THE FARMERS BANK OF WILLARDS

Financial Highlights

	2021	2020	2019	2018	2017
At year end					
Assets	**$498,279,633**	$445,550,721	$389,484,790	$375,596,642	$348,778,738
Deposits	**433,174,437**	367,738,349	298,118,304	300,165,471	281,328,487
Loans, net	**287,091,890**	309,544,222	331,455,253	325,637,727	309,093,798
Stockholders' equity	**45,684,379**	45,599,802	43,119,631	40,326,991	38,253,625
Average balances					
Assets	**$478,796,973**	$425,128,854	$386,047,014	$365,890,774	$346,385,258
Deposits	**404,452,899**	342,151,221	302,709,983	293,693,257	276,828,944
Loans, net	**295,074,235**	321,937,236	329,341,317	315,667,327	302,952,681
Stockholders' equity	**46,621,093**	45,002,824	42,457,501	40,001,547	38,145,550
For the year					
Net interest income	**$ 15,575,264**	$ 15,793,087	$ 16,287,242	$ 15,317,312	$ 14,698,051
Income before income taxes	**5,067,275**	5,217,655	5,603,985	4,518,226	5,385,595
Net income	**3,755,231**	3,875,848	4,155,019	3,365,337	3,109,840
Cash dividend declared	**1,492,639**	1,510,352	1,512,133	1,314,898	1,117,663
Per share data (restated giving retroactive effect to stock dividends declared)					
Net income	**$2.88**	$2.95	$3.16	$2.56	$2.35
Cash dividend declared	**1.15**	1.15	1.15	1.00	0.85
Book value	**35.27**	34.73	32.80	30.67	29.09
Ratios					
Return on average assets	0.78%	0.91%	1.08%	0.92%	0.90%
Return on average equity	8.05%	8.61%	9.79%	8.41%	8.15%

Balance Sheets

	December 31, 2021	2020
Assets		
Cash and due from banks	$ 81,395,802	$ 88,009,871
Federal funds sold	-	-
Total cash and cash equivalents	81,395,802	88,009,871
Certificates of deposit in other banks	2,636,000	2,340,000
Investment securities available for sale	110,084,945	27,089,181
Federal Home Loan Bank stock, at cost	785,300	1,540,600
Loans, less allowance for loan losses of $2,926,133 and $3,176,328	287,091,890	309,544,222
Premises and equipment	5,750,551	6,848,623
Accrued interest receivable	1,065,336	1,096,759
Bank owned life insurance	4,859,283	4,735,022
Foreclosed real estate	2,894,697	3,299,858
Other assets	1,715,829	1,046,585
	$ 498,279,633	$ 445,550,721
Liabilities and Stockholders' Equity		
Deposits		
Noninterest-bearing	$ 152,777,366	$ 114,511,522
Interest-bearing	280,397,071	253,226,827
Total deposits	433,174,437	367,738,349
Federal funds purchased and other short term debt	-	52,284
Federal Home Loan Bank advances	15,000,000	28,000,000
Accrued interest payable	162,625	262,651
Cash dividend payable	1,492,639	1,510,352
Other liabilities	2,765,553	2,387,283
	452,595,254	399,950,919
Stockholders' equity		
Common stock, par value $1 per share, authorized 30,000,000 shares, issued and outstanding 1,295,133 shares in 2021 and 1,313,070 shares in 2020	1,295,133	1,313,070
Surplus	22,127,458	22,652,813
Undivided profits	23,607,165	21,344,573
Accumulated other comprehensive income (loss)	(1,345,377)	289,346
	45,684,379	45,599,802
	$ 498,279,633	$ 445,550,721

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

Statements of Income

	Years Ended December 31, 2021	2020	2019
Interest revenue			
Loans, including fees	$ 16,980,221	$ 18,071,605	$ 18,858,971
Investment securities	663,509	548,567	506,898
Federal funds sold	-	3,439	17,586
Other	244,330	257,136	336,598
Total interest revenue	17,888,060	18,880,747	19,720,053
Interest expense			
Deposits	1,785,579	2,344,693	2,452,630
Borrowed funds	527,217	742,967	980,181
Total interest expense	2,312,796	3,087,660	3,432,811
Net interest income	15,575,264	15,793,087	16,287,242
Provision for loan losses	(70,000)	875,000	1,065,354
Net interest income after provision for loan losses	15,645,264	14,918,087	15,221,888
Noninterest revenue			
Card services	1,342,194	1,022,698	876,352
Service charges on deposit accounts	300,839	256,906	360,153
Increase in cash surrender value of life insurance	124,261	123,129	122,211
Gain (loss) on sale/valuation of foreclosed real estate	(115,769)	(38,829)	(182,394)
Gain (loss) on sale/impairment of investment securities	10,042	14,158	(755)
Gain (loss) on early extinguishment of debt	(50,363)	-	-
Gain (loss) on sale/valuation of repossessed property	(6,450)	-	-
Gain (loss) on other dispositions	8,775	7,510	16,365
Other noninterest revenue	111,819	95,774	103,434
	1,725,348	1,481,346	1,295,366
Noninterest expense			
Salaries	5,076,006	4,833,366	4,778,632
Employee benefits	1,338,352	1,235,329	1,261,990
Occupancy	651,873	590,783	557,754
Furniture and equipment	536,235	498,472	468,239
Deposit insurance premiums	136,710	106,212	88,756
Data communications and processing costs	1,583,824	1,139,848	962,537
Loan processing and collections	78,133	186,781	334,712
Foreclosed real estate holding costs	59,540	156,597	158,154
Card services	1,107,409	780,492	583,881
Promotional	397,848	381,783	418,262
Other operating	1,337,407	1,272,115	1,300,352
	12,303,337	11,181,778	10,913,269
Income before income taxes	5,067,275	5,217,655	5,603,985
Income taxes	1,312,044	1,341,807	1,448,966
Net income	$ 3,755,231	$ 3,875,848	$ 4,155,019
Earnings per common share - basic and diluted	$ 2.88	$ 2.95	$ 3.16

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

Statements of Comprehensive Income

	Years Ended December 31,		
	2021	2020	2019
Net income	**$ 3,755,231**	$3,875,848	$4,155,019
Other comprehensive income (loss)			
Unrealized gain (loss) on investment securities available for sale	**(2,244,729)**	214,874	216,377
Reclassify (gain) loss realized on sale of investment securities available for sale	**(10,042)**	(14,158)	755
Income tax relating to unrealized gain (loss) on investment securities available for sale	**620,048**	(44,969)	(58,378)
Other comprehensive income (loss)	**(1,634,723)**	155,747	158,754
Comprehensive income	**$ 2,120,508**	$4,031,595	$4,313,773

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

Statements of Changes in Stockholders' Equity

	Common stock				Accumulated other comprehensive
	Shares	Par value	Surplus	Undivided profits	income
Balance, December 31, 2018	1,314,898	**$ 1,314,898**	**$ 22,701,057**	**$ 16,336,191**	**$ (25,155)**
Net income	-	-	-	4,155,019	-
Cash dividend, $1.15 per share	-	-	-	(1,512,133)	-
Stock repurchased	(300)	(300)	(8,700)	-	-
Unrealized gain on investment securities available for sale net of income taxes of $58,378	-	-	-	-	158,754
Balance, December 31, 2019	1,314,598	1,314,598	22,692,357	18,979,077	133,599
Net income	-	-	-	3,875,848	-
Cash dividend, $1.15 per share	-	-	-	(1,510,352)	-
Stock repurchased	(1,528)	(1,528)	(39,544)	-	-
Unrealized gain on investment securities available for sale net of income taxes of $44,969	-	-	-	-	155,747
Balance, December 31, 2020	1,313,070	1,313,070	22,652,813	21,344,573	289,346
Net income	-	-	-	3,755,231	-
Cash dividend, $1.15 per share	-	-	-	(1,492,639)	-
Stock repurchased	(17,937)	(17,937)	(525,355)	-	-
Unrealized loss on investment securities available for sale net of income taxes of $620,048	-	-	-	-	(1,634,723)
Balance, December 31, 2021	**1,295,133**	**$ 1,295,133**	**$ 22,127,458**	**$ 23,607,165**	**$ (1,345,377)**

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

Statements of Cash Flows

	Years Ended December 31,		
	2021	2020	2019
Cash flows from operating activities			
Interest received	**$ 17,679,103**	$19,235,324	$19,431,698
Fees and commissions received	**1,884,216**	1,603,730	1,415,936
Interest paid	**(2,412,822)**	(3,175,085)	(3,390,230)
Cash paid to suppliers and employees	**(11,321,338)**	(10,519,244)	(10,300,967)
Income taxes paid	**(1,468,213)**	(1,686,394)	(1,195,604)
	4,360,946	5,458,331	5,960,833
Cash flows from investing activities			
Proceeds from maturities and calls of investment securities available for sale	**6,593,498**	15,768,180	13,910,928
Proceeds from sale of securities available for sale	**2,147,920**	968,411	1,170,060
Net redemption (purchase) of Federal Home Loan Bank stock	**755,300**	522,500	(410,300)
Proceeds from disposition of premises, equipment and software	**854,650**	-	8,000
Proceeds from sale of foreclosed/repossessed assets	**143,210**	866,243	1,467,800
Proceeds from loans held for sale	-	-	881,938
Loans advanced, net of principal collected	**22,857,610**	18,185,698	(7,416,557)
Proceeds from sale of certificates of deposit	-	-	2,439,108
Net redemption (purchase) of certificates of deposit	**(296,000)**	722,000	(248,000)
Purchases of investment securities available for sale	**(94,089,018)**	(20,192,213)	(26,706,132)
Investment in foreclosed real estate	-	-	-
Purchases of premises, equipment, and software	**(221,982)**	(314,674)	(731,629)
	(61,254,812)	16,526,145	(15,634,784)
Cash flows from financing activities			
Net increase (decrease) in			
Time deposits	**(7,749,951)**	(1,976,431)	(11,044,602)
Other deposits	**73,186,039**	71,596,476	8,997,435
Proceeds from Federal Home Loan Bank advances, net of repayments	**(13,050,363)**	(12,585,000)	9,085,000
Proceeds from Federal funds purchased, net of repayments	**(52,284)**	(3,500,000)	3,500,000
Stock repurchased	**(543,292)**	(41,072)	(9,000)
Dividends paid	**(1,510,352)**	(1,512,133)	(1,314,898)
	50,279,797	51,981,840	9,213,935
Net increase (decrease) in cash and cash equivalents	**(6,614,069)**	73,966,316	(460,016)
Cash and cash equivalents at beginning of year	**88,009,871**	14,043,555	14,503,571
Cash and cash equivalents at end of year	**$ 81,395,802**	$88,009,871	$14,043,555

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

Statements of Cash Flows (Continued)

	Years Ended December 31, 2021	2020	2019
Reconciliation of net income to net cash provided by operating activities			
Net income	**$ 3,755,231**	$3,875,848	$4,155,019
Adjustments to reconcile net income to net cash provided by operating activities			
Depreciation and amortization	**484,408**	445,855	385,076
Amortization of computer software	**42,572**	42,320	38,534
Provision for loan losses	**(70,000)**	875,000	1,065,354
Deferred income taxes	**(120,498)**	(127,010)	(117,659)
Amortization of premiums and (accretion) of discounts, net	**107,107**	31,489	(54,928)
Loss (gain) on sale and writedown of assets			
Foreclosed real estate, net of deferred gain realized	**123,649**	38,829	182,394
Repossessed assets	**6,450**	-	-
Premises, equipment and software	**(8,775)**	(7,510)	10,063
Investment securities available for sale	**(10,042)**	(14,158)	755
Certifcates of deposit in other banks	**-**		1,892
Loans held for sale	**-**	-	(28,320)
Early extinguishment of debt	**50,363**		
Decrease (increase) in			
Cash surrender value of life insurance	**(124,261)**	(123,129)	(122,211)
Accrued interest receivable	**31,423**	221,364	(99,636)
Prepaid income taxes net of income taxes payable	**(35,671)**	(217,577)	371,021
Other assets	**(12,350)**	70,018	(17,991)
Increase (decrease) in			
Deferred origination fees, net	**(223,226)**	224,853	(11,580)
Accrued interest payable	**(100,026)**	(87,425)	42,581
Other liabilities	**464,592**	209,564	160,469
	$ 4,360,946	$5,458,331	$5,960,833

	2021	2020	2019
Noncash investing activity			
Real estate acquired through foreclosure or deed in lieu of foreclosure	**$ -**	$2,625,320	$ 545,257
Repossessed assets	**26,250**	-	-
Borrowing for automobile purchase	**-**	52,284	-
	$ 26,250	$2,677,604	$ 545,257

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

Notes to Financial Statements

1. Summary of Significant Accounting Policies

The accounting and reporting policies reflected in the financial statements conform to United States generally accepted accounting principles and to general practices within the banking industry. The Farmers Bank of Willards is not considered a public business entity. As such, it is not required to comply with disclosures that pertain only to public companies. For accounting standards issued by the Financial Accounting Standards Board, the Bank is subject to the effective dates applicable to private companies.

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements. These estimates and assumptions may affect the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates. The estimate that is particularly susceptible to significant change is the allowance for loan losses.

Nature of operations

The Farmers Bank of Willards is a financial institution operating primarily in the Maryland counties of Wicomico and Worcester as well as lower Sussex County in Delaware. The Bank does not limit its services to customers in these areas; but it is the Bank's priority to serve the financial needs of those within its community.

The Bank offers deposit services and loans to individuals, small businesses, associations, and government entities. Other services include automatic drafts from accounts, automated teller machine services, safe deposit boxes, debit cards, internet banking with bill pay feature, and digital banking with a lock-it feature. Prior to 2019, the Bank offered credit card loans but sold the portfolio in February 2019.

COVID-19 impact

The COVID-19 pandemic continues to spread and is still a public health risk. As a result of COVID-19, the Bank has seen a decrease in its lobby business and a more rapid adoption of its technology channels. As customers have received government funds and decreased their spending, the deposits of the Bank have grown at a higher rate than normal. Management expects some of these deposits to roll off during 2022.

Per share data and stock dividends

Earnings per common share and dividends per common share are determined by dividing net income and dividends by the weighted average number of shares outstanding after giving retroactive effect to stock dividends declared. There are no common stock equivalents. The adjusted weighted average number of shares used in the earnings per share calculation was 1,306,038, 1,314,315, and 1,314,888 for the years ended December 31, 2021, 2020, and 2019, respectively.

Stock dividends of 20% or more are recorded at par value while stock dividends of less than 20% are recorded at fair value. This value is determined based on the most recent sale before the dividend. Stock dividends may be funded from earned surplus. As of December 31, 2021, the entire balance of surplus represents paid in surplus with no earned surplus as a result of transfers between the capital accounts.

Cash and cash equivalents

For purposes of reporting cash flows, cash and cash equivalents include cash on hand, demand amounts due from banks, and federal funds sold. Federal funds are purchased and sold for one-day periods. Due from banks includes interest-bearing accounts that are payable on demand.

Notes to Financial Statements

1. Summary of Significant Accounting Policies (Continued)

Certificates of deposit in other banks

Certificates of deposit in other banks are recorded at cost.

Federal Home Loan Bank stock

As a member of the Federal Home Loan Bank, the Bank is required to purchase stock based on its total assets. Additional stock is purchased and redeemed based on the outstanding Federal Home Loan Bank advances to the Bank. This investment is carried at cost.

Investment securities

As debt securities are purchased, management determines if the securities should be classified as held to maturity or available for sale. Declines in the fair value of individual securities below their cost that are other than temporary result in write-downs of the individual securities to their estimated recoverable value. Factors affecting the determination of whether an impairment that is other than temporary 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 likely hold a security for a period of time sufficient to allow for any anticipated recovery of fair value. Gains and losses on the disposition of securities are recorded as of the trade date using the specific identification method.

Securities held to meet liquidity needs or which may be sold before maturity are classified as available for sale and carried at fair value with unrealized gains and losses included in stockholders' equity on an after-tax basis. Equity securities are recorded at fair value.

Securities that management has the intent and ability to hold to maturity are recorded at amortized cost, which is cost adjusted for amortization of premiums to the bond's first call date and accretion of discounts to maturity. Premiums and discounts of mortgage-backed securities are amortized over the expected lives of the securities. Amortization and accretion are recorded using a method that approximates the level yield method.

Loans held for sale

During 2018, the Bank classified its credit card portfolio as available for sale as a result of a signed agreement to sell its credit card loans. When the loans were sold in February, 2019, the Bank recognized a gain on sale of \$28,320. There are no loans held for sale as of December 31, 2021 or 2020.

Loans and allowance for loan losses

Loans are stated at face value adjusted for deferred origination fees, costs, and the allowance for loan losses. Interest on loans is accrued on the principal amounts outstanding. Nonrefundable fees and costs associated with originating loans are recognized as income over the life of the related loans. Generally the accrual of interest is discontinued when any portion of principal or interest is ninety days past due and collateral is insufficient to discharge the debt in full. Loans specifically reviewed for nonaccrual treatment are not considered impaired during periods of "minimal delay" in payment (usually ninety days or less) or if they are both well secured and in the process of collection by an attorney, provided eventual collection of all amounts due is expected.

Payments received on nonaccrual loans are generally accounted for as a reduction in principal with interest recognized after all principal has been collected. Loans are returned to accrual status when all principal and interest amounts contractually due are brought current and future payments are reasonably assured.

Notes to Financial Statements

1. Summary of Significant Accounting Policies (Continued)

Loans and allowance for loan losses (continued)

Loans are considered impaired when, based on current information, it is probable that the Bank will not collect all principal and interest payments according to contractual terms. Impaired loans include loan relationships where management of the Bank has worked with the borrowers to restructure the original terms of the loan. This may include reducing the payments to interest only for a set period or reducing the interest rate on the loan.

Management considers the financial condition of the borrower, cash flows of the loan, and the value of the related collateral. Impaired loans are measured based on the present value of expected future cash flows discounted at the loan's effective interest rate, except that the Bank will measure impairment based on the fair value of the collateral, if the loan is collateral dependent. For collateral dependent real estate loans, management reviews its current appraisal, obtaining either a new appraisal or making adjustments to the original appraised value based on current trends in the real estate market. For other collateral dependent loans, the Bank uses other estimation methods.

The allowance for loan losses is established through a provision for loan losses charged to expense. Loans are charged against the allowance for loan losses when management believes that the collectability of the principal is unlikely. The allowance, based on evaluations of the collectability of loans, is an amount that management believes will be adequate to absorb probable losses on existing loans that may become uncollectible. The evaluations take into consideration such factors as changes in the nature and volume of the loan portfolio, overall portfolio quality, review of specific problem loans, and current economic conditions and trends that may affect the borrowers' ability to pay.

The allowance for loan losses represents an estimation of losses in the loan portfolio. The Bank uses a loan grading system to identify its impaired loans. For the balance of the loan portfolio, management applies a factor to pools of loans with similar characteristics to provide for losses. The pooled loan portions of the allowance reflect management's estimate of probable inherent but undetected losses within the portfolio due to uncertainties in economic conditions, delays in obtaining information, including unfavorable information about a borrower's financial condition, the difficulty in identifying triggering events that correlate perfectly to subsequent loss rates, and risk factors that have not yet manifested themselves in loss allocation factors. These loss allocation factors are general indicators of future loss and include current historic losses, economic conditions, officer experience or unseasoned new products and current delinquency ratios compared to historic ratios. The adequacy of the allowance is determined through careful and continuous evaluation of the loan portfolio, and involves consideration of a number of factors to establish a prudent level.

Management believes it has established the allowance for loan losses in accordance with generally accepted accounting principles and has taken into account the views of its regulators and the current economic environment. There can be no assurance that in the future the Bank's regulators will not require, or the changes in economic environment will not necessitate further increases in the allowance.

Management reports loans as delinquent based on the terms of the promissory note including any modifications.

Premises and equipment

Premises and equipment are recorded at cost less accumulated depreciation. Land is recorded at cost. Depreciation is computed using the straight-line method over the estimated useful lives of the assets or, if shorter, the expected terms of the leases including lease option periods where exercise is reasonably certain.

Notes to Financial Statements

1. Summary of Significant Accounting Policies (Continued)

Bank owned life insurance

The Bank owns five life insurance policies through two carriers on its three current and retired executive officers. The policies are recorded at their cash surrender values.

Foreclosed real estate

Real estate acquired through foreclosure is recorded at the lower of cost or fair value on the date acquired, less estimated cost to sell. In general, cost equals the Bank's investment in the property at the time of foreclosure. Losses incurred at the time of acquisition of the property are charged to the allowance for loan losses. Subsequent reductions in the estimated fair value of the property are included with gains and losses on sales and valuations of foreclosed real estate. Expenses of owning the property are included in noninterest expense.

Loans are transferred to foreclosed real estate once either the sale has been ratified or the Bank receives a deed in lieu of foreclosure from the borrower.

Income taxes

Income tax expense is based on the results of operations, adjusted for permanent differences between items of income or expense reported in the financial statements and those reported for tax purposes. Deferred income taxes are provided for the temporary differences between financial and taxable income. Deferred tax assets and liabilities are determined based on the difference between the financial statement and tax bases of assets and liabilities, using enacted tax rates in effect for the year in which the differences are expected to reverse.

Recent accounting pronouncements

During February 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2016-02, "Leases (Topic 842)." Among other things, in the amendments in ASU 2016-02, lessees will be required to recognize the following for all leases (with the exception of short-term leases) at the commencement date: (1) a lease liability, which is a lessee's obligation to make lease payments arising from a lease, measured on a discounted basis; and (2) a right-of-use asset, which is an asset that represents the lessee's right to use, or control the use of, a specified asset for the lease term. Under the new guidance, lessor accounting is largely unchanged. The ASU was initially effective for non-public business entities' financial statements issued for fiscal years beginning after December 15, 2019, and interim periods with fiscal years beginning after December 15, 2020. In June 2020, the FASB issued ASU 2020-05. Under ASU 2020-05, private companies may apply the new leases standard for fiscal years beginning after December 15, 2021, and to interim periods within fiscal years beginning after December 15, 2022. Earlier application is permitted. The Bank will be adopting this standard during the year-ended December 31, 2022. It is not expected to have a significant impact on the Bank's financial statements.

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

Notes to Financial Statements

1. Summary of Significant Accounting Policies (Continued)

Subsequent events

The Bank has evaluated events and transactions subsequent to December 31, 2021, through March 2, 2022, the date these financial statements were available to be issued. No significant subsequent events were identified that would affect the presentation of the financial statements.

2. Correspondent Bank Relationships

The Bank normally carries balances with other banks that exceed the federally insured limit. The average balances carried in excess of the limit, including unsecured federal funds sold to the same banks, were approximately $12,926,898 and $13,999,723 for 2021 and 2020, respectively. The balance maintained at the Federal Reserve Bank is excluded from this average.

Deposits held in noninterest-bearing transaction accounts are aggregated with any interest-bearing deposits the owner may hold in the same ownership category. The combined total is insured up to $250,000.

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

3. Certificates of Deposit in Other Banks

The certificates mature as follows:

Maturity period	2021	2020
One year or less	$ 1,463,000	$ 947,000
Over one to two years	449,000	470,000
Over two to three years	249,000	449,000
Over three to four years	225,000	249,000
Over four to five years	250,000	225,000
	$ 2,636,000	$ 2,340,000

All individual certificates of deposit balances are in increments of $250,000 or less to allow for full FDIC insurance coverage.

Notes to Financial Statements

4. Investment Securities Available for Sale

Investment securities are summarized as follows:

December 31, 2021	Amortized cost	Unrealized gains	Unrealized losses	Fair value	Annual income
U.S. Treasury	$ 15,620,392	$ -	$ 67,971	$ 15,552,421	$ 7,962
U.S. government agency	9,247,576	55,879	163,039	9,140,416	110,738
Corporate	24,656,568	25,393	186,127	24,495,834	52,497
State and municipal	14,048,064	87,569	205,420	13,930,213	189,321
Mortgage-backed securities	48,367,922	31,808	1,433,669	46,966,061	302,991
	$111,940,522	$ 200,649	$2,056,226	$ 110,084,945	$ 663,509

December 31, 2020	Amortized cost	Unrealized gains	Unrealized losses	Fair value	Annual income
U.S. Treasury	$ -	$ -	$ -	$ -	$ 99,952
U.S. government agency	5,213,052	133,950	7,209	5,339,793	132,923
Corporate	1,211,453	83,572	8,853	1,286,172	35,027
State and municipal	9,082,903	166,701	59,970	9,189,634	126,231
Mortgage-backed securities	11,182,578	129,974	38,970	11,273,582	154,434
	$ 26,689,986	$ 514,197	$115,002	$ 27,089,181	$ 548,567

The decline in fair values of debt securities is a result of the fluctuations in interest rates. Since no loss is expected on these securities, no impairment has been recorded. During 2021 and 2020, management sold securities with a book value of $2,137,878 and $954,253, respectively realizing gross gains of $31,084 and gross losses of $21,042 in 2021 and gross gains of $30,354 and gross losses of $16,196 in 2020. During 2019, management sold securities with a book value of $1,170,815, realizing gross gains of $5,918 and gross losses of $6,673.

The Bank has pledged investment securities as collateral on certain deposits. The Bank also has a secured line of credit from a correspondent bank that, when drawn, requires pledging of securities.

Contractual maturities and the amount of pledged securities are summarized below. Actual maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations. Mortgage-backed securities are due in monthly installments and Small Business Administration agency securities are payable in quarterly installments.

	December 31, 2021		December 31, 2020	
Maturity period	Amortized cost	Fair value	Amortized cost	Fair value
One year or less	$ 13,561,226	$ 13,546,686	$ 695,937	$ 707,335
One through five years	36,348,242	36,057,127	2,224,943	2,272,215
Five through ten years	5,447,267	5,350,372	3,866,084	3,994,952
After ten years	6,506,146	6,416,714	6,551,976	6,567,645
Mortgage-backed securities	48,367,922	46,966,061	11,182,578	11,273,582
Small Business Administration agencies	1,709,719	1,747,985	2,168,468	2,273,452
	$111,940,522	$110,084,945	$ 26,689,986	$ 27,089,181
Pledged securities	$ 4,839,134	$ 4,802,281	$ 3,559,873	$ 3,637,426

Notes to Financial Statements

4. Investment Securities Available for Sale (Continued)

Investment securities with unrealized losses for continuous periods of less than twelve months and twelve months or longer are as follows:

December 31, 2021	Less than 12 months		12 months or longer		Total	
	Fair value	Unrealized losses	Fair value	Unrealized losses	Fair value	Unrealized losses
U.S. Treasury	$15,552,421	$ 67,971	$ -	$ -	$15,552,421	$ 67,971
U.S. government agency	5,598,678	77,206	1,736,003	85,833	7,334,681	163,039
Corporate	18,752,189	186,127	-	-	18,752,189	186,127
State and municipal	7,559,933	102,825	2,663,511	102,595	10,223,444	205,420
Mortgage-backed securities	42,326,394	1,278,578	3,281,325	155,091	45,607,719	1,433,669
	$89,789,615	$1,712,707	$ 7,680,839	$ 343,519	$97,470,454	$2,056,226

December 31, 2020	Less than 12 months		12 months or longer		Total	
	Fair value	Unrealized losses	Fair value	Unrealized losses	Fair value	Unrealized losses
U.S. Treasury	$ -	$ -	$ -	$ -	$ -	$ -
U.S. government agency	1,542,864	5,401	47,565	1,808	1,590,429	7,209
Corporate	216,147	38,970	-	-	216,147	8,853
State and municipal	2,995,590	59,970	-	-	2,995,590	59,970
Mortgage-backed securities	5,445,536	8,853	-	-	5,445,536	38,970
	$10,200,137	$ 113,194	$ 47,565	$ 1,808	$ 10,247,702	$ 115,002

5. Loans

Major classifications of loans are as follows:

December 31,	2021	2020
Mortgage		
Residential	$ 144,968,690	$ 148,626,792
Commercial	60,587,588	76,541,316
Farm	12,505,472	17,134,015
Construction	33,725,607	23,272,350
Commercial and agricultural	28,499,710	38,650,459
Consumer	9,730,956	8,495,618
	290,018,023	312,720,550
Allowance for loan losses	2,926,133	3,176,328
Loans, net	$ 287,091,890	$ 309,544,222

Loans are reported after adding the balances of the deferred costs net of deferred origination fees and unearned interest recorded as a result of restoring loans to accrual status. The total adjustment for net fees and unearned interest was $171,424 and $394,650 as of December 31, 2021 and 2020, respectively.

Notes to Financial Statements

5. Loans (Continued)

Nonaccrual loans are as follows:

December 31,	2021	2020
Mortgage		
Residential	$ 113,971	$ 121,036
Commercial	23,913	-
Farm	-	-
Construction	205,564	367,906
Commercial and agricultural	-	98,915
Consumer	138,959	7,580
	$ 482,407	$ 595,437
Interest not accrued	$ 83,762	$ 125,633

Information regarding impaired loans as of and for the year ending December 31, 2021 is as follows:

	Unpaid contractual principal balance	Recorded investment	Related allowance	Average recorded investment	Interest income recognized
With no related allowance					
Mortgage					
Residential	$ 310,307	$ 303,095	$ -	$ 306,493	$ 12,183
Commercial	-	-	-	-	-
Farm	-	-	-	-	-
Construction	144,039	55,180	-	85,985	-
Commercial and agricultural	-	-	-	-	-
Consumer	-	-	-	-	-
	454,346	358,275	-	392,478	12,183
With related allowance					
Mortgage					
Residential	584,711	577,655	106,081	589,919	20,459
Commercial	-	-	-	-	-
Farm	-	-	-	-	-
Construction	392,320	263,523	17,239	271,624	7,729
Commercial and agricultural	134,311	94,475	94,475	131,137	3,258
Consumer	171,461	170,530	141,520	177,147	9,943
	1,282,803	1,106,183	359,315	1,169,827	41,389
Totals					
Mortgage					
Residential	895,018	880,750	106,081	896,412	32,642
Commercial	-	-	-	-	-
Farm	-	-	-	-	-
Construction	536,359	318,703	17,239	357,609	7,729
Commercial and agricultural	134,311	94,475	94,475	131,137	3,258
Consumer	171,461	170,530	141,520	177,147	9,943
	$ 1,737,149	$ 1,464,458	$ 359,315	$ 1,562,305	$ 53,572

Notes to Financial Statements

5. Loans (Continued)

Information regarding impaired loans as of and for the year ending December 31, 2020 is as follows:

	Unpaid contractual principal balance	Recorded investment	Related allowance	Average recorded investment	Interest income recognized
With no related allowance					
Mortgage					
Residential	$ 289,652	$ 289,652	$ -	$ 290,999	$ 17,900
Commercial	748,353	367,906	-	432,094	-
Farm	500,000	500,000	-	589,289	32,795
Construction	-	-	-	-	-
Commercial and agricultural	-	-	-	-	-
Consumer	14,601	7,579	-	13,034	-
	1,552,606	1,165,137	-	1,325,416	50,695
With related allowance					
Mortgage					
Residential	670,071	656,152	131,755	670,531	18,292
Commercial	144,826	144,826	10,151	145,798	7,510
Farm	-	-	-	-	-
Construction	154,389	115,472	2,761	123,378	7,922
Commercial and agricultural	314,672	246,296	87,487	260,289	7,968
Consumer	46,968	46,417	11,036	49,808	1,773
	1,330,926	1,209,163	243,190	1,249,804	43,465
Totals					
Mortgage					
Residential	959,723	945,804	131,755	961,530	36,192
Commercial	893,179	512,732	10,151	577,892	7,510
Farm	500,000	500,000	-	589,289	32,795
Construction	154,389	115,472	2,761	123,378	7,922
Commercial and agricultural	314,672	246,296	87,487	260,289	7,968
Consumer	61,569	53,996	11,036	62,842	1,773
	$2,883,532	$2,374,300	$ 243,190	$2,575,220	$ 94,160

Outstanding loan balances based on allowance impairment analysis are as follows:

	December 31, 2021		December 31, 2020	
	Individually evaluated	Collectively evaluated	Individually evaluated	Collectively evaluated
Mortgage				
Residential	$ 880,750	$ 144,087,940	$ 945,804	$ 147,680,988
Commercial	-	60,587,588	512,732	76,028,584
Farm	-	12,505,472	500,000	16,634,015
Construction	318,703	33,406,904	115,472	23,156,878
Commercial and agricultural	94,475	28,405,235	246,296	38,404,163
Consumer	170,530	9,560,426	53,996	8,441,622
	$ 1,464,458	$ 288,553,565	$ 2,374,300	$ 310,346,250

Notes to Financial Statements

5. **Loans** (Continued)

Composition of the allowance for loan losses, by loan classification and based on impairment analysis, is as follows:

	December 31, 2021		December 31, 2020	
	Individually evaluated	Collectively evaluated	Individually evaluated	Collectively evaluated
Mortgage				
Residential	$ 106,081	$ 638,104	$ 131,755	$ 734,967
Commercial	-	584,604	10,151	925,871
Farm	-	149,272	-	234,572
Construction	17,239	485,205	2,761	351,453
Commercial and agricultural	94,475	493,900	87,487	445,634
Consumer	141,520	118,040	11,036	47,724
Unallocated	-	97,693	-	192,917
	$ 359,315	$ 2,566,818	$ 243,190	$ 2,933,138

Transactions in the allowance for loan losses, by loan classification, are as follows:

December 31, 2021	Beginning balance	Provision for loan losses	Charge-offs	Recoveries	Ending balance
Mortgage					
Residential	$ 866,722	$ (96,287)	$ 26,250	$ -	$ 744,185
Commercial	936,022	(452,216)	5,709	106,507	584,604
Farm	234,572	(85,465)	-	165	149,272
Construction	354,214	148,230	-	-	502,444
Commercial and agricultural	533,121	98,154	74,162	31,262	588,375
Consumer	58,760	412,808	235,201	23,193	259,560
Unallocated	192,917	(95,224)	-	-	97,693
	$ 3,176,328	$ (70,000)	$ 341,322	$ 161,127	$ 2,926,133

December 31, 2020	Beginning balance	Provision for loan losses	Charge-offs	Recoveries	Ending balance
Mortgage					
Residential	$ 976,212	$ (125,117)	$ 110,695	$ 126,322	$ 866,722
Commercial	587,915	889,434	587,827	46,500	936,022
Farm	207,846	345,094	349,503	31,135	234,572
Construction	643,444	(289,230)	-	-	354,214
Commercial and agricultural	519,787	86,708	125,655	52,281	533,121
Consumer	57,136	5,194	73,808	70,238	58,760
Unallocated	230,000	(37,083)	-	-	192,917
	$ 3,222,340	$ 875,000	$ 1,247,488	$ 326,476	$ 3,176,328

The Bank makes loans to customers primarily located in the Delmarva region. Although the loan portfolio is diversified, its performance will be influenced by the economy of the region.

Notes to Financial Statements

5. **Loans** (Continued)

An analysis of past due loans as of December 31, 2021 follows:

	Loans 30-89 days past due	Loans 90 or more days past due	Total past due loans	Current loans	Total loans	Accruing Loans 90 or more days past due
Mortgage						
Residential	$ 677,611	$ -	$ 677,611	$ 144,291,079	$ 144,968,690	$ -
Commercial	-	-	-	60,587,588	60,587,588	-
Farm	-	-	-	12,505,472	12,505,472	-
Construction	-	205,563	205,563	33,520,044	33,725,607	-
Commercial and agricultural	86,485	23,913	110,398	28,389,312	28,499,710	-
Consumer	72,431	127,207	199,638	9,531,318	9,730,956	-
	$ 836,527	$ 356,683	$ 1,193,210	$ 288,824,813	$ 290,018,023	$ -

An analysis of past due loans as of December 31, 2020 follows:

	Loans 30-89 days past due	Loans 90 or more days past due	Total past due loans	Current loans	Total loans	Accruing Loans 90 or more days past due
Mortgage						
Residential	$ 196,559	$ -	$ 196,559	$ 148,430,233	$ 148,626,792	$ -
Commercial	-	-	-	76,541,316	76,541,316	-
Farm	-	-	-	17,134,015	17,134,015	-
Construction	-	367,906	367,906	22,904,444	23,272,350	-
Commercial and agricultural	74,559	98,915	173,474	38,476,985	38,650,459	-
Consumer	52,828	4,156	56,984	8,438,634	8,495,618	4,156
	$ 323,946	$ 470,977	$ 794,923	$ 311,925,627	$ 312,720,550	$ 4,156

Credit quality indicators

Management has developed a loan risk grading system to help monitor the overall credit quality of its loan portfolio. Each loan is assigned a risk grade at origination. Large credits, regardless of performance, are reviewed annually to determine the risk grade is still suitable. Loan grades are changed as borrowers' circumstances change and either develop credit weaknesses or improved conditions and performance are noted.

Special mention

A special mention loan has potential weaknesses in the credit that require management's close attention. Generally, special mention credits have a weakness that can be corrected in a relatively short period of time. Poor liquidity or fault in collateral title can result in a special mention grade. If left uncorrected, these potential credit weaknesses may result in deterioration of repayment prospects. Special mention loans do not expose the Bank to sufficient risk to warrant an adverse classification.

Substandard

A substandard loan has a well-defined weakness or weaknesses that jeopardize the ultimate repayment of the loan and require more intense supervision by Bank management. The weaknesses in the collateral value, cash flows or borrower's/project's performance would likely result in some loss to the Bank if the deficiencies are not corrected. Borrowers may exhibit recent or unexpected losses, and inadequate debt service coverage ratio, or marginal liquidity and capitalization. Loans that are classified as troubled debt restructured loans are generally graded substandard until the borrower shows the ability to perform under the modified terms of the restructure.

Notes to Financial Statements

5. **Loans** (Continued)

Doubtful

A loan classified as doubtful has all the weaknesses of a substandard loan with the added characteristic that the weaknesses in the credit make collection or liquidation in full, highly improbable.

Loss

Rarely does the Bank use this category. If a credit is deemed loss, management generally records a charge-off unless there are extenuating circumstances.

Summarized below is the credit risk profile of the loan portfolio as of December 31, 2021:

	Pass credits	Special Mention	Substandard	Doubtful	Loss
Mortgage					
Residential	$ 144,664,216	$ 190,503	$ 113,971	$ -	$ -
Commercial	60,587,588	-	-	-	-
Farm	12,505,472	-	-	-	-
Construction	33,520,043	-	205,564	-	-
Commercial and agricultural	28,405,235	-	94,475	-	-
Consumer	9,591,997	-	138,959	-	-
	$ 289,274,551	$ 190,503	$ 552,969	$ -	$ -

Summarized below is the credit risk profile of the loan portfolio as of December 31, 2020:

	Pass credits	Special Mention	Substandard	Doubtful	Loss
Mortgage					
Residential	$148,347,316	$ 158,440	$ 121,036	$ -	$ -
Commercial	76,541,316	-	-	-	-
Farm	17,134,015	-	-	-	-
Construction	22,904,444	-	367,906	-	-
Commercial and agricultural	38,551,544	-	98,915	-	-
Consumer	8,480,920	-	14,698	-	-
	$311,959,555	$ 158,440	$ 602,555	$ -	$ -

During the year ended December 31, 2020, the Bank provided short-term deferrals of loan principal payments up to 90 days for borrowers who were affected by the COVID-19 pandemic. These borrowers were required to meet certain criteria, such as being in good standing and not more than 30 days past due prior to the pandemic. As of December 31, 2020, four borrowers had $578,018 outstanding under this program and three additional borrowers with balances totaling $26,888 received a second 90-day concession. There were no extensions related to COVID-19 as of December 31, 2021.

The restructuring of a loan is considered a "troubled debt restructuring" if both (i) the borrower is experiencing financial difficulties and (ii) the creditor has granted a concession. These concessions typically result from the Bank's loss mitigation activities and may include interest rate reductions or below market interest rates, principal forgiveness, restructuring amortization schedules, forbearance and other actions intended to minimize potential losses and to avoid foreclosure or repossession of collateral.

The Bank works with customers to restructure loans by changing the interest rate, modifying the payment term, and writing off accrued interest.

Notes to Financial Statements

5. **Loans** (Continued)

The Bank has outstanding troubled debt restructured (TDR) loans as follows:

	December 31, 2021			December 31, 2020		
	Count	Contract balance	Modified balance	Count	Contract balance	Modified balance
Performing						
Mortgage						
Residential	5	$ 583,333	$ 576,277	6	$ 673,845	$ 673,845
Commercial	-	-	-	-	-	-
Farm	-	-	-	1	500,000	500,000
Construction	1	150,568	113,139	1	154,390	150,066
Commercial and agricultural	1	86,485	70,562	2	165,757	164,108
Consumer	1	32,098	31,571	1	39,850	39,850
	8	852,484	791,549	11	1,533,842	1,527,869
Nonperforming						
Mortgage						
Residential	1	121,183	113,971	1	127,437	121,036
Commercial	-	-	-	-	-	-
Farm	-	-	-	-	-	-
Construction	1	241,752	150,384	2	552,972	261,385
Commercial and agricultural	-	-	-	-	-	-
Consumer	-	-	-	-	-	-
	2	362,935	264,355	3	680,409	382,421
Total	10	$ 1,215,419	$ 1,055,904	14	$ 2,214,251	$ 1,910,290

As of December 31, 2021, and 2020, there were no delinquent TDR loans more than ninety days and still accruing interest. During 2020 the Bank transferred a restructured residential mortgage with a balance of $323,122 into foreclosed real estate. During 2021, the Bank recorded recoveries of $9,195 for a TDR residential mortgage, In 2020 the Bank also recorded charge-offs on restructured loans of $37,827 for TDR commercial mortgages while recording recoveries of $11,034 for TDR residential mortgages.

During 2020, the Bank restructured one residential mortgage loan with a total outstanding balance of $128,485 and one farm loan with a total outstanding balance of $500,000. There were no new troubled debt restructurings in 2021.

The Bank has the following loan commitments outstanding:

December 31,	2021	2020
Construction loans	$ 13,198,412	$ 8,020,050
Home equity and revolving residential lines	6,541,461	5,407,525
Other lines of credit	29,559,813	17,902,599
Standby letters of credit	1,957,131	1,172,359
Payment letters of credit	5,000	-
	$ 51,261,817	$ 32,502,533

Loan commitments and lines of credit are agreements to lend to a customer as long as there is no violation of any condition to the contract. Loan commitments generally have interest fixed at current market rates,

Notes to Financial Statements

5. **Loans** (Continued)

fixed expiration dates, and may require payment of a fee. Lines of credit generally have variable interest rates. Such lines do not represent future cash requirements because it is unlikely that all customers will draw upon their lines in full at any time.

Letters of credit are commitments issued to guarantee the performance of a customer to a third party. Loan commitments, lines of credit, and letters of credit are made on the same terms, including collateral, as outstanding loans. The Bank's exposure to loss in the event of nonperformance by the borrower is represented by the contract amount of the commitment. Management is not aware of any accounting loss the Bank will incur by the funding of these commitments.

6. **Premises and Equipment**

A summary of premises and equipment and the related depreciation follows:

	Useful life	2021	2020
Land		$ 1,276,607	$ 2,091,716
Buildings and improvements	10-40 years	3,747,791	3,753,379
Leasehold improvements	10-40 years	1,817,592	1,822,192
Furniture and equipment	5-10 years	4,026,783	3,927,939
Automobiles	4-5 years	74,284	74,284
		10,943,057	11,669,510
Accumulated depreciation and amortization		5,192,506	4,820,887
Net premises and equipment		$ 5,750,551	$ 6,848,623
Depreciation and amortization expense		$ 484,408	$ 445,855

Included in other assets at December 31, 2021 and 2020, is computer software carried at an amortized cost of $101,769 and $117,909, respectively. Software amortization expense was $42,572 and $42,320 in 2021 and 2020, respectively.

7. **Lease Commitments**

The Bank has entered into agreements to lease branch premises at the following locations:

Location	Branch	Lease expiration	Renewals
Ocean City, Maryland	West OC	April 30, 2030	One 5-year term
Ocean City, Maryland	North OC	December 31, 2025	none
Ocean City, Maryland	Talbot St.	May 31, 2024	Three 3-year term
Millsboro, Delaware	Millsboro	April 15, 2037	Three 10-year terms

Rent expense for 2021, 2020, and 2019 was $194,846, $174,406, and $137,805, respectively. The Bank is also required to pay certain executory costs including insurance, real estate taxes, and common area maintenance.

Notes to Financial Statements

7. Lease Commitments (Continued)

Lease obligations, including renewal periods management is reasonably certain will be exercised, will require minimum payments as follows:

Period	Amount
2022	$ 197,338
2023	199,024
2024	189,512
2025	129,945
2026	55,301
Remaining years	688,326
	$ 1,459,446

8. Foreclosed Real Estate

Transactions in foreclosed real estate are as follows:

	2021	2020	2019
Beginning of year balance	$ 3,299,858	$ 1,579,610	$ 2,720,960
Additions and improvements	-	2,625,320	545,257
Sale deferred (recognized)	(146,182)	(55,016)	(524,730)
Sales proceeds	(143,210)	(811,227)	(943,070)
Writedowns and losses	(115,769)	(38,829)	(218,807)
End of year balance	$ 2,894,697	$ 3,299,858	$ 1,579,610

The Bank has financed some of the sales of its foreclosed real estate properties. If the down payments on these sales are less than required by accounting standards for sales treatment, the financed properties remain in foreclosed real estate until payments made on the loans plus the original down payments exceed thresholds for required down payment. Any gains on these sales are also deferred. Deferred gains of $7,880, $160 and $36,413 were recognized on loans transferred out of foreclosed real estate in 2021, 2020 and 2019, respectively. Financed properties reported as foreclosed real estate as of December 31, 2021, 2020, and 2019 totaled $454,252, $271,152, and $326,168, respectively.

Five loans, totaling $474,507 were in the process of foreclosure as of December 31, 2021. There were no loans in the process of foreclosure as of December 31, 2020.

9. Deposits

Major classifications of interest-bearing deposits are as follows:

December 31,	2021	2020
Money market and NOW	$ 86,343,902	$ 67,086,136
Savings	74,965,109	59,302,680
Certificates of deposit over $250,000	16,469,428	19,718,403
Other time	102,618,632	107,119,608
	$ 280,397,071	$ 253,226,827

Demand deposits and interest-bearing escrow accounts, in an overdraft status, totaling $62,889 and $38,268, as of December 31, 2021 and 2020, respectively have been reclassified as loans.

Notes to Financial Statements

9. Deposits (Continued)

The maturity and repricing distributions of time deposits as of December 31, 2021 follows:

Time deposits	Over $250,000	Other	Maturity Total
One year or less	$ 5,704,945	$ 48,070,301	$ 53,775,246
Over one to two years	5,431,610	17,023,647	22,455,257
Over two to three years	1,986,928	9,754,087	11,741,015
Over three to four years	1,238,747	14,955,962	16,194,709
Over four to five years	2,107,198	12,814,635	14,921,833
	$ 16,469,428	$ 102,618,632	$ 119,088,060

Certain certificates are issued with a step-up feature that provides the owner a one-time opportunity to increase the certificate of deposit rate to the current rate of newly issued certificates of the same term at the date the option is exercised. Once a certificate of deposit step-up feature has been exercised, the deposit becomes fixed rate.

10. Lines of Credit and Federal Home Loan Bank Advances

The Bank has an available line of credit of $12,000,000 in overnight federal funds from a correspondent bank. $6,000,000 of this line is unsecured while the balance of the line of credit is collateralized with pledged investment securities. The entire line was available as of December 31, 2021 and 2020.

The Bank also has a line of credit with the Federal Home Loan Bank (FHLB) which allows total outstanding advances of twenty five percent of total assets. Because the Bank has pledged as collateral its portfolio of first mortgages on residential properties, the total available advances is limited by this portfolio. Based on this collateral, the total remaining credit available with the FHLB as of December 31, 2021 and 2020 was $37,027,422 and $32,846,171, respectively. In addition to the first residential mortgage portfolio, the FHLB has placed a blanket lien on all of the loans of the Bank with the exception of the nonmortgage consumer and commercial loans.

The nonmortgage consumer and commercial loan portfolios are pledged as collateral on a line of credit from the Federal Reserve Bank. The total available under this line of credit as of December 31, 2021 and 2020 was $20,570,039 and $20,168,101, respectively.

A summary of outstanding FHLB advances is as follows:

Description	Rate	December 31, 2021	December 31, 2020	Maturity
Five year advance	1.4900%	-	8,000,000	March 13, 2025
Six year advance	1.7900%	-	5,000,000	March 13, 2026
Seven year advance	2.3930%	15,000,000	15,000,000	March 13, 2027
		$ 15,000,000	$ 28,000,000	

The interest rates on the closed end advances are fixed. In March of 2020, the Bank refinanced $28 million of outstanding advances at lower rates and extended the maturities of the advances. There were no fees associated with the refinances.

Notes to Financial Statements

10. Lines of Credit and Federal Home Loan Bank Advances (Continued)

During 2021, the Bank paid off the two smaller advances, totaling $13,000,000, recognizing a net early extinguishment loss of $50,363. On January 6, 2022, the Bank paid off its final advance of $15,000,000. The Bank recognized a loss of $249,701 on this payoff but will save $358,950 of interest on this advance during the year ending December 31, 2022.

11. Employment Contract

The Bank is party to a ten-year employment agreement, dated September 2002, with an executive that provides for compensation and certain other benefits. The agreement had one ten-year extension, which extended the agreement through 2022. The contract provides severance payments of three years of compensation under certain circumstances.

12. Retirement Plans

The Bank sponsors a profit-sharing plan that covers all employees with one year of service who have attained age twenty-one. Contributions are determined annually by the Board of Directors. During 2021, 2020, and 2019 the Board made safe harbor contributions which matched 100% of the first 3% of employee compensation and 50% of the next 2% of employee compensation for a maximum match of 4%, resulting in total of contributions of $148,189, $142,000, and $130,950, respectively.

The Bank has adopted a supplemental executive retirement plan for three of its executive officers. The plan provides fixed annual benefits to each participant at normal retirement or disability date. The benefits vest over the period from adoption to normal retirement age. The Bank recorded expenses, including interest, of $205,402, $189,979, and $186,883 for the years ended December 31, 2021, 2020, and 2019, respectively. These plans are funded by five life insurance contracts, with a face value of $3,000,000, which are owned by the Bank. During 2019, one of the three executives retired. He is receiving annual benefits in accordance with terms of the plan.

13. Related Party Transactions

Officers, directors and employees are depositors of the Bank. They receive the same deposit rates and terms as other customers with similar deposits. As of December 31, 2021 and 2020, the deposits of executive officers and directors were $18,783,198 and $10,926,394, respectively.

Executive officers and directors of the Bank enter into loan transactions with the Bank in the ordinary course of business. The terms of these transactions are similar to the terms provided to other borrowers entering into similar loan transactions.

A summary of the activity in these loans is as follows:

	2021	2020
Beginning balance	$ 12,573,568	$ 11,932,096
Advances	165,000	2,954,019
Change in related parties	(5,830,483)	-
Repayments	(1,992,655)	(2,312,547)
Ending balance	$ 4,915,430	$ 12,573,568

Notes to Financial Statements

13. Related Party Transactions (Continued)

In 2005 the Bank entered into an agreement to lease a branch from a company owned by the Chairman of the Board of Directors. Rent paid to this company in 2021, 2020, and 2019 totaled $49,149, $48,735, and $48,322, respectively with additional executory costs of $5,083, $172, and $95 in 2021, 2020, and 2019, respectively. During 2021, 2020, and 2019 the Bank also purchased supplies totaling $220, $182, and $167, respectively, from a store owned by this director.

The Bank built a branch in Millsboro, Delaware upon land owned by a director. The Bank paid rent on the lease of this land totaling $46,923, $44,991, and $43,597 for 2021, 2020, and 2019, respectively. This director owns an auto body shop that performed $2,045 in repairs on the Bank automobile in 2020. During 2020 the Bank foreclosed on property that included land, buildings, and equipment. At the November 2020 auction of this property, this director purchased most of the equipment at a price of $825,000. The Bank has agreed to rent him the buildings in which the large production equipment is located at $1,000 per month beginning May 2021. During 2021, the Bank collected $8,000 rent.

14. Income Taxes

A reconciliation of the statutory federal income tax rates to the effective income tax rates follows:

	2021	2020	2019
Statutory federal income tax rate	21.0 %	21.0 %	21.0 %
Increase (decrease) in tax rate resulting from:			
Tax-exempt income	(1.1)	(1.0)	(1.0)
State tax, net of federal tax benefit	5.9	5.9	5.8
Other, net	0.1	(0.2)	0.1
Income tax expense	25.9 %	25.7 %	25.9 %

The components of income tax expense (benefits) are as follows:

	2021	2020	2019
Current			
Federal	$1,028,401	$1,060,030	$1,097,320
State	404,141	408,787	469,305
	1,432,542	1,468,817	1,566,625
Deferred	(120,498)	(127,010)	(117,659)
	$1,312,044	$1,341,807	$1,448,966

The components of the deferred taxes are as follows:

	2021	2020	2019
Provision for loan losses	$ 19,262	$ (175,551)	$ (160,324)
Writedowns of foreclosed real estate	(44,796)	8,612	2,350
Deferred gain on foreclosed property sales	2,168	44	8,603
Supplemental executive retirement plan	(43,698)	(37,803)	(40,253)
Interest on nonaccrual loans	11,522	66,974	(40,165)
Bonuses	(31,821)	-	-
Depreciation	(33,135)	10,714	112,130
	$ (120,498)	$ (127,010)	$ (117,659)

Notes to Financial Statements

14. Income Taxes (Continued)

The components of the net deferred tax asset are as follows:

	2021	2020	2019
Deferred tax assets			
Allowance for loan and letter of credit losses	$ 468,697	$ 487,959	$ 312,408
Foreclosed real estate writedowns	119,192	74,396	83,008
Deferred gain on foreclosed property sales	625	2,793	2,837
Supplemental executive retirement plan	468,565	424,867	387,064
Interest on nonaccrual loans	23,049	34,571	101,545
Bonuses	31,821	-	-
Unrealized loss on securities available for sale	510,609	-	-
	1,622,558	1,024,586	886,862
Deferred tax liability			
Unrealized gain on securities available for sale	-	109,848	50,720
Depreciation	439,741	472,876	462,162
	439,741	582,724	512,882
	$ 1,182,817	$ 441,862	$ 373,980

The Bank does not have material uncertain tax positions and did not recognize any adjustment for unrecognized tax benefits. The Bank remains subject to examination of income tax returns for the years ending after December 31, 2017.

15. Capital Standards

The Bank is subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory, and possible additional discretionary, actions by the regulators that, if undertaken, could have a direct material effect on 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 accounts and classifications are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

The Basel III Capital Rules became effective for the Bank on January 1, 2015 (subject to a phase-in period for certain provisions). With the adoption of the Basel III Capital Rules, the Bank elected to opt-out of the requirement to include accumulated other comprehensive income in Common Equity Tier 1 capital.

Common Equity Tier 1 capital consists of common stock, surplus, and undivided profits less disallowed deferred tax assets. Tier 1 capital includes Common Equity Tier 1 capital components with adjustments for certain investments and other items in which the Bank does not participate. Consequently, the Bank's Common Equity Tier 1 capital and Tier 1 capital are the same.

Total capital includes the allowance for loan losses, as limited based on total risk-weighted assets. In calculating risk-weighted assets, specified risk percentages are applied to each category of asset and off-balance sheet items.

Failure to meet the capital requirements could affect the Bank's ability to pay dividends and accept deposits and may significantly affect the operations of the Bank. Effective in 2016, a capital conservation buffer was phased in over four years, at the rate of .625% per annum, until it reached 2.5% of risk-weighted assets in 2019.

Notes to Financial Statements

15. Capital Standards (Continued)

The capital conservation buffer is not applied to the leverage, or Tier 1 capital to average assets, ratio. The buffer provides additional capital the Bank must hold to make the Bank more resilient during downturns in the economic cycle. If the Bank fails to meet the buffer, its ability to pay out dividends, buy back stock and pay discretionary bonuses will be limited.

As of its most recent regulatory examination, the Bank was considered well capitalized. Management knows of no conditions or events since the last regulatory examination that would change this classification.

The FDIC, through formal or informal agreement, has the authority to require an institution to maintain higher capital ratios than those provided by statute to be categorized as well capitalized under the regulatory framework for prompt corrective action.

The following table presents actual and required capital ratios as of December 31, 2021, and December 31, 2020, for the Bank under the Basel III Capital Rules.

(Dollars in thousands)	Actual		Minimum capital adequacy		To be well capitalized	
December 31, 2021	Amount	Ratio	Amount	Ratio	Amount	Ratio
Total capital (to risk-weighted assets)	$ 49,973	18.08%	$ 22,114	8.00%	$ 27,642	10.00%
Tier 1 capital (to risk-weighted assets)	$ 45,684	16.53%	$ 16,585	6.00%	$ 22,114	8.00%
Common equity tier 1 capital (to risk-weighted assets)	$ 45,684	16.53%	$ 12,438	4.50%	$ 17,967	6.50%
Capital conservation buffer	$ 27,859	10.08%	$ 6,910	2.50%		
Tier 1 capital (to average assets)	$ 45,684	9.20%	$ 19,855	4.00%	$ 24,819	5.00%
December 31, 2020	Amount	Ratio	Amount	Ratio	Amount	Ratio
Total capital (to risk-weighted assets)	$ 48,505	17.97%	$ 21,591	8.00%	$ 26,989	10.00%
Tier 1 capital (to risk-weighted assets)	$ 45,311	16.79%	$ 16,193	6.00%	$ 21,591	8.00%
Common equity tier 1 capital (to risk-weighted assets)	$ 45,311	16.79%	$ 12,145	4.50%	$ 17,543	6.50%
Capital conservation buffer	$ 26,914	9.97%	$ 6,747	2.50%		
Tier 1 capital (to average assets)	$ 45,311	10.15%	$ 17,859	4.00%	$ 22,324	5.00%

16. Fair Value Measures

The fair value of a financial instrument is the current amount that would be exchanged between willing parties, other than in a forced liquidation. The Financial Accounting Standards Board (FASB) defines fair value and establishes a framework for measuring fair value. Its guidance also establishes a hierarchy for determining fair value measurements. The hierarchy includes three levels and is based upon the valuation techniques used to measure assets and liabilities.

Level one uses inputs of quoted prices, unadjusted, for identical assets or liabilities in active markets. Level two inputs to the valuation method include quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument. Level three assumes inputs to the valuation method that are unobservable and significant to the fair value measurement.

Debt securities classified as available for sale are measured at fair value on a recurring basis. The fair value of municipal bonds classified as available for sale are estimated by applying spreads to curve using the municipal

Notes to Financial Statements

16. Fair Value Measures (Continued)

yield curve provided daily by market makers. The fair value of U.S. Treasury, U.S. Agency, mortgage-backed securities, and corporate bonds are calculated from a yield curve derived daily using various market makers. The values are generated by applying spreads to this curve. The Bank does not measure the fair value of any of its other financial assets or liabilities on a recurring basis.

The assets measured at fair value on a recurring basis are as follows:

		Fair value measurements using:		
December 31, 2021	Total	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Investment securities available for sale				
U.S. Treasury	$ 15,552,421	$ -	$ 15,552,421	$ -
U.S. government agency	9,140,416	-	9,140,416	-
Corporate	24,495,834	-	24,495,834	-
State and municipal	13,930,213	-	13,930,213	-
Mortgage-backed securities	46,966,061	-	46,966,061	-
	$ 110,084,945	$ -	$ 110,084,945	$ -
December 31, 2020				
Investment securities available for sale				
U.S. government agency	$ 5,339,793	$ -	$ 5,339,793	$ -
Corporate	1,286,172	-	1,286,172	-
State and municipal	9,189,634	-	9,189,634	-
Mortgage-backed securities	11,273,582	-	11,273,582	-
	$ 27,089,181	$ -	$ 27,089,181	$ -

Impaired loans are generally measured based on the fair value of the loan's collateral on a nonrecurring basis. Fair value is generally determined based upon independent third-party appraisals of the properties, or discounted cash flows based upon the expected proceeds. These assets are included as Level 3 fair values. As of December 31, 2021 and 2020, the fair values of impaired loans are estimated to be $767,363 and $2,131,110, respectively. As of December 31, 2021 and 2020, the fair values of these loans consist of recorded investment in loan balances of $1,123,612 and $2,374,300, net of valuation allowances of $356,249 and $243,190, respectively.

The Bank measures its foreclosed real estate, on a nonrecurring basis at fair value less costs to sell. As of December 31, 2021 and 2020, the fair value was estimated to be $2,894,697 and $3,299,858, respectively. The fair value of foreclosed real estate was based on offers and/or appraisals. Cost to sell the real estate was based on standard market factors. The Bank has categorized its foreclosed real estate as Level 3. The lack of an active local real estate market makes these fair values "best estimates" only. There is no assurance that the Bank will realize the recorded fair value of these properties as they are sold.

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INDEPENDENT AUDITOR'S REPORT

The Board of Directors and Stockholders
The Farmers Bank of Willards
Willards, Maryland

Opinion

We have audited the financial statements of The Farmers Bank of Willards, which comprise the balance sheet as of December 31, 2021, and the related statements of income, comprehensive income, changes in stockholders' equity, and cash flows for the year then ended, and the related notes to the financial statements.

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

Basis for Opinion

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

Responsibilities of Management for the Financial Statements

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

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

75th ANNIVERSARY
—1947 - 2022—

Auditors' Responsibilities for the Audit of the Financial Statements

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

In performing an audit in accordance with GAAS, we:

- Exercise professional judgement and maintain professional skepticism throughout the audit.
- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of The Farmers Bank of Willards' internal control. Accordingly, no such opinion is expressed.
- Evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the financial statements.
- Conclude whether, in our judgement, there are conditions or events, considered in the aggregate, that raise substantial doubt about The Farmers Bank of Willards' ability to continue as a going concern for a reasonable period of time.

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

Prior Period Financial Statements

The financial statements of The Farmers Bank of Willards as of and for the year ended December 31, 2020, were audited by other auditors, whose report dated March 9, 2021, expressed an unmodified opinion on those statements.

Yount, Hyde & Barbour, P.C.

Baltimore, Maryland
March 2, 2022

Average Balances, Interest, and Yields (Unaudited)

	For the Year Ended December 31, 2021			For the Year Ended December 31, 2020		
	Average balance	Interest	Yield	Average balance	Interest	Yield
Assets						
Federal funds sold	$ -	$ -	0.00%	$ 2,245,486	$ 3,439	0.15%
Interest bearing deposits	108,610,352	201,110	0.19%	52,220,408	160,402	0.31%
Investment securities						
U. S treasury	1,631,711	8,517	0.52%	5,810,444	106,921	1.84%
U. S. agency and MBS	30,520,894	420,914	1.38%	12,320,453	296,074	2.40%
State and municipal	10,160,199	205,247	2.02%	5,684,974	142,174	2.50%
Other	4,313,446	52,497	1.22%	1,145,749	35,027	3.06%
Total investment securities	46,626,250	687,175	1.47%	24,961,620	580,196	2.32%
Bank stock	1,212,087	54,013	4.46%	1,883,928	107,476	5.70%
Loans						
Commercial	34,869,654	2,389,880	6.85%	43,353,166	2,459,528	5.67%
Mortgage	254,402,624	13,870,368	5.45%	274,043,621	14,935,923	5.45%
Consumer	8,961,454	742,213	8.28%	7,956,598	699,770	8.79%
Total loans	298,233,732	17,002,461	5.70%	325,353,385	18,095,221	5.56%
Allowance for loan losses	3,159,497			3,416,149		
Total loans, net of allowance	295,074,235	17,002,461	5.76%	321,937,236	18,095,221	5.62%
Total interest-earning assets	451,522,924	17,944,759	3.97%	403,248,678	18,946,734	4.70%
Noninterest-bearing cash	10,920,835	-		6,150,485	-	
Premises and equipment	6,237,049	-		6,744,861	-	
Other assets	10,116,165	-		8,984,830	-	
Total assets	$478,796,973	$ 17,944,759		$425,128,854	$18,946,734	
Liabilities and Stockholders' Equity						
Interest-bearing deposits						
Savings and NOW deposits	$102,133,725	$ 237,586	0.23%	$ 76,428,385	$ 198,490	0.26%
Money market	42,421,007	129,546	0.31%	31,854,121	111,386	0.35%
Other time deposits	122,898,580	1,418,447	1.15%	130,353,861	2,034,817	1.56%
Total interest-bearing deposits	267,453,312	1,785,579	0.67%	238,636,367	2,344,693	0.98%
Borrowed funds	24,876,868	527,217	2.12%	35,117,788	742,967	2.12%
Total interest-bearing liabilities	292,330,180	2,312,796	0.79%	273,754,155	3,087,660	1.13%
Noninterest-bearing deposits	136,999,587	-		103,514,854	-	
	429,329,767	2,312,796		377,269,009	3,087,660	
Other liabilities	2,846,113	-		2,857,021	-	
Stockholders' equity	46,621,093	-		45,002,824	-	
Total liabilities and stockholders' equity	$478,796,973	$ 2,312,796		$425,128,854	$ 3,087,660	
Net interest spread			3.18%			3.57%
Net interest income		$15,631,963			$15,859,074	
Net margin on interest-earning assets			3.46%			3.93%

Interest on tax-exempt securities and loans is reported on a fully taxable equivalent basis.

EXECUTIVE and SENIOR OFFICERS

CHRISTOPHER F. DAVIS
President

WILLIAM S. TURNER
Executive Vice President

RENEE M. LOVELL
Chief Financial Officer

MARY K. O'CONNELL
Chief Operations Officer

TERRY B. SPARROW
Vice President of Information Systems

CELESTE M. RAYNE
Vice President of Worcester County Operations

JUSTIN M. GRAY
Vice President of Business Development

GEORGE O. BURBAGE
Vice President, Loan Officer

MATTHEW C. DAVIS
Vice President, Loan Officer

NATALIE N. BINDER
Treasurer

OTHER MANAGEMENT STAFF

KRIS DERICKSON
Assistant Vice President, Director of Human Resources and Talent Management

TINA SMACK
Assistant Vice President

KIMBERLY BENTON
Assistant Vice President, Loan Officer

HEATHER MARINE
Assistant Vice President Retail Operations

MARY DRYDEN
Assistant Vice President Special Assets

VICKIE DAVIS
Compliance, Bank Secrecy Act & Security Officer

IRINA POTAPENKO
Internal Auditor

SARAH STRICKLAND
Assistant Vice President, Loan Administration

ELIZABETH WALKER
CRA Officer