem credits in each portfolio. While portions of the allowance are attributed to specific portfolio segments, the entire allowance is available to credit losses inherent in the total loan portfolio.

The following table provides information on the activity in the allowance for credit losses by the respective loan portfolio segment for the years ended December 31, 2015 and 2014:

	December 31, 2015							
(in thousands)	Construction and land	Residential first lien	Residential junior lien	Commercial owner occupied	Commercial non-owner occupied	Commercial loans and leases	Consumer loans	Total
Allowance for credit losses:								
Beginning balance	$174	$272	$55	$160	$562	$2,366	$13	$3,602
Charge-offs	-	(23)	(12)	-	(82)	(825)	(5)	(947)
Recoveries	-	3	1	-	318	52	4	378
Provision for credit losses	91	48	3	149	(70)	1,501	114	1,836
Ending balance	$265	$300	$47	$309	$728	$3,094	$126	$4,869

Allowance allocated to:								
Legacy Loans:								
individually evaluated for impairment	$ -	$ -	$ -	$ -	$ -	$ 1,160	$ -	$ 1,160
collectively evaluated for impairment	257	289	40	262	621	1,799	30	3,298
Acquired Loans:								
individually evaluated for impairment	-	-	-	-	-	48	75	123
collectively evaluated for impairment	8	11	7	47	107	87	21	288
Loans:								
Legacy Loans:								
Ending balance	$ 63,085	$ 89,649	$ 15,098	$ 94,393	$ 122,304	$ 124,981	$ 1,302	$ 510,811
individually evaluated for impairment	-	631	63	-	2,838	5,086	-	8,618
collectively evaluated for impairment	63,085	89,018	15,035	94,393	119,466	119,895	1,302	502,193
Acquired Loans:								
Ending balance	6,300	93,339	12,379	36,722	59,057	38,443	2,951	249,191
individually evaluated for impairment	-	363	-	232	151	1,728	150	2,624
collectively evaluated for impairment	6,300	92,976	12,379	36,490	58,906	36,715	2,801	246,565

	December 31, 2014							
(in thousands)	Construction and land	Residential first lien	Residential junior lien	Commercial owner occupied	Commercial non-owner occupied	Commercial loans and leases	Consumer loans	Total
Allowance for credit losses:								
Beginning balance	$122	$200	$34	$131	$541	$1,464	$14	$2,506
Charge-offs	-	-	-	-	(160)	(2,054)	(5)	(2,219)
Recoveries	-	1	-	-	4	55	-	60
Provision for credit losses	52	71	21	29	177	2,901	4	3,255
Ending balance	$174	$272	$55	$160	$562	$2,366	$13	$3,602
Allowance allocated to:								
Legacy Loans:								
individually evaluated for impairment	$60	$-	$-	$-	$-	$483	$-	$543
collectively evaluated for impairment	108	271	25	142	502	1,745	13	2,806
Acquired Loans:								
individually evaluated for impairment	-	-	30	-	-	55	-	85
collectively evaluated for impairment	6	1	-	18	60	83	-	168
Loans:								
Legacy Loans:								
Ending balance	$56,490	$58,904	$11,006	$85,824	$100,589	$113,176	$1,485	$427,474
individually evaluated for impairment	1,144	308	-	-	2,700	2,073	-	6,225
collectively evaluated for impairment	55,346	58,596	11,006	85,824	97,889	111,103	1,485	421,249
Acquired Loans:								
Ending balance	6,260	19,525	7,539	37,519	33,021	18,745	2,834	125,443
individually evaluated for impairment	-	411	57	-	-	405	92	965
collectively evaluated for impairment	6,260	19,114	7,482	37,519	33,021	18,340	2,742	124,478

Integral to the assessment of the allowance process is an evaluation that is performed to determine whether a specific reserve on an impaired credit is warranted. At such time an action plan is agreed upon for the particular loan and an appraisal will be ordered (for real estate based collateral) depending on the time elapsed since the prior appraisal, the loan balance and/or the result of the internal evaluation. The Company's policy is to strictly adhere to regulatory appraisal standards. If an appraisal is ordered, no more than a 45 day turnaround is requested from the appraiser, who is selected from an approved appraiser list. After receipt of the updated appraisal, the Company's Watch Committee will determine whether a specific reserve or a charge-off should be taken based upon an impairment analysis. When potential losses are identified, a specific provision and/or charge-off may be taken, based on the then current likelihood of repayment, that is at least in the amount of the collateral deficiency, and any potential collection costs, as

determined by the independent third party appraisal. Any further collateral deterioration may result in either further specific reserves being established or additional charge-offs. The President and the Chief Lending Officer have the authority to approve a specific reserve or charge-off between Watch Committee meetings to ensure that there are no significant time lapses during this process.

The Company's systematic methodology for evaluating whether a loan is impaired begins with risk-rating credits on an individual basis and includes consideration of the borrower's overall financial condition, resources and payment record, the sufficiency of collateral and, in a select few cases, support from financial guarantors. In measuring impairment, the Company looks to the discounted cash flows of the project itself or the value of the collateral as the primary sources of repayment of the loan. The Company will consider the existence of guarantees and the financial strength and wherewithal of the guarantors involved in any loan relationship as both a secondary source of repayment and for the potential as the primary repayment of the loan**.**

The Company typically relies on recent third party appraisals of the collateral to assist in measuring impairment.

Management has established a credit process that dictates that structured procedures be performed to monitor these loans between the receipt of an original appraisal and the updated appraisal. These procedures include the following:

· An internal evaluation is updated quarterly to include borrower financial statements and/or cash flow projections.
· The borrower may be contacted for a meeting to discuss an update or revised action plan which may include a request for additional collateral.
· Re-verification of the documentation supporting the Company's position with respect to the collateral securing the loan.
· At the Watch Committee meeting the loan may be downgraded and a specific reserve may be decided upon in advance of the receipt of the appraisal if it is determined that the likelihood of repayment is in doubt.

The Company generally follows a policy of not extending maturities on non-performing loans under existing terms. The Company may extend the maturity of a performing or current loan that may have some inherent weakness associated with the loan. Maturity date extensions only occur under terms that clearly place the Company in a position to assure full collection of the loan under the contractual terms and /or terms at the time of the extension that may eliminate or mitigate the inherent weakness in the loan. These terms may incorporate, but are not limited to additional assignment of collateral, significant balance curtailments/liquidations and assignments of additional project cash flows. Guarantees may be a consideration in the extension of loan maturities, but the Company does not extend loans based solely on guarantees. As a general matter, the Company does not view extension of a loan to be a satisfactory approach to resolving non-performing credits. On an exception basis, certain performing loans that have displayed some inherent weakness in the underlying collateral values, an inability to comply with certain loan covenants which are not affecting the performance of the credit or other identified weakness may be extended.

Collateral values or estimates of discounted cash flows (inclusive of any potential cash flow from guarantees) are evaluated to estimate the probability and severity of potential losses. A specific amount of impairment is established based on the Company's calculation of the probable loss inherent in the individual loan. The actual occurrence and severity of losses involving impaired credits can differ substantially from estimates.

Credit risk profile by portfolio segment based upon internally assigned risk assignments are presented below:

	December 31, 2015							
(in thousands)	Construction and land	Residential first lien	Residential junior lien	Commercial owner occupied	Commercial non-owner occupied	Commercial loans and leases	Consumer loans	Total
Credit quality indicators:								
Legacy Loans:								
Not classified	$63,085	$89,081	$15,035	$94,393	$119,637	$121,288	$1,302	$503,820
Special mention	-	-	-	-	-	614	-	614
Substandard	-	410	-	-	2,073	7	-	2,490
Doubtful	-	158	63	-	594	3,072	-	3,887
Total	$63,085	$89,649	$15,098	$94,393	$122,304	$124,981	$1,302	$510,811
Acquired Loans:								
Not classified	$6,300	$92,975	$12,379	$36,484	$58,393	$36,731	$2,801	$246,063
Special mention	-	-	-	-	-	-	-	-
Substandard	-	-	-	-	519	-	-	519
Doubtful	-	364	-	238	145	1,712	150	2,609
Total	$6,300	$93,339	$12,379	$36,722	$59,057	$38,443	$2,951	$249,191

	December 31, 2014							
				Commercial	Commercial	Commercial		

(in thousands)	Construction and land	Residential first lien	Residential junior lien	owner occupied	non-owner occupied	loans and leases	Consumer loans	Total
Credit quality indicators:								
Legacy Loans:								
Not classified	$55,346	$58,439	$10,932	$85,580	$97,889	$111,312	$1,485	$420,983
Special mention	-	-	-	-	-	-	-	-
Substandard	1,144	465	74	244	2,700	1,864	-	6,491
Doubtful	-	-	-	-	-	-	-	-
Total	$56,490	$58,904	$11,006	$85,824	$100,589	$113,176	$1,485	$427,474
Acquired Loans:								
Not classified	$6,260	$18,567	$7,482	$37,519	$33,021	$18,340	$2,742	$123,931
Special mention	-	-	-	-	-	-	-	-
Substandard	-	546	-	-	-	-	-	546
Doubtful	-	412	57	-	-	405	92	966
Total	$6,260	$19,525	$7,539	$37,519	$33,021	$18,745	$2,834	$125,443

- **Special Mention** - A Special Mention asset has potential weaknesses that deserve management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the asset or in the institution's credit position at some future date. Special Mention assets are not adversely classified and do not expose an institution to sufficient risk to warrant adverse classification.
- **Substandard** - Substandard loans are inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any. Loans so classified must have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the Bank will sustain some loss if the deficiencies are not corrected.
- **Doubtful** - Loans classified Doubtful have all the weaknesses inherent in those classified Substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently known facts, conditions and values, highly questionable and improbable.

Loans classified Special Mention, Substandard, Doubtful or Loss are reviewed at least quarterly to determine their appropriate classification. All commercial loan relationships are reviewed annually. Non-classified residential mortgage loans and consumer loans are not evaluated unless a specific event occurs to raise the awareness of a possible credit deterioration.

An aged analysis of past due loans is as follows:

	December 31, 2015							
(in thousands)	Construction and land	Residential first lien	Residential junior lien	Commercial owner occupied	Commercial non-owner occupied	Commercial loans and leases	Consumer loans	Total
Analysis of past due loans:								
Legacy Loans:								
Accruing loans current	$63,070	$ 89,319	$ 15,034	$ 94,141	$ 121,094	$ 120,025	$ 1,301	$503,983
Accruing loans past due:								
31-59 days past due	-	-	1	252	-	24	1	278
60-89 days past due	-	-	-	-	-	725	-	725
Greater than 90 days past due	15	-	-	-	445	-	-	460
Total past due	15	-	1	252	445	749	1	1,463
Non-accrual loans	-	330	63	-	765	4,207	-	5,365
Total loans	$63,085	$ 89,649	$ 15,098	$ 94,393	$ 122,304	$ 124,981	$ 1,302	$510,811
Acquired Loans:								
Accruing loans current	$5,924	$ 91,936	$ 12,290	$ 35,574	$ 58,369	$ 36,568	$ 2,765	$243,426

Accruing loans past due:								
31-59 days past due	67	89	59	73	337	-	11	636
60-89 days past due	309	10	-	607	200	-	23	1,149
Greater than 90 days past due	-	941	30	236	-	147	2	1,356
Total past due	376	1,040	89	916	537	147	36	3,141
Non-accrual loans	-	363	-	232	151	1,728	150	2,624
Total loans	$6,300	$ 93,339	$ 12,379	$ 36,722	$ 59,057	$ 38,443	$ 2,951	$249,191

	December 31, 2014							
(in thousands)	Construction and land	Residential first lien	Residential junior lien	Commercial owner occupied	Commercial non-owner occupied	Commercial loans and leases	Consumer loans	Total
Analysis of past due loans:								
Legacy Loans:								
Accruing loans current	$55,346	$ 58,122	$ 10,932	$ 85,824	$ 100,439	$ 108,451	$ 1,480	$420,594
Accruing loans past due:								
31-59 days past due	-	-	-	-	-	-	5	5
60-89 days past due	-	316	74	-	-	2,816	-	3,206
Greater than 90 days past due	-	158	-	-	150	244	-	552
Total past due	-	474	74	-	150	3,060	5	3,763
Non-accrual loans	1,144	308	-	-	-	1,665	-	3,117
Total loans	$56,490	$ 58,904	$ 11,006	$ 85,824	$ 100,589	$ 113,176	$ 1,485	$427,474
Acquired Loans:								
Accruing loans current	$5,982	$ 18,867	$ 7,430	$ 37,519	$ 33,021	$ 17,990	$ 2,742	$123,551
Accruing loans past due:								
31-59 days past due	-	247	52	-	-	54	-	353
60-89 days past due	-	-	-	-	-	24	-	24
Greater than 90 days past due	278	-	-	-	-	327	-	605
Total past due	278	247	52	-	-	405	-	982
Non-accrual loans	-	411	57	-	-	350	92	910
Total loans	$6,260	$ 19,525	$ 7,539	$ 37,519	$ 33,021	$ 18,745	$ 2,834	$125,443

Total loans either in non-accrual status or in excess of 90 days delinquent totaled $9.8 million or 1.3% of total loans outstanding at December 31, 2015, an increase from the total of $5.2 million or 0.9% of total loans outstanding at December 31, 2014.

The impaired loans for the years ended December 31, 2015 and 2014 are as follows:

	December 31, 2015							
(in thousands)	Construction & land	Residential first lien	Residential junior lien	Commercial owner occupied	Commercial non-owner occupied	Commercial loans and leases	Consumer loans	Total
Impaired loans:								
Legacy Loans:								
Recorded investment	$-	$ 631	$ 63	$ -	$ 2,838	$ 5,086	$ -	$8,618
With an allowance recorded	-	-	-	-	-	1,160	-	1,160
With no related allowance recorded	-	631	63	-	2,838	3,926	-	7,458
Related allowance	-	-	-	-	-	1,160	-	1,160
Unpaid principal	-	631	63	-	2,838	5,086	-	8,618
Average balance of impaired loans	-	622	74	-	3,417	7,198	-	11,311
Interest income recognized	-	29	-	-	119	284	-	432
Acquired Loans:								
Recorded investment	$-	$ 363	$ -	$ 232	$ 151	$ 1,728	$ 150	$2,624
With an allowance recorded	-	-	-	-	-	48	75	123
With no related allowance recorded	-	363	-	232	151	1,680	75	2,501
Related allowance	-	-	-	-	-	48	75	123
Unpaid principal	-	426	-	402	302	2,742	150	4,022
Average balance of impaired loans	-	444	-	197	63	901	106	1,711
Interest income recognized	-	8	-	8	-	3	6	25

	December 31, 2014							
(in thousands)	Construction & land	Residential first lien	Residential junior lien	Commercial owner occupied	Commercial non-owner occupied	Commercial loans and leases	Consumer loans	Total
Impaired loans:								
Legacy Loans:								
Recorded investment	$1,144	$ 308	$ -	$ -	$ 2,700	$ 2,073	$ -	$6,225
With an allowance recorded	334	-	-	-	-	690	-	1,024

With no related allowance recorded	810	308	-	-	2,700	1,383	-	5,201
Related allowance	60	-	-	-	-	483	-	543
Unpaid principal	1,144	308	-	-	2,700	2,127	-	6,279
Average balance of impaired loans	1,108	329	-	-	2,713	2,558	-	6,708
Interest income recognized	37	18	-	-	166	167	-	388
Acquired Loans:								
Recorded investment	$-	$ 411	$ 57	$ -	$ -	$ 405	$ 92	$965
With an allowance recorded	-	-	57	-	-	55	-	112
With no related allowance recorded	-	411	-	-	-	350	92	853
Related allowance	-	-	30	-	-	55	-	85
Unpaid principal	-	565	83	-	530	825	327	2,330
Average balance of impaired loans	-	568	83	-	560	829	379	2,419
Interest income recognized	-	-	-	-	-	-	-	-

Included in the total impaired loans above were non-accrual loans of $8.0 million and $4.0 million at December 31, 2015 and 2014, respectively. Interest income that would have been recorded if non-accrual loans had been current and in accordance with their original terms, was $345 thousand, $187 thousand and $154 thousand for the years ended December 31, 2015, 2014 and 2013, respectively.

The following table outlines the acquired impaired loans at December 31, 2015:

	December 31, 2015							
(in thousands)	Construction and land	Residential first lien	Residential junior lien	Commercial owner occupied	Commercial non-owner occupied	Commercial loans and leases	Consumer loans	Total
Acquired Impaired Loans:								
Substandard								
Contractual payment receivable	$-	$ -	$ -	$ 539	$ -	$ -	$ -	$539
Non-Accretable adjustment	-	-	-	-	-	-	-	-
Cash flow expected	-	-	-	539	-	-	-	539
Accretable yield	-	-	-	20	-	-	-	20
Loan receivable	$-	$ -	$ -	$ 519	$ -	$ -	$ -	$519
Doubtful								
Contractual payment receivable	$-	$ 426	$ -	$ 403	$ 302	$ 2,742	$ -	$3,873
Non-Accretable adjustment	-	18	-	125	125	793	-	1,061
Cash flow expected	-	408	-	278	177	1,949	-	2,812
Accretable yield	-	44	-	40	32	237	-	353
Loan receivable	$-	$ 364	$ -	$ 238	$ 145	$ 1,712	$ -	$2,459

	December 31, 2014							
(in thousands)	Construction and land	Residential first lien	Residential junior lien	Commercial owner occupied	Commercial non-owner occupied	Commercial loans and leases	Consumer loans	Total
Acquired Impaired Loans:								
Substandard								
Contractual payment receivable	$-	$ 553	$ -	$ -	$ -	$ -	$ -	$553
Non-Accretable adjustment	-	-	-	-	-	-	-	-
Cash flow expected	-	553	-	-	-	-	-	553
Accretable yield	-	7	-	-	-	-	-	7
Loan receivable	$-	$ 546	$ -	$ -	$ -	$ -	$ -	$546

Doubtful								
Contractual payment receivable	$-	$ 565	$ 83	$ -	$ 530	$ 825	$ 328	$2,331
Non-Accretable adjustment	-	50	11	-	530	329	198	1,118
Cash flow expected	-	515	72	-	-	496	130	1,213
Accretable yield	-	103	15	-	-	91	38	247
Loan receivable	$-	$ 412	$ 57	$ -	$ -	$ 405	$ 92	$966

The Company transferred in 2015 and 2014 one loan totaling $625 thousand and one loan totaling $95 thousand, respectively, net of reserves to other real estate owned (“OREO”). Management routinely evaluates OREO based upon periodic appraisals. In 2015 the Bank recorded an additional valuation allowance of $736 thousand in non-interest expense. In 2014 no valuation allowance was recorded and in 2013, the Bank recorded a valuation allowance of $347 thousand in non-interest expense for properties whose current appraised value was less than the carrying amount.

Loans may have their terms restructured (e.g., interest rates, loan maturity date, payment and amortization period, etc.) in circumstances that provide payment relief to a borrower experiencing financial difficulty. Such restructured loans are considered impaired loans that may either be in accruing status or non-accruing status. 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 they have performed based on all of the restructured loan terms.

The trouble debt restructured loans ("TDRs") at December 31, 2015 and December 31, 2014 are as follows:

	December 31, 2015				
(dollars in thousands)	Number of Loans	Non-Accrual Status	Number of Loans	Accrual Status	Total TDRs
Residential real estate - first lien	-	$ -	1	$ 301	$ 301
Commercial - non-owner occupied	1	594	1	2,073	2,667
Commercial loans and leases	-	-	1	7	7
Consumer	1	150	-	-	150
	2	$ 744	3	$ 2,381	$ 3,125

	December 31, 2014				
(dollars in thousands)	Number of Loans	Non-Accrual Status	Number of Loans	Accrual Status	Total TDRs
Residential real estate - first lien	1	$ 308	-	$ -	$ 308
Commercial loans	6	723	1	226	949
	7	$ 1,031	1	$ 226	$ 1,257

A summary of TDR modifications outstanding and performance under modified terms is as follows:

	December 31, 2015		
(in thousands)	Not Performing to Modified Terms	Performing to Modified Terms	Total TDRs
Residential real estate (RE) - first lien			
Forbearance	$ -	$ 301	$ 301
Commercial RE - non-owner occupied			
Rate modification	594	2,073	2,667
Commercial loans			
Extension or other modification	-	7	7
Consumer			
Extension or other modification	150	-	150
Total trouble debt restructure loans	$ 744	$ 2,381	$ 3,125

	December 31, 2014	
	Not Performing	Performing

(in thousands)	to Modified Terms	to Modified Terms	Total TDRs
Residential real estate - first lien			
Forbearance	$308	$ -	$308
Commercial loans			
Forbearance	723	-	723
Extension or other modification	-	226	226
Total trouble debt restructure loans	$1,031	$ 226	$1,257

There were four loans restructured in 2015 while two loans were restructured in 2014. Performing TDRs were in compliance with their modified terms and there are no further commitments associated with these credits.

Note 8: Goodwill and Other Intangible Assets

In the third quarter 2015 the Company initially recorded $1.1 million in goodwill relating to the Patapsco Bancorp acquisition. Subsequently, in the fourth quarter 2015 goodwill was adjusted to reflect the finalization of valuations for certain assets and liabilities associated with the filing of Patapsco Bancorp's final income tax returns. Goodwill is evaluated for impairment annually as of September 30 of each year or as events occur or circumstances change that would more-likely-than-not reduce the fair value below the carrying amount. Fair value is determined by using discounted cash flow analyses. Carrying value is determined using an equity allocation methodology considering both regulatory risk-based capital and tangible equity relative to tangible assets.

The Bank has one unit, which is the core banking operation. The table below shows goodwill balances at December 31, 2015. There was no goodwill at December 31, 2014.

(in thousands)	December 31 2015
Goodwill	
Banking	$ 603

Core deposit intangible is premiums paid for the acquisitions of core deposits, and are amortized based upon the estimated economic benefits received. The gross carrying amount and accumulated amortization of other intangible assets are as follows:

	December 31, 2015			Weighted
(in thousands)	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Average Remaining Life (Years)
Amortizing intangible assets:				
Core deposit intangible	$3,540	$ 637	$ 2,903	7.61

	December 31, 2014			Weighted
(in thousands)	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Average Remaining Life (Years)
Amortizing intangible assets:				
Core deposit intangible	$1,566	$ 175	$ 1,391	8.59

In 2015 the Bank recorded an additional $2.0 million in additional core deposit intangible associated with the Patapsco Bancorp acquisition. During 2014, we acquired additional core deposit intangible totaling $513 thousand for the Havre de Grace branch acquisition, and $677 thousand for the NBRS acqusition.

Estimated future amortizing expense for amortization intangibles within the years ending December 31, are as follows:

(in thousands)	
2016	$655
2017	506
2018	396
2018	314
2020	269
Thereafter	763
Total amortizing intangible assets	$2,903

Note 9: Premises and Equipment

Premises and equipment include the following at:

	December 31,	
(in thousands)	2015	2014
Land	$4,516	$2,850
Building and leasehold improvements	15,664	9,002
Furniture and equipment	5,065	3,823
Software	227	200
	25,472	15,875
Less: accumulated depreciation and amortization	4,707	3,753
Net premises and equipment	$20,765	$12,122

Depreciation and amortization expense for premises and equipment were $814 thousand, $734 thousand and $599 thousand for the years ended December 31, 2015, 2014 and 2013, respectively

The Company occupies banking and office space in 22 locations, 13 of which are under noncancellable lease arrangements accounted for as operating leases. The initial lease periods range from 5 to 20 years and provide for one or more renewal options. Rent expense applicable to operating leases amounted to $2.0 million, $1.4 million and $903 thousand for the years ended December 31, 2015, 2014 and 2013, respectively. Rental income from owned properties and subleases totaled $309 thousand, $307 thousand and $256 thousand for the years ended December 31, 2015, 2014 and 2013, respectively

Future minimum lease payments under noncancellable operating leases within the years ending December 31, having an initial term in excess of one year are as follows:

(in thousands)	
2016	$1,825
2017	1,768
2018	1,790
2019	1,483
2020	1,172
Thereafter	4,255
Total minimum lease payments	$12,293

Note 10: Deposits

The following table details the composition of deposits and the related percentage mix of total deposits, respectively:

(dollars in thousands)	December 31, **2015**			2014		
	Amount	% of Total	Weighted Average Rate	Amount	% of Total	Weighted Average Rate
Noninterest-bearing demand	$173,689	23 %	- %	$142,727	26 %	- %
Interest-bearing checking	54,014	7	0.21	49,988	9	0.24
Money market accounts	230,661	31	0.47	140,426	25	0.47
Savings	51,989	7	0.18	31,354	6	0.19
Certificates of deposit $100,000 and over	142,599	19	0.86	108,904	19	1.20
Certificates of deposit under $100,000	94,456	13	0.61	80,640	15	0.52
Total deposits	$747,408	100 %	0.55 %	$554,039	100 %	0.61 %

As of December 31, 2015 and December 31, 2014, time deposit accounts in excess of $250 thousand totaled $15.8 million and $18.7 million, respectively.

The following table presents the maturity schedule for time deposits maturing within years ending December 31:

(in thousands)	
2016	$157,206
2017	41,580
2018	14,502
2019	9,539
2020	14,228
Total time deposits	$237,055

Interest expense on deposits for the twelve months ended December 31, 2015, December 31, 2014 and December 31, 2013 was as follows

	December 31,		
(in thousands)	2015	2014	2013
Interest-bearing checking	$101	$83	$69
Savings and money market	880	581	368
Certificates of deposit $100,000 and over	1,086	917	719
Certificates of deposit under $100,000	544	498	500
Total	$2,611	$2,079	$1,656

Note 11: Short-Term Borrowings

Short-term borrowings consist of overnight unsecured master notes, overnight securities sold under agreement to repurchase and FHLB advances with a final remaining maturity of less than one year. Information relating to short-term borrowings at December 31, 2015 and December 31, 2014 is presented below:

	December 31,			
	2015		2014	
(dollars in thousands)	Amount	Rate	Amount	Rate
At period end	$69,121	0.44%	$48,628	0.23%
Average for the year	$46,893	0.33%	$39,326	0.27%
Maximum month-end balance	$69,121		$51,956	

The Company pledges U.S. Government Agency securities, based upon their fair value, as collateral for 100% of the principal and accrued interest of its repurchase agreements. At December 31, 2015 and 2014 there were $15.7 million

and $23.8 million, respectively, in borrowings under these agreements.

If the Company should need to supplement its liquidity, it could borrow, subject to collateral requirements, up to approximately $203.5 million on a line of credit arrangement with the FHLB. At December 31, 2015 and 2014 there were $78.5 million and $43.0 million, respectively, in advances outstanding under this arrangement. Total loans pledged as collateral towards short and long term borrowing was $248.6 million at December 31, 2015.

Note 12: Long-Term Borrowings

Long-term borrowings for the periods consisted of the following:

(in thousands)		December 31, 2015	2014
Federal Home Loan Bank Advances			
0.62% Due 2016	[1]	$-	$2,000
0.98% Due 2016	[1]	-	5,000
0.44% Due 2016	[1]	-	2,000
1.46% Due 2017	[1]	2,500	2,500
1.12% Due 2017	[1]	2,500	2,500
0.87% Due 2017	[1]	3,000	-
0.84% Due 2017	[1]	4,000	-
3.25% Due 2017	[2]	6,236	-
1.88% Due 2018	[1]	2,500	2,500
1.62% Due 2018	[1]	2,500	2,500
2.59% Due 2018	[3]	3,100	-
Junior subordinated debentures			
2.09% Due 2035	[4]	3,371	-
Total long-term borrowings		$29,707	$19,000

(1) Fixed rate advances

(2) Fixed rate hybrid advances

(3) Convertible to three-month LIBOR at the option of the FHLB. It is convertible on a quarterly basis upon written notice from the FHLB.

(4) Junior subordinated debt. Interest adjust quarterly at the rate of three month LIBOR plus 1.48%

Note 13: Income Taxes

Federal and state income tax expense consists of the following for the years ended:

(in thousands)	December 31, 2015	2014	2013
Current federal income tax	$3,998	$1,001	$780
Current state income tax	(15)	27	159
Deferred federal income tax	(2,832)	5,513	27

Deferred state income tax	(178)	312	18
Total income tax expense	$973	$6,853	$984

A reconciliation of the statutory federal income tax rate to the Company's effective tax rate for the years ended follows:

	December 31,		
(in thousands)	2015	2014	2013
Statutory federal income tax rate	34.0%	34.0%	34.0%
State income taxes, net of federal income tax expense	5.9	5.3	4.0
Bank owned life insurance	(6.5)	(0.7)	(3.3)
Acqusition related costs	10.7	-	-
Other, net	1.9	1.1	(1.3)
Effective tax rate	46.0%	39.7%	33.4%

The following table is a summary of the tax effect of temporary differences that give rise to a significant portion of deferred tax assets and liabilities:

	December, 31	
(in thousands)	2015	2014
Deferred tax assets:		
Net operating loss	$1,227	$-
Allowance for credit losses	1,298	621
Valuation on foreclosed real estate	1,126	836
Supplemental executive benefit plans	547	247
Stock-based compensation	34	86
Deferred loan fees and costs, net	111	185
Unrealized loss on securities	19	10
Other assets	282	65
Total deferred tax assets	4,644	2,050
Deferred tax liabilities:		
Acquisition activity	5,344	6,259
Fair value	741	343
Depreciation and amortization	226	134
Total deferred tax liabilities	6,311	6,736
Net deferred tax liabilities	$(1,667)	$(4,686)

Note 14: Related Party Loans

In the normal course of business, loans are made to officers and directors of the Company, as well as to their related interests. In the opinion of management, these loans are consistent with sound banking practices, are within regulatory lending limitations and do not involve more than the normal risk of collectability.

Total outstanding balances to the Company’s executive officers, directors and their related interests at are presented below.

	December 31,	
(in thousands)	2015	2014
Balance January 1	$13,873	$18,620
Additions	6,034	2,215
Change in director status	(3,035)	(2,456)
Repayments	(2,543)	(4,506)
Balance December 31	$14,329	$13,873

In addition to the outstanding balances above, total unfunded commitments to these parties at December 31, 2015 and December 31, 2014 were $1.2 million and $1.6 million, respectively. The Bank also routinely enters into deposit relationships with its officers and directors in the normal course of business. These deposit accounts bear the same terms and conditions for comparable deposit accounts of unrelated parties.

Note 15: Financial Instruments with Off-Balance Sheet Risk

The Company is a party to financial instruments with off-balance sheet risk in the normal course of business. These financial instruments may include commitments to extend credit, standby letters of credit and purchase commitments. The Company uses these financial instruments to meet the financing needs of its customers. Financial instruments involve, to varying degrees, elements of credit, interest rate, and liquidity risk. These do not represent unusual risks, and management does not anticipate any losses which would have a material effect on the accompanying financial statements.

Outstanding loan commitments and lines and letters of credit are as follows:

	December 31,	
(in thousands)	2015	2014
Unfunded loan commitments	$95,009	$64,375
Unused lines of credit	72,664	50,889
Letters of credit	7,848	12,397

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. The Company generally requires collateral to support financial instruments with credit risk on the same basis as it does for on-balance sheet instruments. The collateral is based on management's credit evaluation of the counterparty. Commitments 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 commitment amount does not necessarily represent future cash requirements. Each customer's credit-worthiness is evaluated on a case-by-case basis.

Standby letters of credit are conditional commitments issued to guarantee the performance of a customer to a third party.

Note 16: Stock Options and Other Equity Awards

The Company's equity incentive plans provide for awards of nonqualified and incentive stock options as well as vested and non-vested common stock awards. Employee stock options can be granted with exercise prices at the fair market value (as defined within the plan) of the stock at the date of grant and with terms of up to ten years. Except as otherwise permitted in the plan, upon termination of employment for reasons other than retirement, permanent

disability or death, the option exercise period is reduced or the options are canceled.

Stock awards may also be granted to non-employee members of the Board of Directors as compensation for attendance and participation at meetings of the Board of Directors and meetings of the various committees of the Board. In 2015 and 2014, the Company issued 7,163 and 5,358 shares of stock, respectively, to directors as compensation for their service.

The following table summarizes the Company's stock option activity and related information for the years ended:

	December 31, 2015		December 31, 2014	
	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price
Balance at January 1,	264,652	$ 11.75	387,101	$ 11.19
Granted	-	-	-	-
Exercised	(62,287)	10.48	(4,139)	8.79
Forfeited	(64,902)	11.83	(118,310)	10.02
Balance at period end	137,463	$ 12.30	264,652	$ 11.75
Exercisable at period end	137,463	$ 12.30	264,652	$ 11.75
Weighted average fair value of options granted during the year		$ -		$ -

The intrinsic value of a stock option is the amount that the market value of the underlying stock exceeds the exercise price of the option. Based upon a fair market value of $13.24 on December 31, 2015 the options outstanding had an aggregate intrinsic value of $185 thousand.

Restricted Stock

In the second quarter of 2013, 50,000 shares of restricted stock were granted, with 30,000 of the shares subject to a three year vesting schedule with one third of the shares vesting each year on the grant date anniversary. The remaining 20,000 awarded shares also are subject to a three year vesting schedule, however they only vest if certain annual performance measures are satisfactorily achieved.

A summary of the activity for the Company's restricted stock for the period indicated is presented in the following table:

	December 31, 2015		December 31, 2014	
	Shares	Weighted Average Grant Date Fair Value	Shares	Weighted Average Grant Date Fair Value
Balance at January 1,	33,330	$ 6.89	50,000	$ 6.89
Granted	-	-	-	-
Vested	(18,336)	6.89	(10,002)	6.91
Forfeited	(6,664)	6.85	(6,668)	6.85
Balance at period end	8,330	$ 6.92	33,330	$ 6.89

At December 31, 2015, based on restricted stock awards outstanding at that time, the total unrecognized pre-tax compensation expense related to unvested restricted stock awards was $14 thousand. This expense is expected to be recognized in 2016.

Restricted Stock Units

Restricted stock units (RSUs) are similar to restricted stock, except the recipient does not receive the stock immediately, but instead receives it according to a vesting plan and distribution schedule after achieving required performance milestones or upon remaining with the employer for a particular length of time. Each RSU that vests entitles the recipient to receive one share of common stock on a specified issuance date. The recipient does not have any stockholder rights, including voting, dividend or liquidation rights, with respect to the shares underlying awarded RSUs until the recipient becomes the record holder of those shares.

During 2015, 73,500 RSUs were granted, with 43,500 of the RSUs subject to a three year vesting schedule with one-third of the RSUs vesting each year on the grant date anniversary. The remaining 30,000 awarded RSUs also are subject to a three year vesting schedule; they only vest, however, if certain annual performance measures are satisfactorily achieved.

In 2014, 44,500 RSUs were granted, with 19,500 of the RSUs subject to a three year vesting schedule with one-third of the RSUs vesting each year on the grant date anniversary. The remaining 25,000 awarded RSUs also are subject to a three year vesting schedule; they only vest, however, if certain annual performance measures are satisfactorily achieved.

A summary of the activity for the Company's RSUs for the periods indicated is presented in the following table:

	December 31, 2015		December 31, 2014	
	Shares	Weighted Average Grant Date Fair Value	Shares	Weighted Average Grant Date Fair Value
Balance at January 1,	44,500	$ 11.21	-	$ -
Granted	73,500	14.00	44,500	11.21
Vested	(19,836)	11.64	-	-
Forfeited	(23,336)	(12.84)	-	-
Balance at period ended	74,828	$ 13.23	44,500	$ 11.21

At December 31, 2015, based on RSU awards outstanding at that time, the total unrecognized pre-tax compensation expense related to unvested RSU awards was $832 thousand. This expense is expected to be recognized through 2018.

Stock-Based Compensation Expense: Stock-based compensation is recognized as compensation cost in the statement of operations based on their fair values on the measurement date, which, for the Company, is the date of the grant. The Company recognized stock-based compensation expense related to the issuance of restricted stock and RSUs of $375 thousand as well as $95 thousand for director compensation paid in stock for the year ended December 31, 2015; RSUs of $226 thousand as well as $54 thousand for director compensation paid in stock for the year ended December 31, 2014; and stock-based compensation expense $123 thousand during 2013.

Valuation of Stock-Based Compensation: The fair value of the Company's stock options granted as compensation is estimated on the measurement date, which, for the Company, is the date of grant. The fair value of stock options was calculated using the Black-Scholes option-pricing model. There were no stock options granted in 2015 or 2014. The Company estimated expected market price volatility and expected term of the options based on historical data and other factors.

Note 17: Benefit Plans

Profit Sharing Plan

The Company sponsors a defined contribution retirement plan through a Section 401(k) profit sharing plan. Employees may contribute up to 15% of their pretax compensation. Participants are eligible for matching Company contributions up to 4% of eligible compensation dependent on the level of voluntary contributions. Company matching contributions totaled $520 thousand, $301 thousand and $147 thousand, respectively, for the years ended December 31, 2015, 2014 and 2013. The Company's matching contributions vest immediately.

Supplemental Executive Retirement Plan (SERP)

In 2014, the Bank created a SERP for the Chief Executive Officer. This plan was amended in 2015. Under defined benefit SERP, Ms. Scully will receive $150,000 each year for 15 years after attainment of the Normal Retirement Age (as defined in the SERP). Ms. Scully will earn vesting on a graduated schedule in which she will become fully vested on August 25, 2019, which has been established for purposes of the SERP as her retirement date. Expense related to this plan totaled $90 thousand and $625 thousand for 2015 and 2014, respectively.

Note 18: Income per Common Share

The table below shows the presentation of basic and diluted income (loss) per common share for the years ended:

	December 31,		
(dollars in thousands, except per share data)	2015	2014	2013
Net income (loss)	$1,142	$10,412	$1,961
Preferred stock dividends	(126)	(126)	(165)
Net income (loss) available to common shareholders (numerator)	$1,016	$10,286	$1,796
BASIC			
Basic average common shares outstanding (denominator)	6,160,005	4,073,077	4,036,291

Basic income (loss) per common share	$0.16	$2.53	$0.44
DILUTED			
Average common shares outstanding	6,160,005	4,073,077	4,036,291
Dilutive effect of common stock equivalents	101,556	81,203	40,179
Diluted average common shares outstanding (denominator)	6,261,561	4,154,280	4,076,470
Diluted income (loss) per common share	$0.16	$2.48	$0.44
Common stock equivalents outstanding that are anti-dilutive and thus excluded from calculation of diluted number of shares presented above	78,861	110,463	479,971

Note 19: Regulatory Matters

The Bank is subject to various regulatory capital requirements administered by the FDIC. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Company's and the Bank's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the 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 classifications are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

In July 2013, the FDIC and the other federal bank regulatory agencies issued a final rule that revised their leverage and risk-based capital requirements and the method for calculating risk-weighted assets to make them consistent with agreements that were reached by the Basel Committee on Banking Supervision ("Basel III") and certain provisions of the Dodd-Frank Act. The final rule, which became effective on January 1, 2015, applies to all depository institutions, top-tier bank holding companies with total consolidated assets of $1 billion or more and top-tier savings and loan holding companies. The Company will become subject to the final rule as administered by the Federal Reserve Board if and when the Company reaches $1 billion in total consolidated assets. The final rule creates a new common equity Tier 1 ("CET1") minimum capital requirement (4.5% of risk-weighted assets), increases the minimum Tier 1 capital ratio (from 4% to 6% of risk-weighted assets), imposes a minimum leverage ratio of 4.0%, and changes the risk-weight of certain assets to better reflect credit risk and other risk exposures. These include, among other things, a 150% risk weight for certain high volatility commercial real estate acquisition, development and construction loans and for non-residential mortgage loans that are 90 days past due or otherwise in non-accrual status, and a 20% credit conversion factor for the unused portion of a commitment with an original maturity of one year or less that is not unconditionally cancellable. The final rule also requires unrealized gains and losses on certain "available-for-sale" securities holdings to be included for purposes of calculating regulatory capital unless Howard Bank elects to opt-out from this treatment. The Bank has elected to permanently opt out of this treatment in our capital calculations, as permitted by the final rule.

The final rule will limit Howard Bank's capital distributions and certain discretionary bonus payments if Howard Bank does not hold a "capital conservation buffer" consisting of 2.5% of common equity Tier 1 capital to risk-weighted assets in addition to the amount necessary to meet its minimum risk-based capital requirements. The capital conservation buffer requirement will be phased in beginning January 1, 2016 and ending January 1, 2019, when the full capital conservation buffer requirement will be effective.

In addition, under revised prompt corrective action requirements effective January 1, 2015, in order to be considered "well-capitalized," Howard Bank must have a CET1 risk-based capital ratio of 6.5% or greater, a Tier 1 risk-based capital ratio of 8.0% or greater, a total risk-based capital ratio of 10.0% or greater and a leverage ratio of 5.0% or greater.

There are two main categories of capital under the regulatory capital guidelines. Tier 1 capital includes common shareholders' equity, qualifying preferred stock and trust preferred securities, less goodwill and certain other deductions (including the unrealized net gains and losses, after applicable income taxes, on securities available for sale carried at fair value). Tier 2 capital includes preferred stock not qualifying as Tier 1 capital, subordinated debt, the allowance for credit losses and net unrealized gains on marketable equity securities, subject to limitations by the guidelines. Tier 2 capital is limited to the amount of Tier 1 capital (i.e., at least half of total capital must be in the form of Tier 1 capital). Under the guidelines, capital is compared to the relative risk related to the balance sheet. To derive the risk included in the balance sheet, one of several risk weights is applied to the different balance sheet and off-balance sheet assets, primarily based on the relative credit risk of the counterparty. For example, claims guaranteed by the U.S. government or one of its agencies are risk-weighted at 0%. Off-balance sheet items, such as loan commitments, are also applied a risk weight after calculating balance sheet equivalent amounts. One of four credit conversion factors (0%, 20%, 50% and 100%) is assigned to loan commitments based on the likelihood of the off-balance sheet item becoming an asset. For example, certain loan commitments are converted at 50% and then

risk-weighted at 100%. The capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

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

Management believes that, as of December 31, 2015 and 2014, the Bank met all capital adequacy requirements to which it is subject.

(dollars in thousands)	Actual Amount	Ratio	For capital adequacy purposes Amount	Ratio	To be well capitalized under the FDICIA prompt corrective action provisions Amount	Ratio
As of December 31, 2015:						
Total capital (to risk-weighted assets)						
Howard Bank	$87,860	11.07%	$ 63,482	8.00 %	$79,353	10.00 %
Howard Bancorp	$95,737	12.09%	$ 63,370	8.00 %	**N/A**	
Common equity tier 1 capital (to risk-weighted assets)						
Howard Bank	$82,991	10.46%	$ 35,709	4.50 %	$51,579	6.50 %
Howard Bancorp	$90,868	11.47%	$ 35,646	4.50 %	**N/A**	
Tier 1 capital (to risk-weighted assets)						
Howard Bank	$82,991	10.46%	$ 47,612	6.00 %	$63,482	8.00 %
Howard Bancorp	$90,868	11.47%	$ 47,528	6.00 %	**N/A**	
Tier 1 capital (to average assets) (Leverage ratio)						
Howard Bank	$82,991	9.04 %	$ 36,703	4.00 %	$45,879	5.00 %
Howard Bancorp	$90,868	9.90 %	$ 36,710	4.00 %	**N/A**	
As of December 31, 2014:						
Total capital (to risk-weighted assets)						
Howard Bank	$61,393	10.69%	$ 45,932	8.00 %	$57,415	10.00 %
Howard Bancorp	$61,811	10.73%	$ 46,067	8.00 %	N/A	
Tier 1 capital (to risk-weighted assets)						
Howard Bank	$57,791	10.07%	$ 22,966	4.00 %	$34,449	6.00 %
Howard Bancorp	$58,208	10.11%	$ 23,033	4.00 %	N/A	
Tier 1 capital (to average assets) (Leverage ratio)						
Howard Bank	$57,791	8.54 %	$ 27,073	4.00 %	$33,842	5.00 %
Howard Bancorp	$58,208	8.60 %	$ 27,072	4.00 %	N/A	

Note 20: Preferred Stock

On September 22, 2011, we entered into a Securities Purchase Agreement with the Secretary of the Treasury, pursuant to which Bancorp issued and sold to the Treasury 12,562 shares of our Senior Non-Cumulative Perpetual Preferred Stock, Series AA, having a liquidation preference of $1,000 per share, for aggregate proceeds of $12,562,000. The issuance was pursuant to the Treasury's Small Business Lending Fund (SBLF) program, a $30 billion fund established under the Small Business Jobs Act of 2010, which encourages lending to small businesses by providing capital to qualified community banks with assets of less than $10 billion. The Series AA Preferred Stock holders are entitled to receive non-cumulative dividends payable quarterly on each January 1, April 1, July 1 and October 1, beginning October 1, 2011. The dividend rate, which is calculated on the aggregate Liquidation Amount, was initially set at 5% per annum based upon the then-current level of "Qualified Small Business Lending" ("QSBL") by the Bank and is currently set at 1%. The dividend rate for each dividend period may vary and is set based upon the percentage change in qualified lending between each dividend period and the baseline QSBL level established at the time the Agreement

was entered into. Such dividend rate may vary from 1% per annum to 5% per annum for the second through tenth dividend periods and from 1% per annum to 7% per annum for the eleventh through the eighteenth dividend periods and though March 22, 2016 with respect to the nineteenth dividend period. If the Series AA Preferred Stock remains outstanding for more than four-and-one-half years, the dividend rate will be fixed at 9%. Prior to that time, in general, the dividend rate decreases as the level of the Bank's QSBL increases. Such dividends are not cumulative, but Bancorp may only declare and pay dividends on its common stock (or any other equity securities junior to the Series AA Preferred Stock) if it has declared and paid dividends for the current dividend period on the Series AA Preferred Stock, and will be subject to other restrictions on its ability to repurchase or redeem other securities. In addition, if we have not timely declared and paid dividends on the Series AA Preferred Stock for six dividend periods or more, whether or not consecutive, the Treasury (or any successor holder of Series AA Preferred Stock) may designate a representative to attend all meetings of Bancorp's Board of Directors in a nonvoting observer capacity and Bancorp must give such representative copies of all notices, minutes, consents and other materials that Bancorp provide to its directors in connection with such meetings.

We may redeem the shares of Series AA Preferred Stock, in whole or in part, at any time at a redemption price equal to the sum of the Liquidation Amount per share and the per-share amount of any unpaid dividends for the then-current period, subject to any required prior approval by our primary federal banking regulator.

Note 21: Fair Value

FASB ASC Topic 820 “Fair Value Measurements” defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. FASB ASC Topic 820 also establishes a fair value hierarchy, which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value.

The Company utilizes fair value measurements to record fair value adjustments to certain assets and to determine fair value disclosures. Securities available for sale are recorded at fair value on a recurring basis. Additionally, from time to time, the Company may be required to record at fair value other assets on a nonrecurring basis, such as loans held for investment and certain other assets. These nonrecurring fair value adjustments typically involve application of lower of cost or market accounting or write-downs of individual assets.

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

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

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

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

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

Recurring Fair Value Measurements

All classes of investment securities available for sale are recorded at fair value using reliable an unbiased evaluations by an industry wide valuation service and therefor fall into a Level 2 of the fair value hierarchy. The service uses evaluated pricing models that vary based on asset class and include available trade, bid and other market information. Various methodologies include broker quotes, propriety models, descriptive terms and conditions databases, and quality control programs.

Fair value of loans held for sale is based upon outstanding investor commitments or, in the absence of such commitments, based on current investor yield requirements or third party pricing models and are considered Level 2. Gains and losses on loans sales are determined using specific identification method. Changes in fair value are recognized in the Consolidated Statement of Operations as part of realized and unrealized gain on mortgage banking activities.

Interest rate lock commitments are recorded at fair value determined as the amount that would be required to settle each of these derivatives at the balance sheet date. In the normal course of business, the Company enters into contractual interest rate lock commitments to extend credit to borrowers with fixed expiration dates. The commitment becomes effective when the borrowers lock in a specified interest rate within the time frames established by the mortgage division. All borrowers are evaluated for credit worthiness prior to the extension of the commitment. Market risk arises if interest rates move adversely between the time interest rate is locked by the borrower and the sale date of the loan to an investor. To mitigate this interest rate risk inherent in providing rate lock comments to borrowers, the Company enters in best effort forward sales contracts to sell loans to investors. The forward sales contracts lock in an interest rate price for the sale of loans similar to the specific rate lock commitment. Rate lock commitments to the borrowers through to the date the loan closes are undesignated derivatives and accordingly, are marked to fair value in earnings. These valuations fall into a Level 2 of the fair value hierarchy.

Non-recurring Fair Value Measurements

Level 3 is for positions that are not traded in active markets or are subject to transfer restrictions, valuations are adjusted to reflect illiquidity and/or non-transferability, and such adjustments are generally based on available market evidence. In the absence of such evidence, management's best estimate is used.

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

Other real estate owned acquired through, or in lieu of, foreclosure are held for sale and are initially recorded at the lower of cost or fair value, less selling costs. Any write-downs to fair value at the time of transfer to OREO are charged to the allowance for credit losses subsequent to foreclosure. Values are derived from appraisals of underlying collateral and discounted cash flow analysis. Valuation losses due to reductions in appraised values on OREO of $736 thousand, $0 and $347 thousand were recognized for years ended December 31, 2015, 2014 and 2013, respectively. These charges were for declines in the value of OREO subsequent to foreclosure. OREO is classified within Level 3 of the hierarchy.

The following table sets forth the Company's financial assets and liabilities that were accounted for or disclosed at fair value on a recurring basis at December 31, 2015 and December 31, 2014.

December 31, 2015		Quoted Price in Active Markets	Significant Other	Significant
	Carrying Value	for Identical Assets	Observable Inputs	Unobservable Inputs
(in thousands)	(Fair Value)	(Level 1)	(Level 2)	(Level 3)
Investment securities:				
U.S. Government agencies	$ 48,422	$ -	$ 48,422	$ -
Mortgage-backed securities	57	-	57	-
Other investments	1,094	-	1,094	-
Loans held for sale	49,677	-	49,677	-

Rate lock commitments	508	-	508	-

December 31, 2014 (in thousands)	Carrying Value (Fair Value)	Quoted Price in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Investment securities:				
U.S. Government agencies	$ 36,981	$ -	$ 36,981	$ -
U.S. Government treasuries	3,997	-	3,997	-
Mortgage-backed securities	101	-	101	-
Loans held for sale	42,881	-	42,881	-
Rate lock commitments	342	-	342	-

Assets under fair value option:

December 31, 2015 (in thousands)	Carrying Fair Value Amount	Aggregate Unpaid Principal	Difference
Loans held for sale	$ 49,677	$ 48,395	$ 1,282

December 31, 2014 (in thousands)	Carrying Fair Value Amount	Aggregate Unpaid Principal	Difference
Loans held for sale	$ 42,881	$ 41,668	$ 1,213

There were no loans held for sale that were nonaccrual or 90 days or more past due and still accruing interest at December 31, 2015. Net gain from the changes included in earnings in fair value of loans held for sale was $69 thousand and $1.2 million at December 31, 2015 and 2014, respectively.

The following table sets forth the Company's financial assets and liabilities that were accounted for or disclosed at fair value on a nonrecurring basis as of December 31, 2015 and December 31, 2014. OREO is carried at fair value less anticipated costs to sell. Impaired loans are measured using the fair of collateral, if applicable.

December 31, 2015 (in thousands)	Carrying Value (Fair Value)	Quoted Price in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Other real estate owned	$ 2,369	$ -	$ -	$ 2,369
Impaired loans:				
Construction and land	-	-	-	-
Residential - first lien	694	-	-	694
Residential - junior lien	364	-	-	364
Commercial - owner occupied	232	-	-	232
Commercial - non-owner occupied	2,989	-	-	2,989
Commercial loans and leases	5,604	-	-	5,604
Consumer	75	-	-	75

December 31, 2014	Carrying Value	Quoted Price in Active Markets for Identical Assets	Significant Other Observable Inputs	Significant Unobservable Inputs

(in thousands)	(Fair Value)	(Level 1)	(Level 2)	(Level 3)
Other real estate owned	$ 2,472	$ -	$ -	$ 2,472
Impaired loans:				
Construction and land	1,084	-	-	1,084
Residential - first lien	719	-	-	719
Residential - junior lien	27	-	-	27
Commercial - owner occupied	-	-	-	-
Commercial - non-owner occupied	2,700	-	-	2,700
Commercial loans and leases	1,940	-	-	1,940
Consumer	92	-	-	92

At December 31, 2015 OREO consisted of an outstanding balance of $5.2 million, less valuation allowance of $2.9 million. At December 31, 2014 OREO consisted of an outstanding balance of $4.6 million, less valuation allowance of $2.1 million. Related allowance on impaired loans for the year ended 2015 and 2014 were $1.3 million and $0.6 million, respectively.

Various techniques are used to valuate OREO and impaired loans. All loans for which the underlying collateral is real estate, either Construction, Land, Commercial, or Residential, an independent appraisal is used to identify the value of the collateral. The approaches within the appraisal report include sales comparison, income, and replacement cost analysis. The resulting value will be adjusted by a selling cost of 9.5% and the residual value will be used to determine if there is an impairment. Commercial loans and leases and consumer utilize a liquidation approach to the impairment analysis.

The following table presents required information in accordance with ASC Topic 825 “Financial Instruments” December 31, 2015 and 2014. The fair value of a financial instrument is the amount at which the instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale. Fair value estimates are based on quoted market prices where available or calculated using present value techniques. Since quoted market prices are not available on many of our financial instruments, estimates may be based on the present value of estimated future cash flows and estimated discount rates. These financial assets and liabilities have not been recorded at fair value:

The following methods and assumptions were used to estimate the fair value of financial instruments where it is practical to estimate fair value:

Securities available-for-sale: Based on quoted market prices. If quoted market price is not available fair value is estimated using quoted market prices for similar securities.

Nonmarketable equity securities: Because these securities are not marketable, the carrying amount approximates the fair value.

Loans held for sale: Loans held for sale are carried at fair value. Based on outstanding investor commitments or, in absent of such commitments, based on current investor yield requirements on third party models.

Derivative financial instruments: Based on estimate loan closing and investor delivery rate based on historical experience.

Loans: For variable rate loans the carrying amount approximates the fair value. For fixed rate loans the fair value is calculated by discounting estimated cash flows using current rates at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturities. The estimated cash flows do not anticipate prepayments.

Deposits: The carrying amount of non-maturity deposits such as demand deposits, money market and saving deposits approximates the fair value. The fair value of deposits with predetermined maturity dates such as certificate of deposits is estimated by discounting the future cash flows using current rates of similar deposits with similar remaining maturities.

Short-term borrowing: Variable rate repurchase agreements carrying amounts approximate the fair values at the reporting date.

Long-term borrowing: Because the borrowing is a variable rate instrument, the carrying amount approximates the fair value.

Management has made estimates of fair value discount rates that it believes to be reasonable. However, because there is no market for many of these financial instruments, management has no basis to determine whether the fair value presented for loans would be indicative of the value negotiated in an actual sale.

The following table presents the estimated fair value of the Company's financial instruments for the periods indicated:

	December 31, 2015				
(in thousands)	Carrying Amount	Fair Value	Quoted Price in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Financial Assets					
Investment securities	$49,573	$49,573	$ -	$ 49,573	$ -
Nonmarketable equity securities	4,163	4,163	-	4,163	-
Loans held for sale	49,677	49,677	-	49,677	-
Rate lock commitments	508	508	-	508	-
Loans and leases	755,133	760,562	-	-	760,562
Financial Liabilities					
Deposits	747,408	747,938	-	-	747,938
Short-term borrowings	69,121	69,121	-	69,121	-
Long-term borrowings	29,707	29,911	-	29,911	-

	December 31, 2014				
(in thousands)	Carrying Amount	Fair Value	Quoted Price in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Financial Assets					
Investment securities	$41,079	$41,079	$ -	$ 41,079	$ -
Nonmarketable equity securities	2,571	2,571	-	2,571	-
Loans held for sale	42,881	42,881	-	42,881	-
Rate lock commitments	342	342	-	342	-
Loans and leases	549,315	547,825	-	-	547,825
Financial Liabilities					
Deposits	554,039	554,660	-	-	554,660
Short-term borrowings	48,628	48,628	-	48,628	-
Long-term borrowings	19,000	19,055	-	19,055	-

Note 22: Parent Company Financial Information

The condensed financial statement for Bancorp (Parent Only) is presented below:

Howard Bancorp, Inc.

Balance Sheets

(in thousands)	December 31, 2015	2014
ASSETS		
Cash and cash equivalents	$12,432	$1,356
Securities available-for-sale, at fair value	100	-
Investment in subsidiaries	85,049	59,166
Other assets	141	71
Total assets	$97,722	$60,593
LIABILITIES		
Short-term borrowings	$890	$874
Long-term borrowings	3,371	-
Other Liabilities	562	76
Total liabilities	4,823	950
SHAREHOLDERS' EQUITY		
Preferred stock—par value $0.01 (liquidation preference of $1,000 per share) authorized 5,000,000; shares issued and outstanding 12,562 series AA at December 31, 2015 and December 31, 2014	12,562	12,562
Common stock - par value of $0.01 authorized 10,000,000 shares; issued and outstanding 6,962,139 shares at December 31, 2015 and 4,145,547 at December 31, 2014	70	41
Capital surplus	70,587	38,360
Retained earnings	9,712	8,696
Accumulated other comprehensive loss	(32)	(16)
Total shareholders’ equity	92,899	59,643
Total liabilities and shareholders’equity	$97,722	$60,593

Statements of Operations

	December 31,		
(in thousands)	2015	2014	2013
INTEREST INCOME			
Interest on securities	$-	$-	$-
Interest and fees on loans	-	-	11
Other interest income	4	-	-
INTEREST EXPENSE			
Short-term borrowings	6	6	5
Long-term borrowings	46	-	-
NET INTEREST EXPENSE	(48)	(6)	6
Provision for credit losses	-	-	(3)
Net interest expense after provision for credit losses	(48)	(6)	9
NONINTEREST EXPENSE			
Compensation and benefits	339	192	86
Other operating expense	119	228	223
Total noninterest expense	458	420	309
Loss before income tax and equity in undistributed loss of subsidiary	(506)	(426)	(300)
Income tax benefit	(172)	(145)	-
Loss before equity in undistributed income of subsidiary	(334)	(281)	(300)
Equity in undistributed income of subsidiary	1,476	10,693	2,261
Net income	$1,142	$10,412	$1,961
Preferred stock dividends	126	126	165
Net income available to common shareholders	$1,016	$10,286	$1,796

Statements of Cash Flows

	Year Ended December 31,		
(in thousands)	2015	2014	2013
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net income	$1,142	$10,412	$1,961
Adjustments to reconcile net income to net cash used by operating activities:			
Provision for credit losses	-	-	(3)
Deferred income taxes (benefits)	519	1	-
Share-based compensation	436	246	124
Equity in undistributed income of subsidiary	(1,476)	(10,693)	(2,245)
Increase in other assets	(86)	(3)	(22)
(Decrease) increase in other liabilities	(33)	4	(109)
Net cash used in operating activities	502	(33)	(294)
CASH FLOWS FROM INVESTING ACTIVITIES:			
Net decrease in loans outstanding	-	-	250
Purchase of investment securities available-for-sale	(100)	-	-
Cash and cash equivalents of acquisition	10,064	-	-
Cash paid for acquisition	(2,015)	-	-
Investment in subsidiary	(24,407)	(750)	(8,500)
Net cash used in investing activities	(16,458)	(750)	(8,250)
CASH FLOWS FROM FINANCING ACTIVITIES:			
Net increase (decrease) increase in short-term borrowings	16	(107)	605
Proceeds from issuance of long-tern debt	3,371	-	-
Net proceeds from issuance of common stock, net of cost	23,771	507	-
Cash dividends on preferred stock	(126)	(126)	(165)
Net cash provided by financing activities	27,032	274	440
Net increase (decrease) in cash and cash equivalents	11,076	(509)	(8,104)
Cash and cash equivalents at beginning of period	1,356	1,865	9,969
Cash and cash equivalents at end of period	$12,432	$1,356	$1,865

Note 23: Quarterly Financial Results (unaudited)

The following table provides a summary of selected consolidated quarterly financial data for the years ended December 31, 2015 and December 31, 2014:

	2015			
(in thousands, except per share data.)	Fourth Quarter	Third Quarter	Second Quarter	First Quarter
Interest income	$9,950	$8,489	$7,484	$7,426
Interest expense	920	808	685	659
Net interest income	9,030	7,681	6,799	6,767
Provision for loan losses	821	230	535	250
Noninterest income	2,883	3,257	3,438	2,349
Noninterest expense	10,378	11,600	8,440	7,835
Net income before income taxes	714	(892)	1,262	1,031
Income tax expenses	226	(106)	471	382
Net income	488	(786)	791	649
Preferred stock dividends	32	31	31	32
Net income available to common shareholders	$456	$(817)	$760	$617
Net income per common share, basic	$0.07	$(0.13)	$0.16	$0.15
Net income per common share, diluted	$0.06	$(0.13)	$0.15	$0.15

	2014			
(in thousands, except per share data.)	Fourth Quarter	Third Quarter	Second Quarter	First Quarter
Interest income	$7,207	$5,813	$5,397	$4,943
Interest expense	671	648	568	515
Net interest income	6,536	5,165	4,829	4,428
Provision for loan losses	686	2,068	325	176
Noninterest income	18,399	2,175	2,059	623
Noninterest expense	8,891	4,961	5,349	4,493
Net income before income taxes	15,358	311	1,214	382
Income tax expenses	6,185	75	477	116
Net income	9,173	236	737	266
Preferred stock dividends	32	31	32	31
Net income available to common shareholders	$9,141	$205	$705	$235
Net income per common share, basic	$2.23	$0.05	$0.17	$0.06
Net income per common share, diluted	$2.18	$0.05	$0.17	$0.06

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosures

None

Item 9A. Controls and Procedures

As required by SEC rules, the Company’s Chief Executive Officer and Chief Financial Officer evaluated the effectiveness of the Company’s disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) as of December 31, 2015. Based on this evaluation, the Company’s Chief Executive Officer and Chief Financial Officer concluded that the Company’s disclosure controls and procedures were effective as of December 31, 2015.

No changes in the Company’s internal control over financial reporting occurred during the fourth quarter of 2015 that have materially affected, or are reasonably likely to materially affect, the Company’s internal control over financial reporting.

Management’s Report On Internal Control Over Financial Reporting

Company management is responsible for establishing and maintaining adequate internal control over financial reporting for the Company. The internal control over financial reporting has been designed under our supervision to provide reasonable assurance regarding the reliability of financial reporting and the preparation of the Company’s consolidated financial statements for external reporting purposes in accordance with accounting principles generally accepted in the United States of America.

Management has conducted an assessment of the effectiveness of the Company’s internal control over financial reporting as of December 31, 2015, utilizing the framework established in Internal Control-Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this assessment, management has determined that the Company’s internal control over financial reporting as of December 31, 2015, is effective.

Item 9B. Other Information

None

Part III

Item 10. Directors, Executive Officers and Corporate Governance

The Company has adopted a code of ethics (conduct) that applies to all of its employees and a separate code of ethics (conduct) that applies to its non-employee directors. These codes of conduct are available on the Company’s Internet Web site at www.howardbank.com. There have been no material changes in the procedures previously disclosed by which shareholders may recommend nominees to the Company's Board of Directors.

The remainder of the information required by this Item is incorporated by reference to the information included under the captions “Election of Directors,” “Committees and Meetings of the Board of Directors; Corporate Governance,” “Executive Officers who are not Directors” and “Section 16(a) Beneficial Ownership Reporting Compliance” in the Company’s definitive proxy statement for its Annual Meeting of Stockholders to be held on May 25, 2016 (the “Proxy Statement”).

Item 11. Executive Compensation

The information required by this Item is incorporated by reference to the information included under the captions “Director Compensation” and “Executive Compensation” in the Proxy Statement.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

The information required by this Item is incorporated by reference to the information included under the captions “Securities Authorized for Issuance Under Equity Compensation Plans” and “Security Ownership of Directors, Officers and Certain Beneficial Owners” in the Proxy Statement.

Item 13. Certain Relationships and Related Transactions, and Director Independence

The information required by this Item is incorporated by reference to the information included under the captions “Election of Directors” and “Certain Relationships and Related Transactions” in the Proxy Statement.

Item 14. Principal Accountant Fees and Services

The information required by this Item is incorporated by reference to the information included under the captions “Fees to Independent Registered Public Accounting Firm” and “Policy on Audit Committee Pre-Approval of Audit and Non-Audit Services of Independent Registered Public Accounting Firm” in the Proxy Statement.

Item 15. Exhibits, Financial Statement Schedules

The following financial statements are included in this report

Consolidated Balance Sheets at December 31, 2015 and 2014

Consolidated Statements of Operations for the years ended December 31, 2015, 2014 and 2013

Consolidated Statements of Comprehensive Income for the years ended December 31, 2015, 2014 and 2013

Consolidated Statements of Changes in Shareholders' Equity for the years ended December 31, 2015, 2014 and 2013

Consolidated Statements of Cash Flows for the years ended December 31, 2015, 2014 and 2013

Notes to the Consolidated Financial Statements

Report of Independent Registered Public Accounting Firm

All financial statement schedules have been omitted as the required information is either inapplicable or included in the consolidated financial statements or related notes.

Exhibit No.	Description	Incorporated by Reference to;
2.1	Agreement and Plan of Merger, dated as of March 2, 2015, by and between Howard Bancorp, Inc. and Patapsco Bancorp, Inc. (the schedules and exhibits have been omitted pursuant to Item 601(b)(2) of Regulation S-K. Howard Bancorp undertakes to furnish supplemental copies of any of the omitted schedules or exhibits upon request by the Securities and Exchange Commission.)	Exhibit 2.1 of the Company's Form 8-K filed on March 3, 2015
2.2	Purchase and Assumption Agreement, dated as of October 17, 2014, by and among the Federal Deposit Insurance Corporation, Receiver of NBRS Financial Bank, the Federal Deposit Insurance Corporation and Howard Bank	Exhibit 2.1 of the Company's Form 8-K filed on October 23, 2014
3.1	Articles of Incorporation of Howard Bancorp, Inc.	Exhibit 3.1 of the Company's Form S-1 filed November 28, 2011
3.2	Articles of Amendment to Articles of Incorporation of Howard Bancorp, Inc.	Exhibit 3.2 of the Company's Form S-1 filed November 28, 2011
3.3	Amended and Restated Articles Supplementary of Senior Non-Cumulative Perpetual Preferred Stock, Series AA	Exhibit 3.3 of the Company's Form S-1 filed November 28, 2011
3.4	Amended and Restated Bylaws of Howard Bancorp, Inc.	Exhibit 3.1 of the Company's Form 8-K filed March 4, 2015
4.1	Form of Common Stock Certificate of Howard Bancorp, Inc.	Exhibit 4.1 of the Company's Form S-1 filed November 28, 2011
4.2	Form of Certificate for the Series AA Preferred Stock	Exhibit 4.2 of the Company's Form S-1 filed November 28, 2011
10.1*	Amended and Restated Employment Agreement between Howard Bank and Mary Ann Scully dated December 18, 2008	Exhibit 10.1 of the Company's Form S-1 filed November 28, 2011
10.3*	Amended and Restated Employment Agreement between Howard Bank and George C. Coffman dated December 18, 2008	Exhibit 10.3 of the Company's Form S-1 filed November 28, 2011
10.4*	Amended and Restated Employment Agreement between Howard Bank and Charles E. Schwabe dated December 18, 2008	Exhibit 10.4 of the Company's Form S-1 filed November 28, 2011
10.5*	Howard Bancorp 2004 Stock Incentive Plan	Exhibit 4.2 of the Company’s Form S-8

		filed April 4, 2013
10.6*	Form of Nonstatutory Stock Option Certificate and Grant Agreement under the 2004 Stock Incentive Plan	Exhibit 10.6 of the Company's Form S-1 filed November 28, 2011
10.7*	Howard Bancorp 2004 Incentive Stock Option Plan	Exhibit 4.5 of the Company’s Form S-8 filed April 4, 2013
10.8*	Form of Incentive Stock Option Certificate and Grant Agreement under the 2004 Incentive Stock Option Plan	Exhibit 10.8 of the Company's Form S-1 filed November 28, 2011
10.9	Securities Purchase Agreement dated September 22, 2011 between the Secretary of the Treasury and Howard Bancorp, Inc. pursuant to Howard Bancorp’s participation in SBLF	Exhibit 10.9 of the Company's Form S-1 filed November 28, 2011
10.10	Letter Purchase Agreement dated September 22, 2011 between the Secretary of the Treasury and Howard Bancorp, Inc. with respect to Howard Bancorp’s repurchase of outstanding Series A and Series B Stock issued pursuant to TARP	Exhibit 10.10 of the Company's Form S-1 filed November 28, 2011
10.11*	Employment Agreement between Howard Bank and Dennis E. Finnegan Dated December 16, 2014	Exhibit 10.11 to the Company’s Form 10-K filed March 27, 2015
10.12	Form of Investment Agreement, dated March 2, 2015, between Howard Bancorp, Inc. and certain investors	Exhibit 10.10 of the Company's Form 8-K filed on March 3, 2015
10.20*	Howard Bancorp, Inc. 2013 Equity Incentive Plan	Exhibit 10.20 to the Company’s Form 10-K filed March 27, 2014
10.21*	Employment Agreement between Howard Bank and Robert A. Altieri dated April 30, 2013	Exhibit 10.21 to the Company’s Form 10-Q filed August 14, 2013
10.22*	Form of Restricted Stock Grant Agreement under Howard Bancorp, Inc. 2013 Equity Incentive Plan	Exhibit 4.3 of the Company’s Form S-8 filed October 28, 2013
10.23*	Form of Nonstatutory Stock Option Grant Agreement under the 2013 Equity Incentive Plan	Exhibit 4.4 of the Company’s Form S-8 filed October 28, 2013
10.24*	Form of Incentive Stock Option Grant Agreement under the 2013 Equity Incentive Plan	Exhibit 4.5 of the Company’s Form S-8 filed October 28, 2013
10.25*	Form of Restricted Stock Grant Agreement under the 2004 Stock Incentive Plan	Exhibit 4.3 of the Company’s Form S-8 filed April 4, 2013
10.26	Branch Purchase and Assumption Agreement between NBRS Financial Bank and Howard Bank dated April 24, 2014	Exhibit 10.26 of the Company’s Form 8-K filed on April 29, 2014
10.27*	Supplemental Executive Retirement Plan of Howard Bank, effective December 1, 2014	Exhibit 10.27 of the Company’s Form 8-K filed January 6, 2015
21	Subsidiaries of the Registrant	

Exhibit 21 of the Company's Form S-1/A filed February 13, 2012

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Exhibit No.	Description	Filed herewith
10.28*	Supplemental Executive Retirement Plan of Howard Bank, effective December 1, 2014 ammended January 19, 2016	
10.29*	Employment Agreement between Howard Bank and Robert A. Altieri dated September 30, 2014	
23	Consent of Stegman & Company	
31(a)	Certification of Chief Executive Officer pursuant to Rule 13a-14(a) or 15d-14(a) of the Exchange Act pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	
31(b)	Certification of Chief Financial Officer pursuant to Rule 13a-14(a) or 15d-14(a) of the Exchange Act pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	
32	Certifications pursuant to 18 U.S.C. Section 1350, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	
101	Extensible Business Reporting Language (“XBRL”) 101.INS XBRL Instance File 101.SCH XBRL Schema File 101.CAL XBRL Calculation File 101.DEF XBRL Definition File 101.LAB XBRL Label File 101.PRE XBRL Presentation File	

* Management compensatory plan, contract or arrangement

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Howard Bancorp, Inc.

March 30, 2016 By: /s/ Mary Ann Scully
Mary Ann Scully
President, Chairman and Chief Executive Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and dates indicated.

Name	Capacities	Date
/s/ Mary Ann Scully Mary Ann Scully	President, Chief Executive Officer, Chairman (Principal Executive Officer)	March 30, 2016
/s/ George C. Coffman George C. Coffman	Chief Financial Officer (Principal Accounting and Financial Officer)	March 30, 2016
/s/ Richard G. Arnold Richard G. Arnold	Director	March 30, 2016
/s/ Nasser Basir Nasser Basir	Director	March 30, 2016
/s/ Gary R. Bozel Gary R. Bozel	Director	March 30, 2016
/s/ Andrew E. Clark Andrew E. Clark	Director	March 30, 2016
/s/ Robert J. Hartson Robert J. Hartson	Director	March 30, 2016
/s/ John J. Keenan John J. Keenan	Director	March 30, 2016
/s/ Paul I. Latta, Jr. Paul I. Latta, Jr.	Director	March 30, 2016

/s/ Kenneth C. Lundeen Kenneth C. Lundeen	Director	March 30, 2016
/s/ Karen D. McGraw Karen D. McGraw	Director	March 30, 2016
/s/ Richard J. Morgan Richard J. Morgan	Director	March 30, 2016
/s/ Thomas P. O'Neill Thomas P. O'Neill	Director	March 30, 2016
/s/ Donna Hill Staton Donna Hill Staton	Director	March 30, 2016
/s/ Robert W. Smith, Jr. Robert W. Smith, Jr.	Director	March 30, 2016