

FIRST MARINER BANCORP
Form 10-Q
August 14, 2013
Table of Contents

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

- QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934.**

For the quarterly period ended June 30, 2013.

- TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934.**

For the transition period from to

Commission file number: 0-21815

FIRST MARINER BANCORP

(Exact name of registrant as specified in its charter)

Edgar Filing: FIRST MARINER BANCORP - Form 10-Q

Maryland
(State of Incorporation)

52-1834860
(I.R.S. Employer Identification Number)

**1501 South Clinton Street, Baltimore,
MD**
(Address of principal executive offices)

21224
(Zip Code)

410-342-2600
(Telephone Number)

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 during the preceding 12 months (or for such shorter period that the registrant was required to file such report, and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically 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 (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No (Not Applicable)

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definitions of large accelerated filer, accelerated filer, and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

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

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

The number of shares of common stock outstanding as of August 9, 2013 is 19,705,896 shares.

Table of Contents

**FIRST MARINER BANCORP AND SUBSIDIARY
TABLE OF CONTENTS**

	Page
<u>PART I - FINANCIAL INFORMATION</u>	5
<u>Item 1 - Financial Statements</u>	5
<u>Consolidated Statements of Financial Condition as of June 30, 2013 (unaudited) and December 31, 2012</u>	5
<u>Consolidated Statements of Operations (unaudited) for the three and six months ended June 30, 2013 and 2012</u>	6
<u>Consolidated Statements of Comprehensive (Loss) Income (unaudited) for the three and six months ended June 30, 2013 and 2012</u>	7
<u>Consolidated Statements of Changes in Stockholders' Deficit (unaudited) for the six months ended June 30, 2013 and 2012</u>	8
<u>Consolidated Statements of Cash Flows (unaudited) for the six months ended June 30, 2013 and 2012</u>	9
<u>Notes to Consolidated Financial Statements (unaudited)</u>	10
<u>Item 2 - Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	36
<u>Item 3 - Quantitative and Qualitative Disclosures About Market Risk</u>	62
<u>Item 4 - Controls and Procedures</u>	63
<u>PART II - OTHER INFORMATION</u>	63
<u>Item 1 - Legal Proceedings</u>	63
<u>Item 1A - Risk Factors</u>	63
<u>Item 2 - Unregistered Sales of Equity Securities and Use of Proceeds</u>	64
<u>Item 3 - Defaults Upon Senior Securities</u>	64
<u>Item 4 - Mine Safety Disclosures</u>	64
<u>Item 5 - Other Information</u>	64
<u>Item 6 - Exhibits</u>	64
<u>Signatures</u>	65
<u>Exhibit Index</u>	66

Table of Contents

CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

Some of our statements contained in, or incorporated by reference into, this Quarterly Report on Form 10-Q are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. We intend such forward-looking statements to be covered by the safe harbor provisions for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995 and are including this statement for purposes of invoking these safe harbor provisions. Forward-looking statements are not guarantees of performance or results. When we use words like may, plan, contemplate, anticipate, believe, intend, expect, project, predict, estimate, target, could, is likely, should, would, will, and similar expressions, you should consider the forward-looking statements, although we may use other phrasing. These forward-looking statements involve risks and uncertainties and are based on our beliefs and assumptions and on the information available to us at the time that these disclosures were prepared. These forward-looking statements involve risks and uncertainties and may not be realized due to a variety of factors, including, but not limited to, the following:

- our ability to continue to operate as a going concern;
- our ability to successfully implement our liquidity contingency plan and meet our liquidity needs;
- our ability to raise sufficient capital to comply with the requirements of our regulators and for continued support of operations;
- our ability to realize the benefits from our cost saving initiatives;
- our ability to meet our interest payment obligations on our junior subordinated deferrable interest debentures upon expiration of the deferral period in 2013;
- our ability to successfully implement our plan to reduce First Mariner Bank's risk exposure to problem assets;
- the failure of assumptions underlying the establishment of our allowance for loan losses that may prove to be materially incorrect or may not be borne out by subsequent events;
- a reduction in the value of the collateral for loans made by us, especially real estate, which, in turn would likely reduce our customers borrowing power and the value of assets and collateral associated with our existing loans;

Edgar Filing: FIRST MARINER BANCORP - Form 10-Q

- increased loan delinquencies and/or an escalation in problem assets and foreclosures;
- a reduction in the value of certain assets held by us;
- the imposition of additional enforcement actions by bank regulatory authorities upon First Mariner Bank or First Mariner Bancorp;
- the success and timing of our business strategies and our ability to effectively carry out our business and capital plans;
- unanticipated regulatory or judicial proceedings;
- our ability to effectively manage market risk, credit risk, and operational risk;
- our ability to continue to realize income through our mortgage-banking operations;
- a decline in demand for our products and services;
- an inability to attract and retain deposits;
- the timely development of competitive new products and services and the acceptance of these products and services by new and existing customers;
- changes in consumer spending and savings habits;
- our ability to retain key employees;
- our estimates of self-insurance accruals and future liability;

Edgar Filing: FIRST MARINER BANCORP - Form 10-Q

Table of Contents

- the effect of any mergers, acquisitions, or other transactions to which we or our subsidiary may from time to time be a party;
- adverse changes in the securities markets;
- the risks of changes in interest rates on the level and composition of deposits, loan demand, and the values of loan collateral, securities, and interest-sensitive assets and liabilities;
- the effects of competition from other commercial banks, thrifts, mortgage-banking firms, consumer finance companies, credit unions, securities brokerage firms, insurance companies, money market and other mutual funds, and other financial institutions operating in our market area and elsewhere, including institutions operating regionally, nationally, and internationally, together with competitors offering banking products and services by mail, telephone, and the Internet;
- costs and potential disruption or interruption of operations due to cyber-security incidents;
- the effect of changes in accounting policies and practices, as may be adopted from time-to-time by bank regulatory agencies, the Securities and Exchange Commission, the Financial Accounting Standards Board, or other accounting standards setters;
- the effects of, and changes in, trade, monetary, and fiscal policies and laws, including interest rate policies of the Federal Reserve Board, inflation, interest rate, market, and monetary fluctuations;
- the strength of the United States economy in general, the strength of the local economies in which we conduct operations, and the unfavorable effects of future economic conditions, including inflation, recession, or decreases in real estate values;
- geopolitical conditions, including acts or threats of terrorism, actions taken by the United States or other governments in response to acts or threats of terrorism and/or military conflicts, which could impact business and economic conditions in the United States and abroad; and
- the risks described in this Quarterly Report on Form 10-Q and our Annual Report on Form 10-K as of and for the year ended December 31, 2012.

Edgar Filing: FIRST MARINER BANCORP - Form 10-Q

All written or oral forward-looking statements attributable to us are expressly qualified in their entirety by this Cautionary Note. Our actual results may differ significantly from those we discuss in these forward-looking statements. For other factors, risks, and uncertainties that could cause our actual results to differ materially from estimates and projections contained in these forward-looking statements, please read the Risk Factors in Item 1A of Part I of our Annual Report on Form 10-K as of and for the year ended December 31, 2012. Any forward-looking statement speaks only as of the date which such statement was made, and, except as required by law, we expressly disclaim any obligation or undertaking to disseminate any updates or revisions to any forward-looking statement to reflect events or circumstances after the date on which such statement is made or to reflect the occurrence of unanticipated events.

Table of Contents**PART I FINANCIAL INFORMATION****Item 1 Financial Statements****First Mariner Bancorp and Subsidiary****Consolidated Statements of Financial Condition***(dollars in thousands, except per share data)*

	June 30, 2013 (unaudited)	December 31, 2012
ASSETS		
Cash and due from banks	\$ 244,533	\$ 169,225
Federal funds sold and interest-bearing deposits	29,672	16,556
Securities available for sale (AFS), at fair value	82,044	57,676
Loans held for sale (LHFS), at fair value	177,508	404,289
Loans receivable	582,120	610,396
Allowance for loan losses	(9,876)	(11,434)
Loans, net	572,244	598,962
Real estate acquired through foreclosure	9,851	18,058
Restricted stock investments	3,517	7,099
Premises and equipment, net	38,453	37,651
Accrued interest receivable	3,009	4,387
Bank-owned life insurance (BOLI)	39,112	38,601
Prepaid expenses and other assets	16,147	25,025
Total assets	\$ 1,216,090	\$ 1,377,529
LIABILITIES AND STOCKHOLDERS' DEFICIT		
Liabilities:		
Deposits:		
Noninterest-bearing	\$ 101,537	\$ 109,966
Interest-bearing	1,024,610	1,076,864
Total deposits	1,126,147	1,186,830
Short-term borrowings	1,731	53,466
Long-term borrowings	40,000	73,515
Junior subordinated deferrable interest debentures	52,068	52,068
Accrued expenses and other liabilities (of which \$650 and \$248 are at fair value, respectively)	9,405	20,022
Total liabilities	1,229,351	1,385,901
Stockholders' deficit:		
Common stock, \$.05 par value; 75,000,000 shares authorized; 19,705,896 and 18,860,482 shares issued and outstanding, respectively	981	939
Additional paid-in capital	80,256	79,872
Accumulated deficit	(91,091)	(87,337)
Accumulated other comprehensive loss	(3,407)	(1,846)

Edgar Filing: FIRST MARINER BANCORP - Form 10-Q

Total stockholders' deficit	(13,261)	(8,372)
Total liabilities and stockholders' deficit	\$ 1,216,090	\$ 1,377,529

See accompanying notes to consolidated financial statements

Table of Contents**First Mariner Bancorp and Subsidiary****Consolidated Statements of Operations***(dollars in thousands except per share data)*

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
	(unaudited)			
Interest income:				
Loans	\$ 9,469	\$ 10,795	\$ 20,262	\$ 22,077
Securities and other earning assets	453	375	793	711
Total interest income	9,922	11,170	21,055	22,788
Interest expense:				
Deposits	2,772	2,871	5,725	5,959
Short-term borrowings	3	31	18	64
Long-term borrowings	755	921	1,775	1,853
Total interest expense	3,530	3,823	7,518	7,876
Net interest income	6,392	7,347	13,537	14,912
(reversal of) provision for loan losses		(428)	1,300	572
Net interest income after (reversal of) provision for loan losses	6,392	7,775	12,237	14,340
Noninterest income:				
Total other-than-temporary impairment (OTTI) charges		43		81
Less: Portion included in other comprehensive income (pre-tax)		(43)		(541)
Net OTTI charges on AFS securities				(460)
Mortgage-banking revenue	5,366	11,117	15,155	20,066
ATM fees	623	701	1,139	1,418
Service fees on deposits	701	623	1,327	1,304
Gain on sale of AFS securities	24		55	
Loss on disposition and sale of premises and equipment and other assets	(3)	(230)	(3)	(322)
Commissions on sales of nondeposit investment products	114	87	159	149
Gain on sale of minority interest in Mariner Finance	2,885		2,885	
Income from BOLI	252	287	511	580
Other	343	249	684	479
Total noninterest income	10,305	12,834	21,912	23,214
Noninterest expense:				
Salaries and employee benefits	6,425	5,552	13,305	11,331
Occupancy	1,968	2,286	4,258	4,508
Furniture, fixtures, and equipment	396	324	785	686
Professional services	1,910	739	2,717	1,112
Advertising	335	231	777	420
Data processing	418	402	621	834
ATM servicing expenses	92	226	197	453
Write-downs, losses, and costs of real estate acquired through foreclosure	1,012	940	3,697	2,214
Federal Deposit Insurance Corporation (FDIC) insurance premiums	1,128	1,074	2,338	2,122
Service and maintenance	791	564	1,507	1,155
Corporate Insurance	786	402	1,580	876
Consulting fees	417	316	829	924

Edgar Filing: FIRST MARINER BANCORP - Form 10-Q

Postage	943	422	1,994	681
Other	1,559	1,459	3,297	2,951
Total noninterest expense	18,180	14,937	37,902	30,267
Net (loss) income before income taxes	(1,483)	5,672	(3,753)	7,287
Income tax expense (benefit)	1		1	(205)
Net (loss) income	\$ (1,484)	\$ 5,672	\$ (3,754)	\$ 7,492
Net (loss) income per common share - basic and diluted	\$ (0.08)	\$ 0.30	\$ (0.20)	\$ 0.40

See accompanying notes to consolidated financial statements.

Table of Contents**First Mariner Bancorp and Subsidiary****Consolidated Statements of Comprehensive (Loss) Income***(dollars in thousands)*

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
	(unaudited)			
Net (loss) income	\$ (1,484)	\$ 5,672	\$ (3,754)	\$ 7,492
Other comprehensive (loss) income items:				
Unrealized holding (losses) gains on securities arising during the period (net of tax (benefit) expense of \$(708), \$127, \$(1,034), and \$431, respectively)	(1,046)	188	(1,528)	637
Reclassification adjustment for net (gains) losses on securities (net of tax (expense) benefit of \$(9), \$0, \$(22), and \$186, respectively) included in net (loss) income	(15)		(33)	274
Total other comprehensive (loss) income	(1,061)	188	(1,561)	911
Total comprehensive (loss) income	\$ (2,545)	\$ 5,860	\$ (5,315)	\$ 8,403

See accompanying notes to consolidated financial statements.

Table of Contents**First Mariner Bancorp and Subsidiary****Consolidated Statements of Changes in Stockholders Deficit***(dollars in thousands except per share data)*

	Six Months Ended June 30, 2013 (unaudited)					
	Number of Shares of Common Stock	Common Stock	Additional Paid-in Capital	Accumulated Deficit	Accumulated Other Comprehensive Loss	Total Stockholders Deficit
Balance at January 1, 2013	18,860,482	\$ 939	\$ 79,872	\$ (87,337)	\$ (1,846)	\$ (8,372)
Net loss				(3,754)		(3,754)
Common stock issued, net of costs	845,414	42	256			298
Stock-based compensation expense			530			530
Change in fair value of warrants			(402)			(402)
Changes in unrealized losses on securities, net of taxes					(1,561)	(1,561)
Balance at June 30, 2013	19,705,896	\$ 981	\$ 80,256	\$ (91,091)	\$ (3,407)	\$ (13,261)

	Six Months Ended June 30, 2012 (unaudited)					
	Number of Shares of Common Stock	Common Stock	Additional Paid-in Capital	Accumulated Deficit	Accumulated Other Comprehensive Loss	Total Stockholders Deficit
Balance at January 1, 2012	18,860,482	\$ 939	\$ 80,125	\$ (103,454)	\$ (3,022)	\$ (25,412)
Net income				7,492		7,492
Costs of common stock issued, net			(11)			(11)
Change in fair value of warrants			(100)			(100)
Changes in unrealized losses on securities, net of taxes					911	911
Balance at June 30, 2012	18,860,482	\$ 939	\$ 80,014	\$ (95,962)	\$ (2,111)	\$ (17,120)

See accompanying notes to consolidated financial statements.

Table of Contents**First Mariner Bancorp and Subsidiary****Consolidated Statements of Cash Flows***(dollars in thousands)*

	Six Months Ended June 30,	
	2013	2012
	(unaudited)	
Cash flows from operating activities:		
Net (loss) income	\$ (3,754)	\$ 7,492
Adjustments to reconcile net (loss) income to net cash from operating activities:		
Depreciation and amortization	1,385	1,413
Stock compensation	530	
(Accretion) amortization of unearned loan fees and costs, net	(213)	335
Amortization of discounts on mortgage-backed securities, net	28	2
Origination fees and gains on sale of mortgage loans	(14,493)	(18,812)
Net OTTI charges on AFS securities		460
Gain on sale of AFS securities	(55)	
Gain on sale of minority interest in Mariner Finance	(2,885)	
Loss on disposition and sale of premises and equipment and other assets	3	322
Decrease in accrued interest receivable	1,377	349
Provision for loan losses	1,300	572
Write-downs and losses on sale of real estate acquired through foreclosure	2,544	941
Increase in cash surrender value of BOLI	(511)	(580)
Originations of mortgage LHFS	(1,352,256)	(1,030,346)
Proceeds from sales of mortgage LHFS	1,586,249	984,690
Net (decrease) increase in accrued expenses and other liabilities	(10,703)	2,968
Net decrease (increase) in prepaids and other assets	8,818	(3,177)
Net cash provided by (used in) operating activities	217,364	(53,371)
Cash flows from investing activities:		
Loan principal repayments, net	23,584	35,462
Sales of held-for-investment loans	8,807	
Repurchase of loans previously sold	(1,114)	
Sale of restricted stock investments	3,582	199
Purchases of premises and equipment	(2,192)	(1,110)
Activity in AFS securities:		
Maturities/calls/repayments	5,363	5,252
Sales	4,515	
Purchases	(36,835)	(22,043)
Proceeds from sales of real estate acquired through foreclosure	7,297	6,511
Proceeds from sale of minority interest in Mariner Finance	4,000	
Net cash provided investing activities	17,007	24,271
Cash flows from financing activities:		
Net (decrease) increase in deposits	(60,684)	32,064
Net decrease in other borrowed funds	(85,251)	(350)
Net costs of stock issuance	(12)	(11)
Net cash (used in) provided by financing activities	(145,947)	31,703
Increase in cash and cash equivalents	88,424	2,603
Cash and cash equivalents at beginning of period	185,781	148,789
Cash and cash equivalents at end of period	\$ 274,205	\$ 151,392
Supplemental information:		
Interest paid on deposits and borrowed funds	\$ 6,756	\$ 7,126
Real estate acquired in satisfaction of loans	\$ 1,634	\$ 4,650

Edgar Filing: FIRST MARINER BANCORP - Form 10-Q

Transfers of LHFS to loan portfolio	\$	7,281	\$	342
-------------------------------------	----	-------	----	-----

See accompanying notes to consolidated financial statements

Table of Contents

First Mariner Bancorp and Subsidiary

Notes to Consolidated Financial Statements

*(Information as of and for the three and six months
ended June 30, 2013 and 2012 is unaudited)*

(1) Summary of Significant Accounting Policies

Basis of Presentation

The accompanying consolidated financial statements for First Mariner Bancorp have been prepared in accordance with the instructions for Form 10-Q and, therefore, do not include all information and notes necessary for a full presentation of financial condition, results of operations, and cash flows in conformity with accounting principles generally accepted in the United States of America (U.S.) (GAAP). The consolidated financial statements should be read in conjunction with the audited financial statements included in First Mariner Bancorp's Annual Report on Form 10-K as of and for the year ended December 31, 2012. When used in these notes, the terms the Company, we, us, and our refer to First Mariner Bancorp and, unless the context requires otherwise, its consolidated subsidiary.

The consolidated financial statements include the accounts of First Mariner and its wholly owned subsidiary, First Mariner Bank (the Bank). All significant intercompany accounts and transactions have been eliminated in consolidation. Events occurring after the date of the financial statements were considered in the preparation of the financial statements. Certain reclassifications have been made to amounts previously reported to conform to classifications made in 2013.

The consolidated financial statements as of June 30, 2013 and for the three and six months ended June 30, 2013 and 2012 are unaudited but include all adjustments, consisting only of normal recurring adjustments, which we consider necessary for a fair presentation of financial position and results of operations for those periods. The results of operations for the three and six months ended June 30, 2013 are not necessarily indicative of the results that will be achieved for the entire year or any future interim period.

The preparation of the financial statements in conformity with GAAP requires management to make estimates and judgments that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of 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 change in the near term relate to the determination of the allowance for loan losses (the allowance), loan repurchases and related valuations, real estate acquired through foreclosure, impairment of AFS securities, valuations of financial instruments, and deferred income taxes. In connection with these determinations, management evaluates historical trends and ratios and, where appropriate, obtains independent appraisals for significant properties and prepares fair value analyses. Actual results could differ significantly from those estimates.

(2) Going Concern Consideration

Due to the conditions and events discussed later in Note 5, there is substantial doubt regarding our ability to continue as a going concern. Management is taking various steps designed to improve the Company's and the Bank's capital position. The Bank has developed a written alternative capital plan designed to improve the Bank's capital ratios. Such plan is dependent upon a capital infusion to meet the capital requirements of the various regulatory agreements (see Note 5 for more information on the agreements). The Company continues to work with its advisors in an attempt to improve capital ratios.

The consolidated financial statements presented above and the accompanying Notes have been prepared on a going concern basis, which contemplates the realization of assets and the discharge of liabilities in the normal course of business for the foreseeable future, and does not include any adjustment to reflect the possible future effects on the recoverability and classification of assets, or the amounts and classification of liabilities that may result from the outcome of any extraordinary regulatory action, which would affect our ability to continue as a going concern.

(3) Securities

The composition of our securities portfolio (all AFS) is as follows:

Edgar Filing: FIRST MARINER BANCORP - Form 10-Q

Table of Contents

	June 30, 2013			
	Amortized Cost	Unrealized Gains	Unrealized Losses	Estimated Fair Value
(dollars in thousands)				
Mortgage-backed securities	\$ 11,106	\$ 74	\$ 569	\$ 10,611
Trust preferred securities	6,120		1,884	4,236
U.S. government agency notes	61,549	29	784	60,794
U.S. Treasury securities	4,768	2		4,770
Equity securities - banks	1,175		298	877
Equity securities - mutual funds	750	6		756
	\$ 85,468	\$ 111	\$ 3,535	\$ 82,044

	December 31, 2012			
	Amortized Cost	Unrealized Gains	Unrealized Losses	Estimated Fair Value
(dollars in thousands)				
Mortgage-backed securities	\$ 7,040	\$ 169	\$ 75	\$ 7,134
Trust preferred securities	11,246	79	2,144	9,181
U.S. government agency notes	33,435	107	5	33,537
U.S. Treasury securities	5,779	2		5,781
Equity securities - banks	1,288	16	48	1,256
Equity securities - mutual funds	750	37		787
	\$ 59,538	\$ 410	\$ 2,272	\$ 57,676

Contractual maturities of debt securities at June 30, 2013 are shown below. Actual maturities may differ from contractual maturities because borrowers have the right to call or prepay obligations with or without call or prepayment penalties.

	Amortized Cost	Estimated Fair Value
(dollars in thousands)		
Due in one year or less	\$ 27,520	\$ 27,143
Due after one year through five years	38,797	38,421
Due after ten years	6,120	4,236
Mortgage-backed securities	11,106	10,611
	\$ 83,543	\$ 80,411

The following tables show the level of our gross unrealized losses and the fair value of the associated securities by type and maturity for AFS securities:

Table of Contents

	Less than 12 months		June 30, 2013 12 months or more		Total	
	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses
	(dollars in thousands)					
Mortgage-backed securities	\$ 9,208	\$ 569	\$	\$	\$ 9,208	\$ 569
Trust preferred securities			4,236	1,884	4,236	1,884
U.S. government agency notes	41,535	784			41,535	784
Equity securities - banks	877	298			877	298
	\$ 51,620	\$ 1,651	\$ 4,236	\$ 1,884	\$ 55,856	\$ 3,535

	Less than 12 months		December 31, 2012 12 months or more		Total	
	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses
	(dollars in thousands)					
Mortgage-backed securities	\$ 3,552	\$ 75	\$	\$	\$ 3,552	\$ 75
Trust preferred securities			5,027	2,144	5,027	2,144
U.S. government agency notes	9,139	5			9,139	5
Equity securities - banks	1,035	47	123	1	1,158	48
	\$ 13,726	\$ 127	\$ 5,150	\$ 2,145	\$ 18,876	\$ 2,272

The trust preferred securities that we hold in our securities portfolio are issued by other banks, bank holding companies, and insurance companies. Certain of these securities have experienced declines in value since acquisition. These declines have occurred due to changes in the market which has limited the demand for these securities and reduced their liquidity. We consider the decline in value for four pooled trust preferred securities to be other than temporary and recorded the credit-related portion of the impairment as net OTTI of \$460,000 during the six months ended June 30, 2012. No additional OTTI charges were required during 2013. See additional information on the pooled trust preferred securities in Note 9.

The following shows the activity in OTTI related to credit losses for the six months ended June 30:

	2013		2012	
	(dollars in thousands)			
Balance at beginning of period	\$	9,190	\$	8,730
Additional OTTI taken for credit losses				460
Balance at end of period	\$	9,190	\$	9,190

All of the remaining securities that are impaired are so due to declines in fair values resulting from changes in interest rates or increased credit/liquidity spreads since the time they were purchased. We have the intent to hold these debt securities to maturity, and, for debt and equity securities in a loss position, for the foreseeable future and do not intend, nor do we believe it is more likely than not, that we will be required to sell the securities before anticipated recovery. We expect these securities will be repaid in full, with no losses realized. As such, management considers the impairments to be temporary.

At June 30, 2013, we held securities with an aggregate carrying value (fair value) of \$45.4 million that we have pledged as collateral for certain mortgage-banking and hedging activities, borrowings, government deposits, and customer deposits.

(4) Loans Receivable (Financing Receivables) and Allowance for Loan Losses

Loans receivable are summarized as follows:

Edgar Filing: FIRST MARINER BANCORP - Form 10-Q

Table of Contents

	June 30, 2013	December 31, 2012
	(dollars in thousands)	
Commercial	\$ 49,084	\$ 47,838
Commercial mortgage	247,730	263,763
Commercial construction	48,456	49,931
Consumer construction	17,905	18,668
Residential mortgage	107,446	111,376
Consumer	110,615	117,581
Total loans	581,236	609,157
Unearned loan fees, net	884	1,239
	\$ 582,120	\$ 610,396

Included in consumer loan totals in the above table are overdrawn commercial and retail checking accounts totaling \$322,000 as of June 30, 2013 and \$919,000 as of December 31, 2012.

Transferred Loans

In accordance with the Financial Accounting Standards Board (FASB) guidance on mortgage-banking activities, any loan which is originally originated for sale into the secondary market and which we subsequently elect to transfer into the Company s loan portfolio is valued at fair value at the time of the transfer with any decline in value recorded as a charge against earnings.

Information on the activity in transferred loans and related accretable yield is as follows for the three months ended June 30:

	Loan Balance		Accretable Yield		Total	
	2013	2012	2013	2012	2013	2012
	(dollars in thousands)					
Beginning balance	\$ 18,335	\$ 12,117	\$ 208	\$ 47	\$ 18,127	\$ 12,070
Loans transferred	6,447	226			6,447	226
Charge-offs		(213)		(6)		(207)
Payments/accretion	(5,525)	(1,257)	(64)	(5)	(5,461)	(1,252)
Ending balance	\$ 19,257	\$ 10,873	\$ 144	\$ 36	\$ 19,113	\$ 10,837

Information on the activity in transferred loans and related accretable yield is as follows for the six months ended June 30:

	Loan Balance		Accretable Yield		Total	
	2013	2012	2013	2012	2013	2012
	(dollars in thousands)					
Beginning balance	\$ 17,501	\$ 14,008	\$ 220	\$ 266	\$ 17,281	\$ 13,742
Loans transferred	7,281	342			7,281	342
Charge-offs		(285)		(14)		(271)
Payments/accretion	(5,525)	(3,192)	(76)	(216)	(5,449)	(2,976)
Ending balance	\$ 19,257	\$ 10,873	\$ 144	\$ 36	\$ 19,113	\$ 10,837

At June 30, 2013, we had pledged loans with a carrying value of \$96.3 million as collateral for Federal Home Loan Bank (FHLB) advances.

Credit Quality

Management has an established methodology to determine the adequacy of the allowance for loan losses that assesses the risks and losses inherent in the loan portfolio. For purposes of determining the allowance for loan losses, we have segmented our loan portfolio by product type. Our portfolio loan segments are commercial, commercial mortgage, commercial construction, consumer construction, residential mortgage, and consumer. We have looked at all segments to determine if subcategorization into classes is warranted based upon our credit review methodology. We have divided consumer loans into two classes, (1) home equity and second mortgage loans and (2) other consumer loans.

To establish the allocated portion of the allowance for loan losses, loans are pooled by portfolio class and an historical loss percentage is applied to each class. The historical loss percentage is based upon a rolling 24-month history, which gives us the most

Table of Contents

relevant charge-off data. The result of that calculation for each loan class is then applied to the current loan portfolio balances to determine the required allocated portion of the allowance for loan loss level per loan class. We then apply additional loss multipliers to the different classes of loans to reflect various environmental factors. This amount is considered our unallocated allowance. These factors capture any changes in economic trends, portfolio composition, real estate trends, as well as other factors and are meant to supplement the required allocated allowance. For individually evaluated loans (impaired loans), we do additional analyses to determine the impairment amount. In general, this impairment is included as part of the allocated allowance for loan losses for troubled debt restructures (TDR or TDRs) and is charged off for all other impaired loans. These loss estimates are performed under multiple economic scenarios to establish a range of potential outcomes for each criterion. Management applies judgment to develop its own view of loss probability within that range, using external and internal parameters with the objective of establishing an allowance for loss inherent within these portfolios as of the reporting date.

The following tables presents by portfolio segment, the changes in the allowance for loan losses, and the recorded investment in loans:

Table of Contents

	Three months ended June 30, 2013							
	Commercial	Commercial Mortgage	Commercial Construction	Consumer Construction	Residential Mortgage	Consumer	Unallocated	Total
	(dollars in thousands)							
Beginning Balance	\$ 2,153	\$ 1,677	\$ 437	\$ 11	\$ 1,882	\$ 1,877	\$ 3,188	\$ 11,225
Charge-offs			(46)	(148)	(1,411)	(211)		(1,816)
Recoveries	91	138			212	26		467
Net recoveries (charge-offs)	91	138	(46)	(148)	(1,199)	(185)		(1,349)
(Reversal of) provision for loan losses	(1,082)	(281)	(153)	221	1,375	(104)	24	
Ending Balance	\$ 1,162	\$ 1,534	\$ 238	\$ 84	\$ 2,058	\$ 1,588	\$ 3,212	\$ 9,876
	Six months ended June 30, 2013							
	Commercial	Commercial Mortgage	Commercial Construction	Consumer Construction	Residential Mortgage	Consumer	Unallocated	Total
	(dollars in thousands)							
Beginning Balance	\$ 2,070	\$ 1,254	\$ 414	\$ 20	\$ 1,774	\$ 2,040	\$ 3,862	\$ 11,434
Charge-offs	(129)	(1,087)	(134)	(148)	(1,706)	(368)		(3,572)
Recoveries	93	149			326	146		714
Net (charge-offs) recoveries	(36)	(938)	(134)	(148)	(1,380)	(222)		(2,858)
(Reversal of) provision for loan losses	(872)	1,218	(42)	212	1,664	(230)	(650)	1,300
Ending Balance	\$ 1,162	\$ 1,534	\$ 238	\$ 84	\$ 2,058	\$ 1,588	\$ 3,212	\$ 9,876
Ending balance - individually evaluated for impairment	\$ 109	\$ 33	\$	\$	\$ 147	\$	\$	\$ 289
Ending balance - collectively evaluated for impairment	1,053	1,501	238	84	1,911	1,588	3,212	9,587
	\$ 1,162	\$ 1,534	\$ 238	\$ 84	\$ 2,058	\$ 1,588	\$ 3,212	\$ 9,876
Ending loan balance - individually evaluated for impairment	\$ 14,197	\$ 28,158	\$ 9,648	\$ 16	\$ 14,974	\$ 1,266		\$ 68,259
Ending loan balance - collectively evaluated for impairment	34,976	219,561	38,803	18,090	92,080	110,351		513,861
	\$ 49,173	\$ 247,719	\$ 48,451	\$ 18,106	\$ 107,054	\$ 111,617		\$ 582,120

Edgar Filing: FIRST MARINER BANCORP - Form 10-Q

Table of Contents

	Three months ended June 30, 2012							
	Commercial	Commercial Mortgage	Commercial Construction	Consumer Construction	Residential Mortgage	Consumer	Unallocated	Total
Beginning Balance	\$ 2,778	\$ 1,871	\$ 1,857	\$ 170	\$ 2,650	\$ 2,518	\$ 1,677	\$ 13,521
Charge-offs		(94)				(546)		(640)
Recoveries		612			384	73		1,069
Net recoveries (charge-offs)		518			384	(473)		429
Provision for (reversal of) loan losses	119	(827)	(179)	(40)	(1,530)	205	1,824	(428)
Ending Balance	\$ 2,897	\$ 1,562	\$ 1,678	\$ 130	\$ 1,504	\$ 2,250	\$ 3,501	\$ 13,522

	Six months ended June 30, 2012							
	Commercial	Commercial Mortgage	Commercial Construction	Consumer Construction	Residential Mortgage	Consumer	Unallocated	Total
Beginning Balance	\$ 2,768	\$ 2,011	\$ 1,809	\$ 156	\$ 2,711	\$ 2,632	\$ 1,714	\$ 13,801
Charge-offs	(187)	(320)	(147)	(7)	(514)	(938)		(2,113)
Recoveries		612	52		420	178		1,262
Net (charge-offs) recoveries	(187)	292	(95)	(7)	(94)	(760)		(851)
Provision for (reversal of) loan losses	316	(741)	(36)	(19)	(1,113)	378	1,787	572
Ending Balance	\$ 2,897	\$ 1,562	\$ 1,678	\$ 130	\$ 1,504	\$ 2,250	\$ 3,501	\$ 13,522

Ending balance - individually evaluated for impairment	\$ 4	\$ 31	\$	\$	\$ 234	\$	\$	\$ 269
--	------	-------	----	----	--------	----	----	--------

Ending balance - collectively evaluated for impairment	2,893	1,531	1,678	130	1,270	2,250	3,501	13,253
	\$ 2,897	\$ 1,562	\$ 1,678	\$ 130	\$ 1,504	\$ 2,250	\$ 3,501	\$ 13,522

Ending loan balance - individually evaluated for impairment	\$ 3,757	\$ 27,642	\$ 17,148	\$ 669	\$ 17,934	\$ 1,135		\$ 68,285
Ending loan balance - collectively evaluated for impairment	48,870	272,139	35,690	15,479	98,239	122,093		592,510
	\$ 52,627	\$ 299,781	\$ 52,838	\$ 16,148	\$ 116,173	\$ 123,228		\$ 660,795

We use creditworthiness categories to grade commercial loans. Our internal grading system is based on experiences with similarly graded loans. Category ratings are reviewed each quarter. Our internal risk ratings are as follows:

Edgar Filing: FIRST MARINER BANCORP - Form 10-Q

Superior Credit Quality (RR1) This category includes credits that are secured by up to 95% advance against cash balances, municipal or corporate bonds carrying an A rating or better (subject to maturity), U.S. Government securities (subject to maturity), and fully marketable securities of companies with an A or better debt rating. In addition, the borrower must have a reasonable financial condition evidenced by complete financial statements.

High Credit Quality (RR2) This category includes credits that are secured by up to 70% advance against municipal or corporate bonds carrying an A rating or better, U.S. Government securities, and marketable securities of companies with an A or better debt rating. For individual credits, the credit must be secured by any of the aforementioned items or first deed of

Table of Contents

trust on residential owner-occupied property with a loan-to-value (LTV) ratio of 80% or less and adequate cash flow to service the debt. Permanent real estate loans on fully-leased properties with A-rated tenants and a 70% or less LTV ratio with income coverage of 1.25 times or higher may qualify for this rating, with confirmation of tenants' financial condition. No commercial construction loans may carry this rating at inception. At June 30, 2013 and December 31, 2012, none of our loans carried this risk rating.

Above Average Credit Quality (RR3) This category includes business loans to publicly traded companies with a B rating or better, commercial construction loans with a contingent-free take-out or substantial pre-leasing (75% or more of leasable space) with an LTV ratio of 75% or less, residential construction loans with pre-sold units and an LTV ratio of 70% or less as long as sales are on a noncontingent basis and the overall project is progressing on schedule as originally determined, loans to individuals with liquid assets and strong net worth and the additional ability to service the debt from sources unrelated to the purpose of the credit extension, and monitored credits to borrowers of sound financial condition with approved advance rates providing adequate margin so that collateral can be easily liquidated within 90 days or less.

Average/Satisfactory Credit Quality (RR4) In general, this category includes small-to-medium sized companies with satisfactory financial condition, cash flow, profitability, and balance sheet and income statement ratios, term loans and revolving credits with annual clean-up requirements, the majority of retail commercial credits, loans to partnerships or small businesses, most wholesale sales finance lines, wholesale distributors whose capital position and profitability are at Risk Management Association averages, and loans to individuals with acceptable financial condition and sufficient net cash flow to service the debt as long as the source of repayment is identifiable and sufficient to liquidate the debt within an acceptable period of time and a secondary source of repayment is evident.

Acceptable With Care (RR5) This category includes secured loans to small- or medium-sized companies which have suffered a financial setback where a convincing plan for correction demonstrates the deficiency is temporary in nature, loans with debt service coverage ratios below or LTV ratios above policy guidelines, most construction and development loans, permanent loans underwritten based on pro forma rents as opposed to historical or actual rents, real estate loans where the project is moderately off the original projections as to cost estimates or absorption, and loans where the interest reserve is no longer adequate but the customer or guarantor has a proven ability to carry the interest expense out of pocket for an extended time period without undue financial strain. These credits require additional attention by the account officer and/or loan administration.

Watch Credits (RR6) This category includes loans to borrowers who have experienced a temporary setback or deterioration in financial condition that should correct itself during the next twelve months, companies whose financial condition has been marginally acceptable for a period of time and prospects for significant improvement are limited, loans to individuals with marginal financial condition, and most credits for start-up operations. Also included in this category are real estate loans where the project is moderately off original projections, interest reserve may be depleted, with the borrower or guarantor having a questionable or unproved ability to pay interest out of pocket. Such loans may have modest cost overruns that will cause a shortage in the budget, raising question as to how the project will be completed. These loans may have a good collateral position, additional collateral, or strong guarantors to mitigate the risk. These credits are considered marginally acceptable, and greater than usual attention is warranted by the account officer and/or loan administration.

Special Mention (RR7) special mention credits are characterized as adequately covered by collateral (if any) and/or the paying capacity of the borrower, but are subject to one or more deteriorating trends. These credits constitute an undue and unwarranted credit risk, but not to the point of justifying a classification of substandard. These credits have potential weaknesses which, if not examined and corrected, may weaken the asset or inadequately protect the Bank's credit position at some future date. This category should not be used to list assets that bear risks usually associated with the particular type of financing. Assets with this rating may have the potential for significant weakness. Loans where weaknesses are evident and significant must be considered for more serious criticism. Examples of credits carried in special mention may include the following:

- loans which are fully covered by collateral and cash flow, but where margins are inadequate;
- loans to borrowers with a strong capital base, who are experiencing modest losses;
- loans to borrowers with very strong cash flows, but experiencing modest losses;
- credits that are subject to manageable, but excessive, leverage;
- credits with material collateral documentation exceptions, but which appear to be strong credits;
- credits to customers who have not provided the Bank with current or satisfactory financial data (unless the credit is

Table of Contents

secured by liquid marketable collateral or guaranteed by financially sound parties);

- credits that the account officer may be unable to supervise properly because of a lack of expertise or lack of control over the collateral and/or its condition;
- loans with deficient documentation or other deviations from prudent lending practices; and
- loans with strong guarantors and/or secondary sources of cash flow are the support for repayment.

Substandard (RR8) Substandard loans are inadequately protected by the current sound worth and paying capacity of the obligor or the collateral pledged, if any. Loans so classified have a well-defined weakness or weaknesses, which jeopardize the orderly liquidation of the debt. They are characterized by the distinct possibility that the Bank will sustain some loss if the deficiencies are not corrected. The borrower's financial condition indicates an inability to repay, even if restructured. Prospects for improvement in the borrower's financial condition are poor. Primary repayment source appears to be shifting from cash flow to liquidation of collateral. Examples of substandard credits may include the following:

- credits adequately covered by collateral value, where repayment is dependent upon the sale of nonliquid collateral, nontrading assets, or from guarantors;
- loans secured by collateral greater than the amount of the credit, but where cash flow is inadequate to amortize the debt over a reasonable period of time;
- credits with negative financial trends coupled with material collateral documentation deficiencies or where there is a high potential for loss of principal;
- unsecured loans to borrowers whose financial condition does not warrant unsecured advances;
- credits where the borrower is in bankruptcy or the work out effort is proceeding toward legal remedies including foreclosure; and
- all nonaccrual loans.

Doubtful (RR9) Doubtful classifications 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. A doubtful classification may be appropriate in cases where significant risk exposures are perceived, but loss cannot be determined because of specific, reasonable, and pending factors which may strengthen and work to the advantage of the credit in the near term. Account officers attempt to identify any principal loss in the credit, where possible, thereby limiting the excessive use of the doubtful classification. The classification is a deferral of the estimated loss until its more exact status may be determined. Pending factors include proposed mergers, acquisition or liquidation procedures, new capital injection, perfecting liens on additional collateral, and refinancing plans. At June 30, 2013 and December 31, 2012, none of our loans carried this risk rating.

Loss (RR10) Losses must be taken as soon as they are realized. In some instances and on a temporary basis, a portion of a loan may receive this rating (split rating) when the actual loss cannot be currently identified. In these instances, additional facts or information is necessary to determine the final amount to be charged against the allowance. When applied for these purposes, this risk rating may be used for a period not to exceed six months. Subsequent to the identification of this split rating, the remaining balance will be risk rated substandard. This category includes advances in excess of calculated current fair value which are considered uncollectible and do not warrant continuance as bankable assets. This classification does not mean that the loan has absolutely no recovery or salvage value, but rather it is not practical or desirable to defer writing off this basically worthless asset even though partial recovery may occur in the future. Credits to distressed borrowers lacking an identifiable and realistic source of repayment are generally charged off. Loans where repayment is dependent upon events that are not predictable in terms of result or timing (such as protracted litigation) are generally charged off. At June 30, 2013 and December 31, 2012, none of our loans carried this risk rating.

Insufficient Information to Rate (RRX) This rating is designed to be a temporary rating until sufficient information is provided to properly evaluate the risk and assign a permanent rating. If adequate information is not provided in a timely manner, this credit will receive a minimum rating of RR6, requiring quarterly reporting go the Watch Committee. At June 30, 2013 and December 31, 2012, none of our loans carried this risk rating.

Edgar Filing: FIRST MARINER BANCORP - Form 10-Q

Table of Contents

The following table shows the credit quality breakdown of our commercial loan portfolio by class as of June 30, 2013 and December 31, 2012:

	Commercial		Commercial Mortgage		Commercial Construction		Consumer Construction		Total	
	2013	2012	2013	2012	2013	2012	2013	2012	2013	2012
	(dollars in thousands)									
RR8	\$ 2,590	\$ 2,678	\$ 20,701	\$ 26,262	\$ 9,950	\$ 10,708	\$	\$	\$ 33,241	\$ 39,648
RR7	7,910	7,268	21,701	17,174	10,608	10,355			40,219	34,797
RR6	9,155	9,966	43,746	48,754	14,106	15,151			67,007	73,871
RR5	18,567	16,008	99,487	101,312	13,053	12,781			131,107	130,101
RR4	10,919	11,971	58,994	67,044	734	907	18,106	18,837	88,753	98,759
RR3			3,090	3,168					3,090	3,168
RR1	32	16							32	16
	\$ 49,173	\$ 47,907	\$ 247,719	\$ 263,714	\$ 48,451	\$ 49,902	\$ 18,106	\$ 18,837	\$ 363,449	\$ 380,360

We do not individually grade residential mortgage or consumer loans. Such loans are classified as performing or nonperforming. Loan performance is reviewed each quarter. The following table shows performing and nonperforming (nonaccrual) residential mortgage and consumer loans by class as of June 30, 2013 and December 31, 2012:

	Residential Mortgage		Home Equity & 2nd Mortgage		Other Consumer		Total	
	2013	2012	2013	2012	2013	2012	2013	2012
	(dollars in thousands)							
Nonaccrual loans	\$ 5,609	\$ 8,826	\$ 1,087	\$ 961	\$ 179	\$ 12	\$ 6,875	\$ 9,799
Performing loans	101,445	102,519	94,384	100,844	15,967	16,874	211,796	220,237
	\$ 107,054	\$ 111,345	\$ 95,471	\$ 101,805	\$ 16,146	\$ 16,886	\$ 218,671	\$ 230,036

The following tables show the aging of our loans receivable by class. Also included are loans that are 90 days or more past due as to interest and principal and still accruing because they are well-secured and in the process of collection.

June 30, 2013:

	30-59 Days Past Due	60-89 Days Past Due	90 Days or More Past Due	Total Past Due	Current	Total Loans	90 Days or More and Accruing
	(dollars in thousands)						
Commercial	\$	\$	\$ 1,154	\$ 1,154	\$ 48,019	\$ 49,173	\$
Commercial mortgage	4,713	1,035	15,228	20,976	226,743	247,719	87
Commercial construction	93	12,708	3,909	16,710	31,741	48,451	
Consumer construction		415	16	431	17,675	18,106	
Residential mortgage	2,032	3,355	5,609	10,996	96,058	107,054	

Edgar Filing: FIRST MARINER BANCORP - Form 10-Q

Home equity and 2nd mortgage	2,946	838	1,087	4,871	90,600	95,471
Other consumer	163	6	181	350	15,796	16,146
	\$ 9,947	\$ 18,357	\$ 27,184	\$ 55,488	\$ 526,632	\$ 582,120
						\$ 89

December 31, 2012:

	30-59 Days Past Due	60-89 Days Past Due	90 Days or More Past Due	Total Past Due	Current	Total Loans	90 Days or More and Accruing
(dollars in thousands)							
Commercial	\$ 221	\$	\$ 2,110	\$ 2,331	\$ 45,576	\$ 47,907	\$
Commercial mortgage	8,233	1,698	21,269	31,200	232,514	263,714	
Commercial construction	2,127		4,637	6,764	43,138	49,902	
Consumer construction	1,075	331	645	2,051	16,786	18,837	
Residential mortgage	6,847	7,650	9,048	23,545	87,800	111,345	222
Home equity and 2nd mortgage	1,287	416	961	2,664	99,141	101,805	
Other consumer	13	7	12	32	16,854	16,886	
	\$ 19,803	\$ 10,102	\$ 38,682	\$ 68,587	\$ 541,809	\$ 610,396	\$ 222

Edgar Filing: FIRST MARINER BANCORP - Form 10-Q

Table of Contents

Impaired loans include nonaccrual loans and TDRs. The following tables show the breakout of impaired loans by class:

	June 30, 2013			Six Months Ended June 30,			2012		
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized	Charge-Offs	Average Recorded Investment	Interest Income Recognized	Charge-Offs
(dollars in thousands)									
With no related allowance:									
Commercial	\$ 6,916	\$ 6,916	\$	\$ 3,880	\$ 77	\$ 129	\$ 4,330	\$ 24	\$ 187
Commercial mortgage	\$ 26,412	\$ 26,412	\$	\$ 28,611	\$ 192	\$ 1,087	\$ 22,911	\$ 260	\$ 320
Commercial construction	\$ 9,648	\$ 9,648	\$	\$ 10,803	\$ 102	\$ 134	\$ 13,571	\$ 162	\$ 147
Consumer construction	\$ 16	\$ 16	\$	\$ 494	\$ 1	\$ 148	\$ 654	\$ 16	\$ 7
Residential mortgage	\$ 9,357	\$ 9,357	\$	\$ 10,913	\$ 160	\$ 1,559	\$ 9,490	\$ 186	\$ 346
Home equity & 2nd mortgage	\$ 1,087	\$ 1,087	\$	\$ 1,077	\$ 6	\$ 368	\$ 1,014	\$ 9	\$ 938
Other consumer	\$ 179	\$ 179	\$	\$ 67	\$ 3	\$	\$ 5	\$ 1	\$
With a related allowance:									
Commercial	7,172	7,281	109	7,161	97		156	2	
Commercial mortgage	1,713	1,746	33	1,828	26		4,705	68	
Commercial construction									
Consumer construction									
Residential mortgage	5,470	5,617	147	5,988	113	147	7,459	142	168
Home equity & 2nd mortgage									
Other consumer									
Total:									
Commercial	\$ 14,088	\$ 14,197	\$ 109	\$ 11,041	\$ 174	\$ 129	\$ 4,486	\$ 26	\$ 187
Commercial mortgage	\$ 28,125	\$ 28,158	\$ 33	\$ 30,439	\$ 218	\$ 1,087	\$ 27,616	\$ 328	\$ 320
Commercial construction	\$ 9,648	\$ 9,648	\$	\$ 10,803	\$ 102	\$ 134	\$ 13,571	\$ 162	\$ 147
Consumer construction	\$ 16	\$ 16	\$	\$ 494	\$ 1	\$ 148	\$ 654	\$ 16	\$ 7
Residential mortgage	\$ 14,827	\$ 14,974	\$ 147	\$ 16,901	\$ 273	\$ 1,706	\$ 16,949	\$ 328	\$ 514
Home equity & 2nd mortgage	\$ 1,087	\$ 1,087	\$	\$ 1,077	\$ 6	\$ 368	\$ 1,014	\$ 9	\$ 938
Other consumer	\$ 179	\$ 179	\$	\$ 67	\$ 3	\$	\$ 5	\$ 1	\$

	December 31, 2012		
	Recorded Investment	Unpaid Principal Balance	Related Allowance
(dollars in thousands)			
With no related allowance:			
Commercial	\$ 2,535	\$ 2,535	\$
Commercial mortgage	\$ 32,561	\$ 32,561	\$
Commercial construction	\$ 11,692	\$ 11,692	\$
Consumer construction	\$ 645	\$ 645	\$
Residential mortgage	\$ 11,776	\$ 11,776	\$
Home equity & 2nd mortgage	\$ 1,235	\$ 1,235	\$

Edgar Filing: FIRST MARINER BANCORP - Form 10-Q

Other consumer	\$	12	\$	12	\$
With a related allowance:					
Commercial		7,150		7,283	133
Commercial mortgage		1,734		1,757	23
Commercial construction					
Consumer construction					
Residential mortgage		6,243		6,414	171
Home equity & 2nd mortgage					
Other consumer					
Total:					
Commercial	\$	9,685	\$	9,818	\$ 133
Commercial mortgage	\$	34,295	\$	34,318	\$ 23
Commercial construction	\$	11,692	\$	11,692	\$
Consumer construction	\$	645	\$	645	\$
Residential mortgage	\$	18,019	\$	18,190	\$ 171
Home equity & 2nd mortgage	\$	1,235	\$	1,235	\$
Other consumer	\$	12	\$	12	\$

Table of Contents

	Number of Modifications	Six Months Ended June 30,				
		2013 Recorded Investment Prior to Modification	Recorded Investment After Modification (dollars in thousands)	Number of Modifications	2012 Recorded Investment Prior to Modification	Recorded Investment After Modification
Commercial	1	\$ 5,358	\$ 5,358	2	\$ 211	\$ 211
Commercial mortgage	3	396	430	6	2,749	2,757
Commercial construction				2	7,093	7,093
Residential mortgage	1	339	339	1	863	863
	5	\$ 6,093	\$ 6,127	11	\$ 10,916	\$ 10,924

The majority of our TDRs are the result of renewals where the only concession is that the interest rate is not considered to be a market rate. As such, the best illustration of the financial impact of the TDRs is the effect on the allowance for loan losses.

During the six months ended June 30, 2013, the allowance for loan losses for TDRs was decreased by \$38,000 (\$24,000 for commercial and \$24,000 for residential mortgage, partially offset by an increase of \$10,000 for commercial mortgage). During the six months ended June 30, 2013, we charged-off \$26,000 for a TDR commercial construction loan, \$147,000 in TDR residential mortgage loans and \$14,000 for a TDR commercial mortgage loan. We transferred one TDR residential mortgage loan in the amount of \$552,000 to real estate acquired through foreclosure. During the six months ended June 30, 2012, the allowance for loan losses for TDRs was reduced by \$14,000 (\$26,000 for commercial mortgage partially offset by an increase of \$12,000 for residential mortgage) and we charged-off \$192,000 for two TDR residential mortgage loans and transferred two TDR residential mortgage loans in the amount of \$516,000 to real estate acquired through foreclosure.

The following table shows defaults during the stated period of modifications made during the previous year:

	2013 Number of Modifications	Six Months Ended June 30,		2012 Recorded Investment
		Recorded Investment (dollars in thousands)	Number of Modifications	
Commercial		\$	\$ 1	\$ 22

(5) Regulatory Matters, Capital Adequacy, and Liquidity***Regulatory Matters and Capital Adequacy***

Various regulatory capital requirements administered by the federal banking agencies apply to First Mariner and the Bank. 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 our 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 assets, liabilities, and certain off-balance sheet items as calculated under regulatory accounting practices. The Bank's capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios of total and Tier I capital to risk-weighted assets, and of Tier I capital to average quarterly assets (leverage). As of both June 30, 2013 and December 31, 2012, the Bank was undercapitalized under the regulatory framework for prompt corrective action.

Edgar Filing: FIRST MARINER BANCORP - Form 10-Q

Table of Contents

Our regulatory capital amounts and ratios as of June 30, 2013 and December 31, 2012 were as follows:

	Actual Amount	Ratio	Minimum Requirements for Capital Adequacy Purposes Amount Ratio (dollars in thousands)		To be Well Capitalized Under Prompt Corrective Action Provision Amount Ratio	
June 30, 2013:						
Total capital (to risk-weighted assets):						
Consolidated	\$ (10,028)	(1.4)%	\$ 58,798	8.0%	\$ 73,498	10.0%
Bank	57,572	7.8%	58,898	8.0%	63,623	10.0%
Tier I capital (to risk-weighted assets):						
Consolidated	(10,028)	(1.4)%	29,399	4.0%	44,099	6.0%
Bank	48,353	6.6%	29,449	4.0%	44,174	6.0%
Tier I capital (to average quarterly assets):						
Consolidated	(10,028)	(0.8)%	50,703	4.0%	63,379	5.0%
Bank	48,353	3.8%	50,578	4.0%	63,222	5.0%
December 31, 2012:						
Total capital (to risk-weighted assets):						
Consolidated	\$ (6,525)	(0.8)%	67,262	8.0%	\$ 84,078	10.0%
Bank	61,292	7.3%	67,073	8.0%	83,841	10.0%
Tier I capital (to risk-weighted assets):						
Consolidated	(6,525)	(0.8)%	33,631	4.0%	50,447	6.0%
Bank	50,777	6.1%	33,536	4.0%	50,304	6.0%
Tier I capital (to average quarterly assets):						
Consolidated	(6,525)	(0.5)%	52,932	4.0%	66,165	5.0%
Bank	50,777	3.8%	52,873	4.0%	66,091	5.0%

The FDIC, through the Deposit Insurance Fund, insures deposits of accountholders up to \$250,000. The Bank pays an annual premium to provide for this insurance.

The Bank is a member of the FHLB System and is required to maintain an investment in the stock of the FHLB based on specific percentages of outstanding mortgages, total assets, or FHLB advances. Purchases and sales of stock are made directly with the Bank at par value.

On September 18, 2009, the Bank entered into an Agreement with the FDIC and the Commissioner of Financial Regulation for the state of Maryland (the Commissioner), pursuant to which it consented to the entry of an Order to Cease and Desist (the September Order), which directs the Bank to (i) increase its capitalization, (ii) improve earnings, (iii) reduce nonperforming loans, (iv) strengthen management policies and practices, and (v) reduce reliance on noncore funding. The September Order required the Bank to adopt a plan to achieve and maintain a leverage capital ratio of at least 7.5% and a total risk-based capital ratio of at least 11% by June 30, 2010. We did not meet the requirements at June 30, 2010, December 31, 2010, December 31, 2011, December 31, 2012, or June 30, 2013. The failure to achieve these capital requirements could result in further action by our regulators.

As part of the September Order, within 30 days after the end of each calendar year, the Bank must submit an annual budget and profit plan and a plan that takes into account the Bank's pricing structure, the Bank's cost of funds and how this can be reduced, and the level of provision expense for adversely classified loans. To address reliance on noncore funding, the Bank was required to submit a liquidity plan intended to reduce the Bank's reliance on noncore funding, wholesale funding sources, and high-cost rate-sensitive deposits. While the September Order is in effect, the Bank may not pay dividends or management fees without the FDIC's prior consent, may not accept, renew, or roll over any brokered deposits, and is restricted in the yields that it may pay on deposits.

First Mariner Bancorp is also a party to agreements with the Federal Reserve Board of Richmond (FRB) (the FRB Agreements), which, together, require it to: (i) develop and implement a strategic business plan that includes (a) actions that will be taken to improve our operating performance and reduce the level of parent company leverage, (b) a comprehensive budget and an expanded budget review process, (c) a description of the operating assumptions that form the basis for major projected income and expense components and provisions needed to maintain an adequate loan loss reserve, and (d) a capital plan incorporating all capital needs, risks, and regulatory guidelines; and (ii) submit plans to improve enterprise-wide risk management and effectiveness of internal audit programs. First Mariner Bancorp has also agreed to provide the FRB with advance notice of any significant capital transactions. The FRB Agreements also prohibit First Mariner and the Bank from taking any of the following actions without the FRB's prior

Table of Contents

written approval: (i) declaring or paying any dividends; (ii) taking dividends from the Bank; (iii) making any distributions of interest, principal, or other sums on First Mariner's subordinated debentures or trust preferred securities; (iv) incurring, increasing, or guaranteeing any debt; or (v) repurchasing or redeeming any shares of its stock. To satisfy the FRB's minimum capital requirements, First Mariner's consolidated Tier I capital to average quarterly assets, Tier I capital to risk-weighted assets, and total capital to risk-weighted assets ratios at each quarter end must be at least 4.0%, 4.0%, and 8.0%, respectively. At June 30, 2013, those capital ratios were (0.8)%, (1.4)%, and (1.4)%, respectively, which were not in compliance with the minimum requirements. The failure to achieve these capital requirements could result in further action by our regulators.

The foregoing will subject us to increased regulatory scrutiny and may have an adverse impact on our business operations. Failure to comply with the provisions of these regulatory requirements may result in more restrictive actions from our regulators, including more severe and restrictive enforcement actions.

Liquidity

The Bank's principal sources of liquidity are cash and cash equivalents (which are cash on hand and amounts due from financial institutions, federal funds sold, money market mutual funds, and interest bearing deposits), AFS securities, deposit accounts, and borrowings. The levels of such sources are dependent on the Bank's operating, financing, and investing activities at any given time. We attempt to primarily rely on core deposits from customers to provide stable and cost-effective sources of funding to support our loan growth. We also seek to augment such deposits with longer term and higher yielding certificates of deposit. Cash and cash equivalents, which totaled \$274.2 million at June 30, 2013, have immediate availability to meet our short-term funding needs. Our entire securities portfolio is classified as AFS, is highly marketable (excluding our holdings of pooled trust preferred securities), and is available to meet our liquidity needs. Additional sources of liquidity include LHFS, which totaled \$177.5 million at June 30, 2013, are committed to be sold into the secondary market, and generally are funded within 60 days and our residential real estate portfolio, which includes loans that are underwritten to secondary market criteria. Additionally, our residential construction loan portfolio provides a source of liquidity as construction periods generally range from 9-12 months, and these loans are subsequently refinanced with permanent first-lien mortgages and sold into the secondary market. We may also, from time to time, sell commercial or consumer loans to enhance our liquidity position and/or improve asset quality.

(6) Stock Options, Warrants, and Stock Incentives

We have stock option plans, which provide for the granting of options to acquire First Mariner common stock to our directors and key employees. Option exercise prices are equal to or greater than the fair market value of the common stock on the date of the grant.

We account for stock options issued under our stockholder-approved Long-Term Incentive Plan (the Plan) in accordance with FASB guidance on share-based payments. The Plan permits the granting of share options and shares to our directors and key employees. As of June 30, 2013, all options and warrants are fully vested and all compensation expense related to currently outstanding options and warrants has been recognized.

All options expire 10 years after the date of grant. The warrants expire five years after date of issuance.

Edgar Filing: FIRST MARINER BANCORP - Form 10-Q

Information with respect to stock options and warrants is as follows for the six months ended June 30:

		2013				2012		
	Number of Shares	Weighted- Average Exercise Price	Weighted- Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value (in thousands)	Number of Shares	Weighted- Average Exercise Price	Weighted- Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value (in thousands)
Outstanding at beginning of year	589,478	\$ 6.12			836,228	\$ 7.98		
Forfeited/cancelled	(56,550)	11.80			(241,400)	12.40		
Outstanding and exercisable at end of period	532,928	5.51	1.9	\$ 389	594,828	6.19	2.7	\$

There were no options or warrants granted or exercised during 2013 or 2012.

Table of Contents

Options and warrants outstanding are summarized as follows at June 30, 2013:

Exercise Price	Options and Warrants Outstanding and Exercisable (shares)	Weighted Average Remaining Contractual Life (in years)
\$ 1.09	18,348	2.0
1.15	347,826	1.7
4.15	11,200	4.8
5.41	2,754	4.5
5.70	19,500	4.7
13.33	7,300	3.8
16.67	4,800	1.8
16.70	1,800	2.3
16.95	2,300	0.3
17.45	16,250	2.5
17.77	70,850	1.6
18.20	4,950	0.8
18.38	16,650	0.5
18.94	2,350	3.4
19.30	6,050	2.8
	532,928	

During 2013, we issued 845,414 shares of common stock as an incentive under the Plan.

(7) (Loss) Income Per Share

Basic (loss) income per share is computed by dividing (loss) income available to common stockholders by the weighted-average number of common shares outstanding. Diluted (loss) income per share is computed after adjusting the denominator of the basic (loss) income per share computation for the effects of all dilutive potential common shares outstanding during the period. The dilutive effects of options, warrants, and their equivalents are computed using the treasury stock method.

Information relating to the calculation of (loss) income per common share is summarized as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
Weighted-average share outstanding - basic and diluted	19,552,065	18,860,482	19,206,274	18,860,482
Net (loss) income (<i>dollars in thousands</i>)	\$ (1,484)	\$ 5,672	\$ (3,754)	\$ 7,492

Edgar Filing: FIRST MARINER BANCORP - Form 10-Q

Basic and diluted (loss) income per share	\$	(0.08)	\$	0.30	\$	(0.20)	\$	0.40
---	----	--------	----	------	----	--------	----	------

Table of Contents**(8) Other Comprehensive (Loss) Income**

The following table presents the changes in the components of accumulated other comprehensive loss, net of tax, for the three months ended June 30:

	Accumulated Other Comprehensive Loss - AFS securities	
	2013	2012
	(dollars in thousands)	
Balance at beginning of period	\$ (2,346)	\$ (2,299)
Other comprehensive (loss) income before reclassification	(1,046)	188
Amounts reclassified to accumulated other comprehensive loss	(15)	
Net other comprehensive (loss) income during period	(1,061)	188
Balance at end of period	\$ (3,407)	\$ (2,111)

The following table presents the changes in the components of accumulated other comprehensive loss, net of tax, for the six months ended June 30:

	Accumulated Other Comprehensive Loss - AFS securities	
	2013	2012
	(dollars in thousands)	
Balance at beginning of period	\$ (1,846)	\$ (3,022)
Other comprehensive (loss) income before reclassification	(1,528)	637
Amounts reclassified (to) from accumulated other comprehensive loss	(33)	274
Net other comprehensive (loss) income during period	(1,561)	911
Balance at end of period	\$ (3,407)	\$ (2,111)

The followings table presents the amounts reclassified into the components of accumulated other comprehensive loss for the three months ended June 30, 2013 (there were no reclassification adjustments for the three months ended June 30, 2012):

	Accumulated Other Comprehensive Loss - AFS securities (dollars in thousands)	Affected Line Item in the Statement Where Net Loss is Presented
Realized gain on sale of AFS securities	\$ (24)	Gain on sale of AFS securities
		9 Tax expense
Total reclassification for period	\$ (15)	Net of tax

The followings tables presents the amounts reclassified (into) out of the components of accumulated other comprehensive loss for the six months ended June 30:

Table of Contents

	2013		Affected Line Item in the Statement Where Net Loss is Presented
	Accumulated Other Comprehensive Loss - AFS securities (dollars in thousands)		
Realized gain on sale of AFS securities	\$	(55)	Gain on sale of AFS securities
		22	Tax expense
Total reclassification for period	\$	(33)	Net of tax

	2012		Affected Line Item in the Statement Where Net Income is Presented
	Accumulated Other Comprehensive Loss - AFS securities (dollars in thousands)		
Net OTTI charges on AFS securities	\$	460	Net OTTI charges on AFS securities
		(186)	Tax benefit
Total reclassification for period	\$	274	Net of tax

(9) Fair Value of Financial Instruments

We group financial assets and financial liabilities measured 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 fair value. These 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 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.

We record transfers between levels at the end of the reporting period in which the change in significant inputs occurs.

Table of Contents**Financial Instruments Measured on a Recurring Basis**

The following table presents fair value measurements for assets, liabilities, and off-balance sheet items that are measured at fair value on a recurring basis:

	Carrying Value	Quoted Prices (Level 1)	June 30, 2013 Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Changes In Fair Values Included In Period Loss
(dollars in thousands)					
Securities:					
Mortgage-backed securities	\$ 10,611	\$	\$ 10,611	\$	\$
Trust preferred securities	4,236		3,045	1,191	
U.S. government agency notes	60,794		60,794		
U.S. Treasury securities	4,770		4,770		
Equity securities - banks	877		877		
Equity securities - mutual funds	756		756		
	\$ 82,044	\$	\$ 80,853	\$ 1,191	\$
Warrants	\$ 650	\$	\$	\$ 650	\$
LHFS	177,508		177,508		(12,529)
Interest rate lock commitments (IRLC or IRLCs) (notional amount of \$219,419)	218,734		218,734		(6,027)
Forward contracts to sell mortgage-backed securities (notional amount of \$261,855)	267,143		267,143		13,193

Table of Contents

	Carrying Value	Quoted Prices (Level 1)	December 31, 2012 Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Changes In Fair Values Included In Period Income
	(dollars in thousands)				
Securities:					
Mortgage-backed securities	\$ 7,134	\$	\$ 7,134	\$	\$
Trust preferred securities	9,181		8,226	955	(460)(1)
U.S. government agency notes	33,537		33,537		
U.S. Treasury securities	5,781		5,781		
Equity securities - banks	1,256		1,256		
Equity securities - mutual funds	787		787		
	\$ 57,676	\$	\$ 56,721	\$ 955	\$ (460)
Warrants	\$ 248	\$	\$	\$ 248	\$
LHFS	404,289		404,289		5,268
IRLCs (notional amount of \$404,645)	410,192		410,192		3,723
Forward contracts to sell mortgage-backed securities (notional amount of \$308,067)	306,682		306,682		(16,295)

(1) Represents net OTTI charges taken on certain Level 3 securities

Level 3 Financial Instruments

Financial instruments are considered Level 3 when their values are determined using pricing models, discounted cash flow methodologies, or similar techniques and at least one significant model assumption or input is unobservable. Level 3 financial instruments also include those for which the determination of fair value requires significant management judgment or estimation.

AFS Securities

The fair value of AFS securities is based on bid quotations received from securities dealers, bid prices received from an external pricing service, or modeling utilizing estimated cash flows, depending on the circumstances of the individual security.

As of June 30, 2013, \$1.2 million (\$10.8 million par value) of our AFS securities (four securities) were classified as Level 3, all of which were pooled trust preferred securities. The market environment has continued to be inactive for these security types and made fair value pricing more subjective. The fair value of these four securities is primarily a function of the credit quality of the issuer, although there is some sensitivity to interest rate changes. A change in the rating of a security will affect its value.

Edgar Filing: FIRST MARINER BANCORP - Form 10-Q

The amount of Level 3 securities will likely continue to be a function of market conditions and additional security transfers from Level 2 to Level 3 could result if further market inactivity occurs.

The following table details the four Level 3 securities:

	Class	Remaining Par Value (4)	Current Rating/Outlook (1)		Maturity	(2) Auction Call Date	(3) Index
			Moody's	Fitch			
ALESCO Preferred Funding VII	C-1	\$ 1,000	Ca	C	7/23/2035	MAR 2015	3ML + 1.5 %
ALESCO Preferred Funding XI	C-1	4,938	C	C	12/23/2036	JUNE 2016	3ML + 1.2 %
MM Community Funding	B	2,500	Ca	C	8/1/2031	N/A	6ML + 3.1 %
MM Community Funding IX	B-1	2,390	Ca	CC	5/1/2033	N/A	3ML + 1.8 %

(1) Ratings as of June 30, 2013.

(2) Under the terms of the offering, if the notes have not been redeemed in full prior to the indicated call date, then an auction of the collateral debt securities will be conducted and the collateral will be sold and the notes redeemed. If the auction is not successful, the collateral manager will conduct auctions on a quarterly basis until the rated notes are redeemed in full.

(3) 3/6ML - 3 or 6 Month LIBOR; LIBOR (London Interbank Offered Rate) daily reference rate based on the interest rates at which banks offer to lend unsecured funds to other banks in the London wholesale money market or interbank market.

(4) In thousands

Classification of Level 3 indicates that significant valuation assumptions are not consistently observable in the market and, as

Edgar Filing: FIRST MARINER BANCORP - Form 10-Q

Table of Contents

such, fair values are derived using the best available data. We calculated fair value for these four securities by using a present value of future cash flows model, which incorporated assumptions as follows as of June 30, 2013:

	Cumulative Default (1)	Deferrals Cured (2)	Credit MTM (3)(6)	Liquidity Premium (4)	Liquidity MTM Adj (5)(6)
ALESCO Preferred Funding VII	50%	3.3%	\$ 30.67	11%	\$ 26.82
ALESCO Preferred Funding XI	36%	5.8%	57.42	11%	41.20
MM Community Funding	65%	1.9%	20.13	11%	13.77
MM Community Funding IX	55%	8.1%	43.36	11%	35.31

-
- (1) The anticipated level of total defaults from the issuers within the pool of performing collateral as of June 30, 2013. There are no recoveries assumed on any default.
 - (2) Deferrals that are cured occur 60 months after the initial deferral starts.
 - (3) The credit mark to market (MTM) represents the discounted value of future cash flows after the assumptions of current and future defaults discounted at the book rate of interest on the security.
 - (4) The risk of being unable to sell the instrument for cash at short notice without significant costs, usually indicative of the level of trading activity for a specific security or class of securities.
 - (5) The liquidity mark to market adjustment on the security represents the difference between the value of the discounted cash flows based on the book interest rate and the value discounted at the liquidity premium. The credit MTM less the liquidity MTM equals the estimated fair value price of the security.
 - (6) Price per \$100.

Fair values were as follows:

	June 30, 2013		December 31, 2012	
	Model Result (1)	Fair Value (in thousands)	Model Result (1)(2)	Fair Value (in thousands)
ALESCO Preferred Funding VII	\$ 3.85	\$ 39	\$ 2.72	\$ 27
ALESCO Preferred Funding XI	16.22	801	11.84	585
MM Community Funding	6.36	159	5.86	146
MM Community Funding IX	8.05	192	8.14	197
		\$ 1,191		\$ 955

-
- (1) Price per \$100.
 - (2) Based on December 31, 2012 assumptions.

During 2012, we determined that, based on our most recent estimate of cash flows at the time, OTTI had occurred in our pooled trust preferred security portfolio. The amount of OTTI that was recognized through earnings was determined by comparing the present value of the expected cash flows to the amortized cost of the security. The discount rate used to determine the credit loss was the expected book yield on the security. The credit loss estimated under the aforementioned method that was charged to operating earnings totaled \$460,000 for the six months ended June 30, 2012. We did not recognize any OTTI charges in 2013.

Warrants

As of June 30, 2013, outstanding warrants were classified as Level 3. The fair value of the warrants is primarily a function of the Company's stock price. Changes in the price will create corresponding changes to the fair value of the warrants.

Table of Contents

The table below presents a reconciliation of financial instruments measured at fair value on a recurring basis using significant unobservable inputs (Level 3) during the three months ended June 30:

	2013		2012	
	Securities	Warrants	Securities	Warrants
	(dollars in thousands)			
Balance at beginning of period	\$ 1,004	\$ 223	\$ 720	\$ 119
Change in fair value included in additional paid-in capital		427		(1)
Total unrealized gains included in accumulated other comprehensive loss	187		43	
Balance at end of period	\$ 1,191	\$ 650	\$ 763	\$ 118

The table below presents a reconciliation of financial instruments measured at fair value on a recurring basis using significant unobservable inputs (Level 3) during the six months ended June 30:

	2013		2012	
	Securities	Warrants	Securities	Warrants
	(dollars in thousands)			
Balance at beginning of period	\$ 955	\$ 248	\$ 682	\$ 18
Change in fair value included in additional paid-in capital		402		100
Total realized losses included in other comprehensive income			(460)	
Total unrealized gains included in accumulated other comprehensive loss	236		541	
Balance at end of period	\$ 1,191	\$ 650	\$ 763	\$ 118

There were no transfers between any of Levels 1, 2, and 3 during the three or six months ended June 30, 2013 or June 30, 2012.

*Other Financial Instruments Measured on a Recurring Basis*LHFS

LHFS are carried at fair value, which is determined based on outstanding investor commitments or, in the absence of such commitments, based on current investor yield requirements or third party pricing models.

IRLCs

Edgar Filing: FIRST MARINER BANCORP - Form 10-Q

We engage an experienced independent third party to estimate the fair market value of our IRLCs. IRLCs are valued based upon mandatory pricing quotes from correspondent lenders less estimated costs to process and settle the loan. Fair value is adjusted for the estimated probability of the loan closing with the borrower.

Forward Contracts to Sell Mortgage-Backed Securities

Fair value of these commitments is determined based upon the quoted market values of the securities.

Table of Contents**Financial Instruments Measured on a Nonrecurring Basis**

We may be required, from time to time, to measure certain other financial assets and liabilities at fair value on a nonrecurring basis. These adjustments to fair value usually result from application of lower-of-cost-or-market (LCM) accounting or write-downs of individual assets. For assets measured at fair value on a nonrecurring basis, the following tables provide the level of valuation assumptions used to determine each adjustment and the carrying value of the assets:

	June 30, 2013			
	Carrying Value	Quoted Prices (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
	(dollars in thousands)			
Impaired loans	\$ 68,259	\$	\$	\$ 68,259
Real estate acquired through foreclosure	9,851			9,851

	December 31, 2012			
	Carrying Value	Quoted Prices (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
	(dollars in thousands)			
Impaired loans	\$ 75,910	\$	\$	\$ 75,910
Real estate acquired through foreclosure	18,058			18,058

Impaired Loans

Allowable methods for estimating fair value for impaired loans include using the fair value of the collateral for collateral dependent loans or, where a loan is determined not to be collateral dependent, using the discounted cash flow method.

If the impaired loan is identified as collateral dependent, then the fair value method of measuring the amount of impairment is utilized. This method requires obtaining a current independent appraisal or utilizing some other method of valuation for the collateral and applying a discount factor to the value based on our loan review policy and procedures.

If the impaired loan is determined not to be collateral dependent, then the discounted cash flow method is used. This method requires the impaired loan to be recorded at the present value of expected future cash flows discounted at the loan's effective interest rate. The effective interest rate of a loan is the contractual interest rate adjusted for any net deferred loan fees or costs, premiums, or discounts existing at origination or acquisition of the loan.

For all loans other than TDRs, a partial charge-off is recorded to reduce the carrying amount of the loan to its fair value. For TDRs that have an estimated fair value that is below the carrying value, an allocation of the allowance is established and remains part of the allowance until such time that it is determined the loan will proceed to foreclosure or is paid off. Total impaired loans had a carrying value of \$68.3 million and \$75.9 million as of June 30, 2013 and December 31, 2012, respectively, with allocated allowances of \$289,000 and \$327,000 as of June 30, 2013 and December 31, 2012, respectively.

See Note 4 for more detailed information about impaired loans by loan class.

Real Estate Acquired Through Foreclosure

We record foreclosed real estate assets at the LCM on their acquisition dates and at the lower of such initial amount or estimated fair value less estimated selling costs thereafter. Estimated fair value is generally based upon independent appraisal of the collateral or listing prices supported by broker recommendation. We consider these collateral values to be estimated using Level 3 inputs. We held real estate acquired through foreclosure of \$9.9 million as of June 30, 2013 and \$18.1 million as of December 31, 2012. During the six months ended June 30, 2013 and 2012, we added \$1.6 million and \$4.7 million, respectively, net of reserves, to real estate acquired through foreclosure and recorded write-downs and losses on sales, included in noninterest expense, of \$2.5 million and \$941,000, respectively. We disposed of \$7.3 million and \$6.5 million of foreclosed properties during the six months ended June 30, 2013 and 2012, respectively.

Table of Contents*All Financial Instruments*

The carrying value and estimated fair value of financial instruments are summarized in the following tables. The descriptions of the fair value calculations for AFS securities, LHFS, impaired loans, real estate acquired through foreclosure, warrants, IRLCs, and forward contracts to sell mortgage-backed securities are included in the discussions above.

	Carrying Value	June 30, 2013			Total
		Level 1	Fair Value		
			Level 2	Level 3	
(dollars in thousands)					
Assets:					
Cash and cash equivalents	\$ 274,205	\$ 274,205	\$	\$	\$ 274,205
AFS securities	82,044		80,853	1,191	82,044
LHFS	177,508		177,508		177,508
Loans receivable	582,120		514,272	68,259	582,531
Real estate acquired through foreclosure	9,851			9,851	9,851
Restricted stock investments	3,517	3,517			3,517
Liabilities:					
Deposits	1,126,147		1,133,383		1,133,383
Long- and short-term borrowings	41,731		43,574		43,574
Junior subordinated deferrable interest debentures	52,068		36,468		36,468
Warrants	650			650	650
Off Balance Sheet Items:					
IRLCs	218,734		218,734		218,734
Forward contracts to sell mortgage-backed securities	267,143		267,143		267,143

	Carrying Value	December 31, 2012			Total
		Level 1	Fair Value		
			Level 2	Level 3	
(dollars in thousands)					
Assets:					
Cash and cash equivalents	\$ 185,781	\$ 185,781	\$	\$	\$ 185,781
AFS securities	57,676		56,721	955	57,676
LHFS	404,289		404,289		404,289
Loans receivable	610,396		533,501	75,910	609,411
Real estate acquired through foreclosure	18,058			18,058	18,058
Restricted stock investments	7,099	7,099			7,099
Liabilities:					
Deposits	1,186,830		1,196,913		1,196,913
Long- and short-term borrowings	126,981		129,859		129,859
Junior subordinated deferrable interest debentures	52,068		37,018		37,018
Warrants	248			248	248
Off Balance Sheet Items:					
IRLCs	410,192		410,192		410,192
Forward contracts to sell mortgage-backed securities	306,682		306,682		306,682

Cash and Cash Equivalents

The carrying amount for cash and cash equivalents approximates fair value due to the short maturity of these instruments.

Loans Receivable

Loans were segmented into portfolios with similar financial characteristics. Loans were also segmented by type such as residential, multifamily, residential and nonresidential construction and land, home equity and second mortgage loans, commercial,

Table of Contents

and consumer. Each loan category was further segmented by fixed- and adjustable-rate interest terms and performing and nonperforming categories. The fair value of each loan category was calculated by discounting anticipated cash flows based on weighted-average contractual maturity, weighted-average coupon, and discount rate.

The fair value for nonperforming loans was determined utilizing FASB guidance on loan impairment. See above for fair value descriptions for impaired loans.

Restricted Stock Investments

The carrying value of restricted stock investments is a reasonable estimate of fair value as these investments do not have a readily available market.

Deposits

The fair value of deposits with no stated maturity, such as noninterest-bearing deposits, interest-bearing NOW accounts, money market, and savings accounts, is deemed to be equal to the carrying amounts. The fair value of certificates of deposit is based on the discounted value of contractual cash flows. The discount rate for certificates of deposit was estimated using the rate currently offered for deposits of similar remaining maturities.

Long- and Short-Term Borrowings and Junior Subordinated Deferrable Interest Debentures

Long- and short-term borrowings and junior subordinated notes were segmented into categories with similar financial characteristics. Carrying values were discounted using a cash flow approach based on market rates.

Limitations

Pricing or valuation models are applied using current market information to estimate fair value and such estimates are made at a specific point in time, based on relevant market information and information about financial instruments. These estimates do not reflect any premium or discount that could result from a one-time sale of our total holdings of a particular financial instrument. Because no market exists for a significant portion of our financial instruments, fair value estimates are based on judgments regarding future expected loss experience, current economic conditions, risk characteristics of various financial instruments, and other factors. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and therefore cannot be determined with precision. Accordingly, the estimates presented herein are not necessarily indicative of the amounts the Company could realize in a current market exchange. Changes in assumptions could significantly affect estimates.

(10) Segment Information

We are in the business of providing financial services, and we operate in two business segments commercial and

consumer banking and mortgage-banking. Commercial and consumer banking is conducted through the Bank and involves delivering a broad range of financial services, including lending and deposit taking, to individuals and commercial enterprises. This segment also includes our treasury and administrative functions. Mortgage-banking is conducted through First Mariner Mortgage, a division of the Bank, and involves originating first- and second-lien residential mortgages for sale in the secondary market and to the Bank.

The following tables present certain information regarding our business segments for the six months ended June 30:

Table of Contents

	Commercial and Consumer Banking	2013 Mortgage- Banking (dollars in thousands)	Total
Interest income	\$ 16,597	\$ 4,458	\$ 21,055
Interest expense	4,963	2,555	7,518
Net interest income	11,634	1,903	13,537
Provision for loan losses	1,300		1,300
Net interest income after provision for loan losses	10,334	1,903	12,237
Noninterest income	6,757	15,155	21,912
Noninterest expense	29,599	8,303	37,902
Net intersegment income	1,487	(1,487)	
Net (loss) income before income taxes	\$ (11,021)	\$ 7,268	\$ (3,753)
Total assets	\$ 1,038,582	\$ 177,508	\$ 1,216,090

	Commercial and Consumer Banking	2012 Mortgage- Banking (dollars in thousands)	Total
Interest income	\$ 19,190	\$ 3,598	\$ 22,788
Interest expense	6,578	1,298	7,876
Net interest income	12,612	2,300	14,912
Provision for loan losses	572		572
Net interest income after provision for loan losses	12,040	2,300	14,340
Noninterest income	3,148	20,066	23,214
Noninterest expense	24,824	5,443	30,267
Net intersegment income	759	(759)	
Net (loss) income before income taxes	\$ (8,877)	\$ 16,164	\$ 7,287
Total assets	\$ 974,973	\$ 247,118	\$ 1,222,091

(11) Subsequent Event

On July 1, 2013, we became self-insured with respect to employee-related health insurance claims. We use commercial insurance above our self-insured retentions to reduce our risk of catastrophic loss. Our reserves for self-insured losses are estimated based on employee claim history.

(12) Recent Accounting Pronouncements***Pronouncement Adopted***

In February 2013, FASB issued Accounting Standards Update (ASU) No. 2013-02, *Comprehensive Income (Topic 220) Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income*. ASU No. 2013-02 requires companies to report either on the income statement or disclose in the footnotes to the financial statements the effects on earnings from items that are reclassified out of the category of shareholder

equity called other comprehensive income and is effective for fiscal years and interim periods within such years beginning after December 15, 2012. We adopted the pronouncement effective January 1, 2013.

Pronouncement Issued

In March 2013, FASB issued ASU No. 2013-04, *Liabilities (Topic 405) Obligations Resulting From Joint and Several Liability Arrangements for Which the Total Amount of the Obligation Is Fixed at the Reporting Date*. ASU No. 2013-04 establishes guidance for the recognition, measurement, and disclosure of obligations arising from joint and several liability arrangements for which the total amount under the arrangement is fixed at the reporting date (e.g., debt arrangements, other contractual obligations, settled litigation, and judicial rulings) and is effective for fiscal years and interim periods within such years beginning after December 15, 2013.

Table of Contents

Item 2 - Management's Discussion and Analysis of Financial Condition and Results of Operations

When used in this report, the terms the Company, we, us, and our refer to First Mariner Bancorp and, unless the context requires otherwise, its consolidated subsidiary. The following discussion should be read and reviewed in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operations set forth in First Mariner Bancorp's Annual Report on Form 10-K for the year ended December 31, 2012.

The Company

First Mariner Bancorp is a bank holding company incorporated under the laws of Maryland and registered under the federal Bank Holding Company Act of 1956, as amended. First Mariner Bancorp's business is conducted primarily through its wholly-owned subsidiary, First Mariner Bank (the Bank). The Company had over 600 employees (approximately 594 full-time equivalent employees) as of June 30, 2013.

The Bank, with assets of \$1.2 billion as of June 30, 2013, is engaged in the general commercial banking business, with particular attention and emphasis on the needs of individuals and small to mid-sized businesses, and delivers a wide range of financial products and services that are offered by many larger competitors. The Bank's primary market area for its core banking operations, which consist of traditional commercial and consumer lending, as well as retail and commercial deposit operations, is central Maryland and portions of Maryland's eastern shore. Products and services of the Bank include traditional deposit products, a variety of consumer and commercial loans, residential and commercial mortgage and construction loans, wire transfer services, nondeposit investment products, and Internet banking and similar services. Most importantly, the Bank provides customers with access to local Bank officers who are empowered to act with flexibility to meet customers' needs in an effort to foster and develop long-term loan and deposit relationships. The Bank is an independent community bank and its deposits are insured by the Federal Deposit Insurance Corporation (FDIC).

First Mariner Mortgage, a division of the Bank, engages in mortgage-banking activities, providing mortgages and associated products to customers and selling most of those mortgages into the secondary market. First Mariner Mortgage had assets of \$177.5 million and \$404.3 million as of June 30, 2013 and December 31, 2012, respectively, and generated revenue of \$19.6 million and \$23.7 million, respectively, for the six months ended June 30, 2013 and 2012. First Mariner Mortgage recognized income before income taxes of \$7.3 million and \$16.2 million during the six months ended June 30, 2013 and 2012, respectively. During 2013, 47% of the originations were made in the state of Maryland, 18% in the immediately surrounding states and Washington, DC., and the remaining 35% in other states throughout the country. First Mariner Mortgage has offices in Maryland, Delaware, Virginia, and North Carolina. See Note 10 to the Consolidated Financial Statements for more detailed information on the results of our mortgage-banking operations.

Critical Accounting Policies

The Company's consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America (U.S.) (GAAP) and follow general practices within the industry in which it operates. Application of these principles requires management to make estimates, assumptions, and judgments that affect the amounts reported in the consolidated financial statements and accompanying notes. These estimates, assumptions, and judgments are based on information available as of the date of the consolidated financial statements; accordingly, as this information changes, the consolidated financial statements could reflect different estimates, assumptions, and

judgments. Certain policies inherently have a greater reliance on the use of estimates, assumptions, and judgments and, as such, have a greater possibility of producing results that could be materially different than originally reported. Estimates, assumptions, and judgments are necessary when assets and liabilities are required to be recorded at fair value, when a decline in the value of an asset not carried on the consolidated financial statements at fair value warrants an impairment write-down or valuation reserve to be established, or when an asset or liability needs to be recorded contingent upon a future event. Carrying assets and liabilities at fair value inherently results in more financial statement volatility. When applying accounting policies in such areas that are subjective in nature, management must use its best judgment to arrive at the carrying value of certain assets and liabilities. Below is a discussion of our critical accounting policies.

Securities

We designate securities into one of three categories at the time of purchase. Debt securities that we have the intent and ability to hold to maturity are classified as held to maturity and recorded at amortized cost. Debt and equity securities are classified as trading if bought and held principally for the purpose of sale in the near term. Trading securities are reported at estimated fair value, with unrealized gains and losses included in earnings. Debt securities not classified as held to maturity and debt and equity securities not classified as trading securities are considered available for sale and are reported at estimated fair value, with unrealized gains and losses reported as a separate component of stockholders' deficit, net of tax effects, in accumulated other comprehensive loss.

Available-for-sale (AFS) securities are evaluated periodically to determine whether a decline in their value is other than

Table of Contents

temporary. The term "other than temporary" is not intended to indicate a permanent decline in value. Rather, it means that the prospects for near-term recovery of value are not necessarily favorable, or that there is a lack of evidence to support fair values equal to, or greater than, the carrying value of the security.

The initial indications of other-than-temporary impairment (OTTI) for both debt and equity securities are a decline in the market value below the amount recorded for a security and the severity and duration of the decline. In determining whether an impairment is other than temporary, we consider the length of time and the extent to which the market value has been below cost, recent events specific to the issuer, including investment downgrades by rating agencies and economic conditions of its industry, our intent to sell the security, and if it is more likely than not that we will be required to sell the security before recovery of its amortized cost basis. For marketable equity securities, we also consider the issuer's financial condition, capital strength, and near-term prospects. For debt securities and for perpetual preferred securities that are treated as debt securities for the purpose of OTTI analysis, we also consider the cause of the price decline (general level of interest rates and industry- and issuer-specific factors), the issuer's financial condition, near-term prospects and current ability to make future payments in a timely manner, the issuer's ability to service debt, and any change in agencies' ratings at evaluation date from acquisition date and any likely imminent action. Once a decline in value is determined to be other than temporary, the security is segmented into credit- and noncredit-related components. Any impairment adjustment due to identified credit-related components is recorded as an adjustment to current period earnings, while noncredit-related fair value adjustments are recorded through accumulated other comprehensive loss. In situations where we intend to sell or it is more likely than not that we will be required to sell the security, the entire OTTI loss is recognized in earnings.

Gains or losses on the sales of securities are calculated using a specific-identification basis and are determined on a trade-date basis. Premiums and discounts on securities are amortized (accreted) over the term of the security using methods that approximate the interest method. Gains and losses on trading securities are recognized regularly in income as the fair value of those securities changes.

Loans

Allowance for loan losses (the "allowance")

Our allowance for loan losses represents an estimated amount that, in management's judgment, will be adequate to absorb probable incurred losses on existing loans. Management uses a disciplined process and methodology to establish the allowance each quarter. The allowance consists of an allocated component and an unallocated component. To determine the total allowance for loan losses, we estimate the allowance requirements for each loan class, including loans analyzed individually and loans analyzed on a pooled basis.

To determine the allocated component of the allowance account, loans are pooled by loan class and losses are modeled using historical experience over the loss emergence period. The models and assumptions used to determine the allowance are validated and reviewed to ensure that their theoretical foundation, assumptions, data integrity, computational processes, reporting practices, and end-user controls are appropriate and properly documented.

The unallocated allowance for loan losses represents environmental factors applied to each loan class and is based upon management's evaluation of various conditions that are not directly measured in the determination of the formula and other allocated allowances.

The establishment of the allowance for loan losses relies on a consistent process that requires multiple layers of management review and judgment and responds timely to changes in economic conditions and other influences. From time to time, events or economic factors may affect the loan portfolio, causing management to provide additional amounts to or release balances from the allowance for loan losses.

Management monitors differences between estimated and actual incurred loan losses utilizing charge-off history. Loans deemed uncollectible are charged against, while recoveries are credited to, the allowance. Management adjusts the level of the allowance through the provision for loan losses, which is recorded as a current period operating expense.

Commercial (including commercial mortgages) and construction loans (including both commercial and consumer) are generally evaluated for impairment when the loan becomes 90 days past due and/or is rated as substandard. The difference between the fair value of the collateral, less estimated selling costs and the carrying value of the loan is charged off at that time. Residential mortgage loans are generally charged down to their fair value when the loan becomes 120 days past due or is placed in nonaccrual status, whichever is earlier. Consumer loans are generally charged off when the loan becomes 120 days past due or when it is determined that the amounts due are uncollectible (whichever is earlier). The above charge-off guidelines may not apply if the loan is both well secured and in the process of collection. These charge-off policies have not changed in the last three years.

As an additional portion of the allowance for loan losses, we also estimate probable losses related to unfunded loan commitments. These commitments are subject to individual review and are analyzed for impairment the same as a correspondent loan.

Table of Contents

Impairment

We determine a loan to be impaired when, based on current information and events, it is probable that we will be unable to collect all amounts due according to the contractual terms of the loan agreement. In general, impaired loans consist of nonaccrual loans and troubled debt restructures (TDR or TDRs). We do not consider a loan impaired during a period of delay in payment if we expect to collect all amounts due, including interest past due. Generally we consider a period of delay in payment to include delinquency up to 90 days, but may extend this period if the loan is collateralized by residential or commercial real estate with a low loan-to-value (LTV) ratio and where collection and repayment efforts are progressing. We evaluate our commercial, commercial mortgage, commercial construction, and consumer construction classes of loans individually for impairment. We evaluate larger groups of smaller-balance homogeneous loans, which include our residential mortgage, home equity and second mortgage, and other consumer classes of loans, collectively for impairment.

We identify impaired loans and measure impairment (1) at the present value of expected cash flows discounted at the loan's effective interest rate, (2) at the observable market price, or (3) at the fair value of the collateral if the loan is collateral dependent. If our measure of the impaired loan is less than the recorded investment in the loan, we record a charge-off for the deficiency unless it is a TDR, for which we recognize an impairment loss through an allocated portion of the allowance for loan losses.

When the ultimate collectability of an impaired loan's principal is in doubt, wholly or partially, all cash receipts are applied to principal. Once the recorded principal balance has been reduced to an amount deemed to be fully collectible, cash receipts may be applied to previously foregone or current interest, and then recorded as recoveries of any amounts previously charged off. When all doubt about the full collectability of the loan is removed, cash receipts are applied under the contractual terms of the loan agreement.

Nonaccrual status

For smaller consumer loans, we place loans in nonaccrual status when they are contractually past due 90 days as to either principal or interest, unless the loan is well secured and in the process of collection, or earlier, when, in the opinion of management, the collection of principal and interest is in doubt. For all commercial loans, larger loans, and certain mortgage loans, management applies Financial Accounting Standards Board (FASB) guidance on impaired loan accounting to determine accrual status. Under that guidance, when it is probable that we will be unable to collect all payments due, including interest, we place the loan in nonaccrual status. A loan remains in nonaccrual status until the loan is current as to payment of both principal and interest and the borrower demonstrates the ability to pay and remain current. Specifically, in order for a nonaccrual loan to be returned to accrual status, a borrower must make six consecutive monthly payments and the borrower must demonstrate the ability to keep the loan current going forward. When a loan is partially charged off, the remaining balance remains in nonaccrual status.

As a result of our ongoing review of the loan portfolio, we may classify loans as nonaccrual even though the presence of collateral or the borrower's financial strength may be sufficient to provide for ultimate repayment. In general, loans are charged off when a loan or a portion thereof is considered uncollectible. We determine that the entire balance of a loan is contractually delinquent for all classes if the minimum payment is not received by the specified due date. Interest and fees continue to accrue on past due loans until the date the loan goes in nonaccrual status.

Income recognition

Interest income on loans is accrued at the contractual rate based on the principal outstanding. Loan origination fees and certain direct loan origination costs are deferred and amortized as a yield adjustment over the contractual loan terms or until the date of sale or disposition. Accrual of interest is discontinued when its receipt is in doubt, which typically occurs when a loan becomes impaired. Any interest accrued to income in the year when interest accruals are discontinued is generally reversed. Management may elect to continue the accrual of interest when a loan is in the process of collection and the estimated fair value of the collateral is sufficient to satisfy the principal balance and accrued interest. See additional information on loan impairment, nonaccrual status, and related interest recognition above.

Real estate acquired through foreclosure

We record real estate acquired through foreclosure at the lower of cost or market value (LCM) on the acquisition date and at the lower of such initial amount or estimated fair value less estimated selling costs thereafter. Estimated fair value is based upon many subjective factors, including location and condition of the property and current economic conditions, among other things. Because the calculation of fair value relies on estimates and judgments relating to inherently uncertain events, results may differ from our estimates.

Write-downs at the time of transfer are made through the allowance for loan losses. Write-downs subsequent to transfer are included in our noninterest expenses, along with operating income, net of related expenses of such properties and gains or losses realized upon disposition.

Table of Contents

Income taxes

Deferred income taxes are recognized for the tax consequences of temporary differences between financial statement carrying amounts and the tax bases of assets and liabilities. Deferred income taxes are provided on income and expense items when they are reported for financial statement purposes in periods different from the periods in which these items are recognized in the income tax returns. Deferred tax assets are recognized only to the extent that it is more likely than not that such amounts will be realized based upon consideration of available evidence, including tax planning strategies and other factors.

The calculation of tax liabilities is complex and requires the use of estimates and judgment since it involves the application of complex tax laws that are subject to different interpretations by us and the various tax authorities. These interpretations are subject to challenge by the tax authorities upon audit or to reinterpretation based on management's ongoing assessment of facts and evolving case law.

Periodically and in the ordinary course of business, we are involved in inquiries and reviews by tax authorities that normally require management to provide supplemental information to support certain tax positions we take in our tax returns. Uncertain tax positions are initially recognized in the financial statements when it is more likely than not the position will be sustained upon examination by the tax authorities. Such tax positions are initially and subsequently measured as the largest amount of tax benefit that is greater than 50% likely of being realized upon ultimate settlement with the tax authority assuming full knowledge of the position and all relevant facts. For tax positions not meeting the more likely than not test, no tax benefit is recorded. As of June 30, 2013 and December 31, 2012, we maintained a valuation allowance against the full amount of our deferred tax assets. Management believes it has taken appropriate positions on its tax returns, although the ultimate outcome of any tax review cannot be predicted with certainty. No assurance can be given that the final outcome of these matters will not be different than what is reflected in the current and historical financial statements.

We recognize interest and penalties related to income tax matters in income tax expense.

Other financial instruments carried at fair value

We record certain financial instruments at fair value (other than those described above), which inherently require assumptions and judgments in their valuation. Such financial instruments include loans held for sale (LHFS), interest rate lock commitments (IRLCs), forward sales of mortgage-backed securities, and warrants.

LHFS

Loans originated for sale are carried at fair value. Fair value is determined based on outstanding investor commitments or, in the absence of such commitments, on current investor yield requirements or third party pricing models. Gains and losses on loan sales are determined using the specific-identification method and are recognized through mortgage-banking revenue in the Consolidated Statement of Operations.

IRLCs

We engage an experienced third party to estimate the fair market value of our IRLCs, which are valued based upon mandatory pricing quotes from correspondent lenders less estimated costs to process and settle the loan. Fair value is adjusted for the estimated probability of the loan closing with the borrower. Gains and losses are recognized through mortgage-banking revenue in the Consolidated Statements of Operations.

Forward sales of mortgage-backed securities

Fair value for forward sales of mortgage-backed securities is determined based upon the quoted market values of the securities. Gains and losses are recognized through mortgage-banking revenue in the Consolidated Statements of Operations.

Warrants

The fair value of warrants is calculated using the Black-Scholes-Merton option-pricing model.

Risk Management

Managing risk is an essential component of successfully operating a financial services company. The risks we face include, but are not limited to, credit, market, liquidity, operational, regulatory compliance, legal, reputational, and strategic. Risk management starts at the top with the Board of Directors who set the tone and culture towards effective risk management and provides

Table of Contents

oversight and guidance to management regarding corporate goals, strategic planning, risk assessment, management, and bank-wide performance. As a result, our risk management approach includes processes for identifying, assessing, managing, monitoring, and reporting risks. An Enterprise Risk Management (ERM) Committee, whose membership includes a broad cross-section of line of business and support representatives, has been implemented to ensure the consistency and adequacy of our risk management approach. In addition, our Internal Audit division provides an independent assessment of our internal control structure and related systems and processes.

The assumption of risk requires robust and active risk management practices that comprise an integrated and comprehensive set of activities, measures, and strategies that apply to the entire organization. We are working on establishing a risk framework that provides the foundations of corporate risk capacity, risk appetite, and risk tolerances. Our risk capacity is represented by our available financial resources. Risk capacity sets an absolute limit on risk-assumption in our annual and strategic plans. Consideration must be given to planned or foreseeable events that would reduce risk capacity.

Risk appetite is the aggregate amount of risk we are willing to accept in pursuit of our strategic and financial objectives. By establishing boundaries around risk taking and business decisions and by incorporating the needs and goals of our stockholders, regulators, rating agencies, and customers, our risk appetite is aligned with our priorities and goals. Risk tolerance is expressed primarily in qualitative terms. Our risk appetite and risk tolerances are supported by appropriate risk targets and risk limits that are used to monitor the amount of risk assumed at a granular level.

While overall risk management oversight and governance is provided by the ERM Committee, this is supplemented by other key management governance committees that specifically monitor ongoing credit, asset/liability, mortgage banking risk, and regulatory compliance risk. The ERM Committee has also put into place processes for new products and initiatives applicable to every line of business to ensure an appropriate standard readiness assessment is performed before launching a new product or initiative.

Financial Condition

Total assets decreased to \$1.2 billion at June 30, 2013 from \$1.4 billion at December 31, 2012. Earning assets decreased \$221.2 million, or 20.2%, to \$874.9 million at June 30, 2013 from \$1.1 billion at December 31, 2012 primarily due to a \$226.8 million decrease in LHFS and a \$28.3 million decrease in loans, partially offset by an \$88.4 million increase in cash and cash equivalents and a \$24.4 million increase in AFS securities. Deposits decreased \$60.7 million, long- and short-term borrowings decreased by \$85.3 million due primarily to payoffs of our short-term FHLB advances and the mortgage loan on a building we own. Stockholders' deficit increased by \$4.9 million.

Securities

We utilize the securities portfolio as part of our overall asset/liability management practices to enhance interest revenue while providing necessary liquidity for the funding of loan growth or deposit withdrawals. We continually monitor the credit risk associated with investments and diversify the risk in the securities portfolios. We held \$82.0 million and \$57.7 million, respectively, in securities classified as AFS as of June 30, 2013 and December 31, 2012.

Edgar Filing: FIRST MARINER BANCORP - Form 10-Q

Changes in current market conditions, such as interest rates and the economic uncertainties in the mortgage, housing, and banking industries have severely impacted the securities market. The secondary market for various types of securities has been limited and has negatively impacted security values. Quarterly, we review each security in our AFS portfolio to determine the nature of any decline in value and evaluate if any impairment should be classified as OTTI. For the six months ended June 30, 2012, we determined that OTTI had occurred with respect to our pooled trust preferred securities portfolio in the amount of \$460,000. No additional OTTI charges were required during 2013.

The trust preferred securities we hold in our securities portfolio were issued by other banks, bank holding companies, and insurance companies. As mentioned above, certain of these securities have experienced declines in credit ratings from credit rating firms, which have devalued these specific securities. While some of these issuers have reported weaker financial performance since acquisition of these securities, in management's opinion, they continue to possess acceptable credit risk. We monitor the actual default rates and interest deferrals for possible losses and contractual shortfalls of interest or principal, which could warrant further recognition of impairment.

All of the remaining securities that are impaired are so due to declines in fair values resulting from changes in interest rates or increased credit/liquidity spreads compared to the time they were purchased. We have the intent to hold these securities to maturity and it is more likely than not that we will not be required to sell the securities before recovery of value. As such, management considers the impairments to be temporary.

Table of Contents

Our AFS securities portfolio composition is as follows:

	June 30, 2013	December 31, 2012
	(dollars in thousands)	
Mortgage-backed securities	\$ 10,611	\$ 7,134
Trust preferred securities	4,236	9,181
U.S. government agency notes	60,794	33,537
U.S. Treasury securities	4,770	5,781
Equity securities - banks	877	1,256
Equity securities - mutual funds	756	787
	\$ 82,044	\$ 57,676

LHFS

We originate residential mortgage loans for sale on the secondary market. At June 30, 2013 and December 31, 2012, such LHFS, which are carried at fair value, amounted to \$177.5 million and \$404.3 million, respectively, the majority of which are subject to purchase commitments from investors.

When we sell mortgage loans we make certain representations to the purchaser related to loan ownership, loan compliance and legality, and accurate documentation, among other things. If a loan is found to be out of compliance with any of the representations subsequent to the date of purchase, we may be required to repurchase the loan or indemnify the purchaser for losses related to the loan, depending on the agreement with the purchaser. In addition other factors may cause us to be required to repurchase or make-whole a loan previously sold.

The most common reason for a loan repurchase is due to a documentation error or disagreement with an investor or on rare occasions for fraud. Repurchase requests are negotiated with each investor at the time we are notified of the demand and an appropriate reserve, if deemed necessary, is taken at that time. Repurchase and or make-whole requests are initially negotiated by the secondary marketing department and monitored by the secondary marketing committee where most disagreements are resolved with no reserve requirement or loss to the Company. In the event there is an unresolved repurchase or make-whole request, the loan is managed by the secondary marketing committee and is elevated to be monitored by the mortgage overview committee to determine the final settlement terms with the investor. Repurchases amounted to \$1.1 million for the six months ended June 30, 2013. We did not repurchase any loans during the six months ended June 30 2012. Our reserve for potential repurchases was \$407,000 and \$484,000 as of June 30, 2013 and December 31, 2012, respectively. These reserves were calculated based upon an analysis of the specific loans in question. We do not foresee increases in repurchases to be a growing trend nor do we see it having a significant impact on our financial results.

Loans

Our loan portfolio is expected to produce higher yields than investment securities and other interest-earning assets; the absolute volume and mix of loans and the volume and mix of loans as a percentage of total earning assets is an important determinant of our net interest margin.

Edgar Filing: FIRST MARINER BANCORP - Form 10-Q

The following table sets forth the composition of our loan portfolio:

	June 30, 2013	Percent of Total (dollars in thousands)	December 31, 2012	Percent of Total
Commercial	\$ 49,173	8.4%	\$ 47,907	7.9%
Commercial mortgage	247,719	42.6%	263,714	43.2%
Commercial construction	48,451	8.3%	49,902	8.2%
Consumer construction	18,106	3.1%	18,837	3.1%
Residential mortgage	107,054	18.4%	111,345	18.2%
Consumer	111,617	19.2%	118,691	19.4%
Total loans	\$ 582,120	100.0%	\$ 610,396	100.0%

Total loans decreased \$28.3 million during 2013. We experienced lower balances in all loan types, with the exception of commercial loans, which increased \$1.3 million. We remained focused on improving asset quality to improve our capital ratios.

Table of ContentsCommercial Construction Portfolio

Our commercial construction portfolio consists of construction and development loans for commercial purposes and includes loans made to builders and developers of residential real estate projects. Of the June 30, 2013 total included above, \$35.2 million represents loans made to borrowers for the development of residential real estate.

The breakdown of the portion of the commercial construction portfolio made to borrowers for residential real estate developments is as follows as of June 30, 2013 and December 31, 2012:

	June 30, 2013		December 31, 2012
	(dollars in thousands)		
Raw residential land	\$ 5,001	\$	5,001
Residential subdivisions	4,773		3,888
Single residential lots	3,397		2,045
Single family construction	10,724		1,978
Multi-family unit construction	11,324		9,860
	\$ 35,219	\$	22,772

Transferred Loans

In accordance with FASB guidance on accounting for certain mortgage-banking activities, any loans which are originally originated for sale into the secondary market and which we subsequently transfer into the Company's loan portfolio are valued at fair value at the time of the transfer with any decline in value recorded as a charge to operating expense. We maintained \$19.1 million and \$17.3 million, respectively, in mortgage loans that were transferred from LHFS to our mortgage and consumer loan portfolios at June 30, 2013 and December 31, 2012, respectively.

Credit Risk Management

Credit risk is the risk of loss arising from the inability of a borrower to meet his or her obligations and entails both general risks, which are inherent in the process of lending, and risks specific to individual borrowers. Our credit risk is mitigated through portfolio diversification, which limits exposure to any single customer, industry, or collateral type.

We manage credit risk by evaluating the risk profile of the borrower, repayment sources, the nature of the underlying collateral, and other support given current events, conditions, and expectations. We attempt to manage the risk characteristics of our loan portfolio through various control processes, such as credit evaluation of borrowers, establishment of lending limits, and application of lending procedures, including the holding of adequate collateral and the maintenance of compensating balances. However, we seek to rely primarily on the cash flow of our borrowers as the principal source of repayment. Although credit policies and evaluation processes are designed to minimize our risk, management recognizes that loan losses will occur and the amount of these losses will fluctuate depending on the risk characteristics of our loan

portfolio, as well as general and regional economic conditions.

Management has an established methodology to determine the adequacy of the allowance for loan losses that assesses the risks and losses inherent in the loan portfolio. Our allowance methodology employs management's assessment as to the level of future losses on existing loans based on our internal review of the loan portfolio, including an analysis of the borrowers' current financial position, and the consideration of current and anticipated economic conditions and their potential effects on specific borrowers and/or lines of business. In determining our ability to collect certain loans, we also consider the fair value of any underlying collateral. In addition, we evaluate credit risk concentrations, including trends in large dollar exposures to related borrowers, industry and geographic concentrations, and economic and environmental factors.

For purposes of determining the allowance for loan losses, we have segmented our loan portfolio by product type. Our loan segments are commercial, commercial mortgage, commercial construction, consumer construction, residential mortgage, and consumer. We have looked at all segments to determine if subcategorization into classes is warranted based upon our credit review methodology. As June 30, 2013, we divided consumer loans into two classes, (1) home equity and second mortgage loans and (2) other consumer loans. For each class of loan, significant judgment is exercised to determine the estimation method that fits the credit risk characteristics of its portfolio segment. We use internally developed models in this process. Management must use judgment in establishing additional input metrics for the modeling processes. The models and assumptions used to determine the allowance are independently validated and reviewed to ensure that their theoretical foundation, assumptions, data integrity, computational processes, reporting practices, and end-user controls are appropriate and properly documented.

Table of Contents

To establish the allocated portion of the allowance for loan losses, which we do on a quarterly basis, loans are pooled by portfolio class and an historical loss percentage is applied to each class. The historical loss percentage is based upon a rolling 24-month history, which gives us the most current and relevant charge-off data. The result of that calculation for each loan class is then applied to the current loan portfolio balances to determine the required allocated portion of the allowance for loan loss level per loan class. We then apply additional loss multipliers to the different classes of loans to reflect various environmental factors. This amount is considered our unallocated allowance. These factors capture any changes in economic trends, portfolio composition, real estate trends, as well as other factors and are meant to supplement the required allocated allowance. For individually evaluated loans (impaired loans), we do additional analyses to determine the impairment amount (see below for more detail on these calculations). In general, this impairment amount is included as an allocated portion of the allowance for loan losses for TDRs and is charged off for all other impaired loans. These loss estimates are performed under multiple economic scenarios to establish a range of potential outcomes for each criterion. Management applies judgment to develop its own view of loss probability within that range, using external and internal parameters with the objective of establishing an allowance for loss inherent within these portfolios as of the reporting date.

See our charge-off policies under [Critical Accounting Policies](#) [Allowance for loan losses](#) above.

See information on partial charge-offs later in this section.

Commercial

Credit risk in commercial lending, which includes commercial, commercial mortgage, commercial construction, and consumer construction loans, can vary significantly, as losses as a percentage of outstanding loans can shift widely during economic cycles and are particularly sensitive to changing economic conditions.

The risks associated with each portfolio class are as follows:

Commercial and Commercial Mortgage - The primary loan-specific risks in commercial and commercial mortgage loans are: deterioration of the business and/or collateral values, deterioration of the financial condition of the borrowers and/or guarantors, which creates a risk of default, and the risk that real estate collateral values determined through appraisals are not reflective of the true property values.

Portfolio risk includes condition of the economy, changing demand for these types of loans, large concentration of these types of loans, and geographic concentrations of these types of loans.

Commercial Construction loan-specific and portfolio risks related to commercial construction loans also carry the loan-specific and portfolio risks of commercial and commercial mortgage loans as described above. Additional loan-specific risks include project budget overruns and performance variables related to the contractor and subcontractors. An additional loan-specific risk for commercial construction of residential developments is the risk that the builder has a geographical concentration of developments.

Consumer Construction loan-specific and portfolio risks related to consumer construction loans to builders and ultimate homeowners carry the same loan-specific and portfolio risks as commercial construction loans as described above.

In general, improving economic conditions result in improved operating results on the part of commercial customers, enhancing their ability to meet debt service requirements. However, any improvements in operating cash flows can be offset by the impact of rising interest rates that could occur during improved economic times. Declining economic conditions have an adverse effect on the operating results of commercial customers, reducing their ability to meet debt service obligations.

Our commercial loans are generally reviewed individually, in accordance with FASB guidance on accounting for loan impairment, to determine impairment, accrual status, and the need for an allocated allowance. We use creditworthiness categories to grade commercial loans. Our internal grading system is based on experiences with similarly graded loans and incorporates a variety of risk considerations, both qualitative and quantitative (see definitions of our various grades and the composition of our loan portfolio within those grades in Note 4 to the Consolidated Financial Statements). Quantitative factors include collateral values, financial condition of borrowers, and other factors. Qualitative factors include judgments concerning general economic conditions that may affect credit quality, credit concentrations, the pace of portfolio growth, and delinquency levels; these qualitative factors are evaluated in connection with the unallocated portion of our allowance for loan losses (see below). We periodically engage outside firms and experts to independently assess our methodology and perform various loan review functions.

Consumer

Our consumer portfolio includes first- and second-lien mortgage loans and other loans to individuals. The risks associated with each portfolio class are as follows:

Table of Contents

Residential Mortgage, Home Equity, and 2nd Mortgage The primary loan-specific risks related to residential mortgage, home equity, and 2nd mortgage lending include: unemployment, deterioration in real estate values, our ability to assess the creditworthiness of the customer, deterioration in the borrowers financial condition, whether the result of personal issues or a general economic downturn, and the risk that property values determined through appraisals are not reflective of the true property values. The portfolio risks for these types of loans are the same as for commercial and commercial mortgages as described above.

Other Consumer - The primary loan-specific risks of consumer loans are: unemployment, deterioration of the borrower's financial condition, whether the result of personal issues or a general economic downturn, and for certain consumer loans such as auto loans and boat loans, there is also a risk of deterioration in the value of the collateral. The portfolio risks for these types of loans are the same as for commercial and commercial mortgages as described above.

Generally, consumer loans are segregated into homogeneous pools with similar risk characteristics. We do not individually grade consumer loans. Such loans are classified as performing or nonperforming. Trends such as delinquency and loss and current economic conditions in consumer loan pools are analyzed and historical loss experience is adjusted accordingly. Quantitative and qualitative adjustment factors for the different consumer portfolios are consistent with those for the commercial portfolios.

Unallocated

The unallocated portion of the allowance is intended to provide for losses that are not identified when establishing the required allocated portion of the allowance and is based upon management's evaluation of various conditions that are not directly measured in the determination of the formula and other allocated allowances. Such conditions include general economic and business conditions affecting key lending areas, credit quality trends (including trends in delinquencies and nonperforming loans expected to result from existing conditions), loan volumes, loan concentrations by class and geography and any changes in such concentrations, specific industry conditions within portfolio categories, duration of the current business cycle, bank regulatory examination results, and management's judgment with respect to various other conditions including changes in management, including credit, loan administration, and origination staff, changes in underwriting standards, lending policies, and procedures, the impact of any new or modified lines of business, level and trends in nonaccrual and delinquent loans and charge-offs, changes in underlying collateral for collateral dependent loans, and management and the quality of risk identification systems. Management reviews these conditions quarterly. Economic factors are an important consideration in determining the adequacy of the loan loss allowance. A strong regional and national economy will reduce the probability of losses. Weaker regional and national economies will usually result in higher unemployment, higher vacancies in commercial real estate, and declining values on both commercial and residential properties, which will gradually increase the probability of losses. Key measures of economic strength or weakness are unemployment levels, interest rates, and economic growth and confidence.

In calculating the unallocated portion of the allowance for loan losses, we apply a basis point factor to the respective portfolios for environmental factors. The addition of these factors represents the top range for the required allowance for the respective portfolios and were as follows as of both June 30, 2013 and December 31, 2012:

	Commercial	Commercial Mortgage	Commercial Construction	Consumer Construction	Residential Mortgage	Consumer
			(in basis points)			
Concentration of credit and changes in level of		5	5	8	10	

Edgar Filing: FIRST MARINER BANCORP - Form 10-Q

concentration						
Nature and volume of portfolio		25	25	4	4	
Trends of past due and classified loans	15	17	17	8	8	
Economic factors	24	24	24	14	14	48
Value of underlying collateral for collateral dependent loans		25	25	23	23	5
	39	96	96	57	59	53

Each of the above factors is evaluated quarterly. The basis points applied to all loan segments remained the same at June 30, 2013 compared to December 31, 2012 as management considered the factors to be constant in the first half of 2013.

We have risk management practices designed to ensure timely identification of changes in loan risk profiles; however, undetected losses may inherently exist within the loan portfolio. The assessments aspects involved in analyzing the quality of individual loans and assessing collateral values can also contribute to undetected, but probable, losses.

See additional detail on our allowance methodology and risk rating system in Note 4 to the Consolidated Financial Statements.

Edgar Filing: FIRST MARINER BANCORP - Form 10-Q

Table of Contents

The following table summarizes the activity in our allowance for loan losses by portfolio segment for the three and six months ended June 30:

	Three Months Ended June 30, 2013		Six Months Ended June 30, 2012	
	(dollars in thousands)			
Allowance for loan losses, beginning of period	\$	11,225	\$	13,521
Charge-offs:				
Commercial				(129)
Commercial mortgage			(94)	(1,087)
Commercial construction		(46)		(134)
Consumer construction		(148)		(148)
Residential mortgage		(1,411)		(1,706)
Consumer		(211)	(546)	(368)
Total charge-offs		(1,816)	(640)	(3,572)
Recoveries:				
Commercial		91		93
Commercial mortgage		138	612	149
Commercial construction				52
Consumer construction				
Residential mortgage		212	384	326
Consumer		26	73	146
Total recoveries		467	1,069	714
Net (charge-offs) recoveries		(1,349)	429	(2,858)
(Reversal of) provision for loan losses			(428)	1,300
Allowance for loan losses, end of period	\$	9,876	\$	13,522
Loans (net of premiums and discounts):				
Period-end balance	\$	582,120	\$	660,795
Average balance during period		589,530		668,996
Allowance as a percentage of period-end loan balance		1.70%		2.05%
Percent of average loans:				
(Reversal of) provision for loan losses			(0.26)%	0.44%
Net charge-offs (recoveries)		0.92%	(0.26)%	0.96%

The following table summarizes our allocation of allowance by loan segment:

	June 30, 2013			December 31, 2012		
	Amount	Percent of Total	Percent of Loans to Total Loans	Amount	Percent of Total	Percent of Loans to Total Loans
	(dollars in thousands)					
Commercial	\$ 1,162	11.8%	8.4%	\$ 2,070	18.1%	7.9%
Commercial mortgage	1,534	15.5%	42.6%	1,254	11.0%	43.2%
Commercial construction	238	2.4%	8.3%	414	3.6%	8.2%
Consumer construction	84	0.9%	3.1%	20	0.2%	3.1%
Residential mortgage	2,058	20.8%	18.4%	1,774	15.5%	18.2%

Edgar Filing: FIRST MARINER BANCORP - Form 10-Q

Consumer		1,588	16.1%	19.2%		2,040	17.8%	19.4%
Unallocated		3,212	32.5%			3,862	33.8%	
Total	\$	9,876	100.0%	100.0%	\$	11,434	100.0%	100.0%

Based upon management's evaluation, provisions are made to maintain the allowance as a best estimate of inherent losses within the portfolio. The allowance for loan losses totaled \$9.9 million at June 30, 2013 and \$11.4 million at December 31, 2012. Any changes in the allowance from period to period reflect management's ongoing application of its methodologies to establish the allowance, which, in 2013, included increases in the allowance for the commercial mortgage, consumer construction, and residential mortgage loan segments. The changes in the allowances for the respective loan segments were primarily a function of the changes in the corresponding loan balances. We reduced the level of delinquencies and nonperforming loans due to aggressive workouts and sales of a portion of our nonperforming loan portfolio.

Table of Contents

The provision for loan losses recognized to maintain the allowance was \$1.3 million and \$572,000 for the six months ended June 30, 2013 and 2012, respectively. We did not provide any additional amounts for loan losses during the three months ended June 30, 2013 compared to a reversal of provision of \$428,000 for the three months ended June 30, 2012. We recorded net charge-offs of \$2.9 million and \$851,000 during the first half of 2013 and 2012, respectively, and \$1.3 million and \$429,000 for the three months ended June 30, 2013 and 2012, respectively. During 2013, net charge-offs as compared to average loans outstanding increased to 0.96%, compared to 0.25% during 2012. We generally record a significant amount of charge-offs as a result of our policy to charge off all fair value deficiencies instead of carrying an allocated portion of the allowance for loan losses (except with respect to nonaccrual TDRs).

Partial charge-offs of nonaccrual loans decrease the amount of nonperforming and impaired loans, as well as any allocated allowance attributable to that loan. They decrease our allowance for loan losses, as well as our allowance for loan losses to nonperforming loans ratio and our allowance for loan losses to total loans ratio. Partial charge-offs increase our net charge-offs to average loans ratio. Total partial charge-offs of nonaccrual loans for the three and six months ended June 30, 2013 amounted to \$709,000 and \$1.0 million, respectively. Total partial charge-offs of nonaccrual loans for the three and six months ended June 30, 2012 amounted to \$173,000 and \$774,000, respectively. The total amount of nonaccrual loans (prior to charge offs) for which we recorded partial charge-offs for the three and six months ended June 30, 2013 were \$7.4 million and \$16.0 million, respectively, and the total amount of nonaccrual loans for which we recorded partial charge-offs for the three and six months ended June 30, 2012 were \$1.2 million and \$3.4 million, respectively.

Our allowance as a percentage of outstanding loans decreased from 1.87% as of December 31, 2012 to 1.70% as of June 30, 2013, reflecting the improvement in our asset quality.

Although management uses available information to establish the appropriate level of the allowance for loan losses, future additions or reductions to the allowance may be necessary based on estimates that are susceptible to change as a result of changes in economic conditions and other factors. As a result, our allowance for loan losses may not be sufficient to cover actual loan losses, and future provisions for loan losses could materially adversely affect our operating results. In addition, various regulatory agencies, as an integral part of their examination process, periodically review our allowance for loan losses and related methodology. Such agencies may require us to recognize adjustments to the allowance based on their judgments about information available to them at the time of their examination.

Management believes the allowance for loan losses is adequate as of June 30, 2013 and is sufficient to address the credit losses inherent in the current loan portfolio. We based this determination on several factors:

- we maintain appropriate oversight committees to track deteriorating credits thereby timely identifying potential problems and noting when current appraisals are due;
- we individually analyze all nonperforming assets (NPAs) and all credits risk rated 8 or above for impairment and we immediately charge off any deficiencies in collateral value that is identified in the impairment analysis (thus, placing all NPAs and risk-ratings (RR) of RR8 at fair value) (see additional detail related to risk ratings in Note 4 to the Consolidated Financial Statements);
- we calculate our required allocated allowance based upon a rolling 24-month average of actual charge-offs, thereby utilizing current trend data of actual losses and apply these calculated loss percentages to our current loan balance by loan class to determine the required

allocated allowance;

- we apply environmental factors to calculate an unallocated portion of the allowance, which is meant to cover any negative economic and business trends that may develop; and
- the combination of the calculated required allocated allowance plus the unallocated allowance results in a total range for our allowance for loan losses and our actual allowance for loan losses has been within the estimated range.

Our determination of the appropriate allowance level is based upon a number of assumptions we make about future events, which we believe are reasonable, but which may or may not prove valid. Thus, there can be no assurance that our charge-offs in future periods will not exceed our allowance for loan losses or that we will not need to make additional increases in our allowance for loan losses.

NPAs and Loans 90 Days Past Due and Still Accruing

Given the volatility of the real estate market, it is very important for us to have current appraisals on our NPAs. Generally, we annually obtain appraisals on NPAs. In addition, as part of our asset monitoring activities, we maintain a Workout Committee that meets three times per month. During these Workout Committee meetings, all NPAs and loan delinquencies are reviewed. We also produce an NPA report which is distributed weekly to senior management and is also discussed and reviewed at the Workout Committee meetings. This report contains all relevant data on the NPAs, including the latest appraised value and valuation date. Accordingly, these reports identify which assets will require an updated appraisal. As a result, we have not experienced any internal

Table of Contents

delays in identifying which loans/credits require appraisals. With respect to the ordering process of the appraisals, we have not experienced any delays in turnaround time nor has this been an issue over the past three years. Furthermore, we have not had any delays in turnaround time or variances thereof in our specific loan operating markets.

NPAs, expressed as a percentage of total assets, totaled 3.0% at June 30, 2013, 4.1% at December 31, 2012 and 4.6% at June 30, 2012. The ratio of allowance for loan losses to nonperforming loans was 36.4% at June 30, 2013, 29.7% at December 31, 2012, and 40.6% at June 30, 2012. The increase in this ratio from December 31, 2012 to June 30, 2013 was a reflection of the decrease in nonperforming loans. Part of the decrease in nonperforming loans was due to full and partial charge-offs of nonperforming loans that existed at December 31, 2012. We record a significant amount of charge-offs as it is our policy to charge off all fair value deficiencies instead of carrying an allocated allowance (except with respect to nonaccrual TDRs).

The distribution of our NPAs and loans greater than 90 days past due and accruing is illustrated in the following table:

	June 30, 2013	December 31, 2012	June 30, 2012
	(dollars in thousands)		
Nonaccruing loans:			
Commercial	\$ 1,154	\$ 2,110	\$ 3,156
Commercial mortgage	15,141	21,269	15,610
Commercial construction	3,909	4,637	5,002
Consumer construction	16	645	669
Residential mortgage	5,609	8,826	7,694
Consumer	1,266	973	1,135
	27,095	38,460	33,266
Real estate acquired through foreclosure:			
Commercial	83	1,658	1,451
Commercial mortgage	3,630	7,386	9,309
Commercial construction	3,629	3,983	5,614
Consumer construction	237	403	230
Residential mortgage	2,163	4,540	5,739
Consumer	109	88	90
	9,851	18,058	22,433
Total NPAs	\$ 36,946	\$ 56,518	\$ 55,699
Loans past-due 90 days or more and accruing:			
Commercial	\$	\$	\$
Commercial mortgage	87		
Commercial construction			
Consumer construction			
Residential mortgage		222	
Consumer	2		
	\$ 89	\$ 222	\$

For information on nonaccruing TDRs, see table under TDRs later in this section.

Edgar Filing: FIRST MARINER BANCORP - Form 10-Q

Nonaccrual loans amounted to \$27.1 million at June 30, 2013 and \$38.5 million at December 31, 2012. The commercial loan nonaccrual balance as of June 30, 2013 consisted of six loans, with the largest balance amounting to \$736,000. All of the nonaccrual commercial loans as of June 30, 2013 were in nonaccrual status as of December 31, 2012. Of the \$2.1 million in nonaccrual commercial loans as of December 31, 2012, two loans in the amount of \$168,000 were sold or paid off during 2013, one loan in the amount of \$35,000 was charged off, and one loan in the amount of \$733,000 was placed back in accrual status.

The commercial mortgage loan nonaccrual balance as of June 30, 2013 consisted of 24 loans, with the largest balance amounting to \$5.0 million. We placed four commercial mortgage loans totaling \$420,000 in nonaccrual status in 2013. Of the balance at December 31, 2012, two commercial mortgage loans for \$499,000 were transferred to real estate acquired through foreclosure, \$4.9 million were sold or paid off, one loan for \$322,000 was placed back in accrual status, and \$323,000 were charged off during 2013.

The commercial construction nonaccrual balance as of June 30, 2013 consisted of six loans, with the largest balance amounting to \$2.3 million. All of the nonaccrual commercial construction loans as of June 30, 2013 were also in nonaccrual status as

Table of Contents

of December 31, 2012. Of the \$4.6 million in commercial construction loans in nonaccrual status as of December 31, 2012, \$134,000 were charged off and \$474,000 were sold during 2013.

The consumer construction nonaccrual balance as of June 30, 2013 consisted of one loan, which was placed in nonaccrual status during 2013. Of the balance of consumer construction nonaccrual loans as of December 31, 2012, \$82,000 was charged off and \$563,000 were sold or paid off.

The residential mortgage nonaccrual balance as of June 30, 2013 consisted of 20 loans, with the largest balance amounting to \$776,000. We placed \$1.7 million of these loans in nonaccrual status during 2013. Of the \$8.8 million balance of nonaccrual residential mortgage loans at December 31, 2012, we transferred \$1.1 million to real estate acquired through foreclosure, sold or received pay-offs of \$3.1 million, returned \$84,000 to accrual status, and charged off \$496,000 during 2013.

The consumer loan nonaccrual balance as of June 30, 2013 consisted of 11 loans, three of which (in the amount of \$433,000) were placed in nonaccrual status during 2013. These loans are well secured and we have determined that they do not require charge-off as of June 30, 2013.

The interest which would have been recorded on nonaccrual loans if those loans had been performing in accordance with their contractual terms for the six months ended June 30, 2013 and 2012 was approximately \$698,000 and \$1.4 million, respectively, and the actual interest income recorded on such loans for the six months ended June 30, 2013 and 2012 was approximately \$130,000 and \$253,000, respectively.

Real estate acquired through foreclosure decreased \$8.2 million compared to December 31, 2012, with decreases in all loan segments, with the exception of consumer, due to resolution of the properties through foreclosure sales or buyouts.

The activity in our real estate acquired through foreclosure was as follows for the three and six months ended June 30:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
	(dollars in thousands)			
Balance at beginning of period	\$ 10,654	\$ 25,531	\$ 18,058	\$ 25,235
Real estate acquired in satisfaction of loans	614	2,095	1,634	4,650
Write-downs and losses on real estate acquired through foreclosure	(674)	(185)	(2,544)	(941)
Proceeds from sales of real estate acquired through foreclosure	(743)	(5,008)	(7,297)	(6,511)
Balance at end of period	\$ 9,851	\$ 22,433	\$ 9,851	\$ 22,433

As of June 30, 2013, we had one commercial mortgage loan in the amount of \$87,000 and one consumer loan in the amount of \$2,000 that were greater than 90 days past due and still accruing. We held \$222,000 (residential mortgage) in such loans at December 31, 2012.

TDRs

In situations where, for economic or legal reasons related to a borrower's financial difficulties, management may grant a concession for other than an insignificant period of time to the borrower that would not otherwise be considered, the related loan is classified as a TDR. Such concessions could include reductions in the interest rate, payment extensions, forgiveness of principal, forbearance, or other actions. These loans are excluded from pooled loss forecasts and a separate allocated portion of the allowance is provided under the accounting guidance for loan impairment. At the time that a loan is modified, management evaluates any possible impairment based on the present value of expected future cash flows, discounted at the contractual interest rate of the original loan agreement, except when the sole remaining source of repayment for the loan is the liquidation of the collateral. In these cases, we use the current fair value of the collateral, less selling costs, instead of discounted cash flows. Any impairment amount is then set up as an allocated portion of the allowance.

Table of Contents

The composition of our TDRs is illustrated in the following table at June 30, 2013 and December 31, 2012:

	June 30, 2013	December 31, 2012
(dollars in thousands)		
Commercial:		
Nonaccrual	\$	\$
< 90 days past due/current	\$ 13,043	\$ 7,708
	13,043	7,708
Commercial mortgage:		
Nonaccrual	6,316	6,394
< 90 days past due/current	13,017	13,049
	19,333	19,443
Commercial construction:		
Nonaccrual		101
< 90 days past due/current	5,739	7,055
	5,739	7,156
Residential mortgage:		
Nonaccrual	1,798	2,019
< 90 days past due/current	9,364	9,638
	11,162	11,657
Totals:		
Nonaccrual	\$ 8,114	\$ 8,514
< 90 days past due/current	\$ 41,163	\$ 37,450
	\$ 49,277	\$ 45,964

The interest income which would have been recorded on TDRs if those loans had performed in accordance with their contractual terms was approximately \$1.7 million and \$1.6 million for the six months ended June 30, 2013 and 2012, respectively. The actual interest income recorded on these loans for the six months ended June 30, 2013 and 2012 was \$792,000 and \$661,000, respectively.

The following tables show the breakdown of loans we modified during the three and six months ended June 30:

	Number of Modifications	Three Months Ended June 30,				
		2013 Recorded Investment Prior to Modification	Recorded Investment After Modification	Number of Modifications	2012 Recorded Investment Prior to Modification	Recorded Investment After Modification
(dollars in thousands)						
Commercial	1	\$ 5,358	\$ 5,358	2	\$ 211	\$ 211
Commercial mortgage				2	566	574
Commercial construction				1	5,060	5,060
Residential mortgage	1	339	339			
	2	\$ 5,697	\$ 5,697	5	\$ 5,837	\$ 5,845

Edgar Filing: FIRST MARINER BANCORP - Form 10-Q

Table of Contents

	Number of Modifications	Six Months Ended June 30,					
		2013 Recorded Investment Prior to Modification	Recorded Investment After Modification	Number of Modifications	2012 Recorded Investment Prior to Modification	Recorded Investment After Modification	
							(dollars in thousands)
Commercial	1	\$ 5,358	\$ 5,358	2	\$ 211	\$ 211	
Commercial mortgage	3	396	430	6	2,749	2,757	
Commercial construction				2	7,093	7,093	
Residential mortgage	1	339	339	1	863	863	
	5	\$ 6,093	\$ 6,127	11	\$ 10,916	\$ 10,924	

Impaired Loans

The following tables show the breakout of impaired loans by class:

	June 30, 2013			Six Months Ended June 30,						
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	2013 Interest Income Recognized	Charge-Offs	Average Recorded Investment	2012 Interest Income Recognized	Charge-Offs	
										(dollars in thousands)
With no related allowance:										
Commercial	\$ 6,916	\$ 6,916	\$	\$ 3,880	\$ 77	\$ 129	\$ 4,330	\$ 24	\$ 187	
Commercial mortgage	\$ 26,412	\$ 26,412	\$	\$ 28,611	\$ 192	\$ 1,087	\$ 22,911	\$ 260	\$ 320	
Commercial construction	\$ 9,648	\$ 9,648	\$	\$ 10,803	\$ 102	\$ 134	\$ 13,571	\$ 162	\$ 147	
Consumer construction	\$ 16	\$ 16	\$	\$ 494	\$ 1	\$ 148	\$ 654	\$ 16	\$ 7	
Residential mortgage	\$ 9,357	\$ 9,357	\$	\$ 10,913	\$ 160	\$ 1,559	\$ 9,490	\$ 186	\$ 346	
Home equity & 2nd mortgage	\$ 1,087	\$ 1,087	\$	\$ 1,077	\$ 6	\$ 368	\$ 1,014	\$ 9	\$ 938	
Other consumer	\$ 179	\$ 179	\$	\$ 67	\$ 3	\$	\$ 5	\$ 1	\$	
With a related allowance:										
Commercial	7,172	7,281	109	7,161	97		156	2		
Commercial mortgage	1,713	1,746	33	1,828	26		4,705	68		
Commercial construction										
Consumer construction										
Residential mortgage	5,470	5,617	147	5,988	113	147	7,459	142	168	
Home equity & 2nd mortgage										
Other consumer										
Total:										
Commercial	\$ 14,088	\$ 14,197	\$ 109	\$ 11,041	\$ 174	\$ 129	\$ 4,486	\$ 26	\$ 187	
Commercial mortgage	\$ 28,125	\$ 28,158	\$ 33	\$ 30,439	\$ 218	\$ 1,087	\$ 27,616	\$ 328	\$ 320	
Commercial construction	\$ 9,648	\$ 9,648	\$	\$ 10,803	\$ 102	\$ 134	\$ 13,571	\$ 162	\$ 147	

Edgar Filing: FIRST MARINER BANCORP - Form 10-Q

Consumer construction	\$	16	\$	16	\$	494	\$	1	\$	148	\$	654	\$	16	\$	7		
Residential mortgage	\$	14,827	\$	14,974	\$	147	\$	16,901	\$	273	\$	1,706	\$	16,949	\$	328	\$	514
Home equity & 2nd mortgage	\$	1,087	\$	1,087	\$	1,077	\$	6	\$	368	\$	1,014	\$	9	\$	938		
Other consumer	\$	179	\$	179	\$	67	\$	3	\$		\$	5	\$	1	\$			

Table of Contents

	December 31, 2012		
	Recorded	Unpaid	Related
	Investment	Principal	Allowance
	Balance		
	(dollars in thousands)		
With no related allowance:			
Commercial	\$ 2,535	\$ 2,535	\$
Commercial mortgage	\$ 32,561	\$ 32,561	\$
Commercial construction	\$ 11,692	\$ 11,692	\$
Consumer construction	\$ 645	\$ 645	\$
Residential mortgage	\$ 11,776	\$ 11,776	\$
Home equity & 2nd mortgage	\$ 1,235	\$ 1,235	\$
Other consumer	\$ 12	\$ 12	\$
With a related allowance:			
Commercial	7,150	7,283	133
Commercial mortgage	1,734	1,757	23
Commercial construction			
Consumer construction			
Residential mortgage	6,243	6,414	171
Home equity & 2nd mortgage			
Other consumer			
Total:			
Commercial	\$ 9,685	\$ 9,818	\$ 133
Commercial mortgage	\$ 34,295	\$ 34,318	\$ 23
Commercial construction	\$ 11,692	\$ 11,692	\$
Consumer construction	\$ 645	\$ 645	\$
Residential mortgage	\$ 18,019	\$ 18,190	\$ 171
Home equity & 2nd mortgage	\$ 1,235	\$ 1,235	\$
Other consumer	\$ 12	\$ 12	\$

Not all of the loans newly classified as impaired since December 31, 2012 required an allocated allowance for impairment, as some of the loans collateral had estimated fair values greater than the carrying amount of the loan or the loan has been written down to its estimated fair value. Additionally, in general, we charge off all impairment amounts immediately for all loans that are not TDRs.

Deposits

Deposits were \$1.1 billion at June 30, 2013 and \$1.2 billion at December 31, 2012. During the six months ended June 30, 2013, we experienced increases in NOW accounts, money market and savings accounts due to the result of successful marketing campaigns. The decrease in time deposits was due to maturities of nonbrokered national time deposits (see below).

We maintain a program (the nonbrokered national deposit program) whereby the Bank utilizes several nonbrokered rate listing services to provide incremental funding as needed. We pay an annual subscription fee for the privilege of posting rates on their websites. The subscription-based services allow the Bank to place or receive funds from other subscribers. Requests to invest are placed through the listing website and the account is funded by wire. At the present time, only financial institutions are allowed to place funds with the Bank. These balances fluctuate according to our liquidity needs.

Edgar Filing: FIRST MARINER BANCORP - Form 10-Q

The deposit breakdown is as follows:

	June 30, 2013		December 31, 2012	
	Balance	Percent of Total (dollars in thousands)	Balance	Percent of Total
NOW & money market	\$ 168,847	15.0%	\$ 158,437	13.3%
Savings	64,602	5.7%	60,729	5.1%
Time	791,161	70.3%	857,698	72.3%
Total interest-bearing deposits	1,024,610	91.0%	1,076,864	90.7%
Noninterest-bearing demand deposits	101,537	9.0%	109,966	9.3%
Total deposits	\$ 1,126,147	100.0%	\$ 1,186,830	100.0%

Core deposits represent deposits that we believe to be less sensitive to changes in interest rates and, therefore, will be retained

Table of Contents

regardless of the movement of interest rates. We consider our core deposits to be all noninterest-bearing, NOW, money market accounts less than \$100,000, and saving deposits, as well as all time deposits less than \$100,000 that are not scheduled to mature within one year. As of June 30, 2013 and December 31, 2012, our core deposits were \$345.5 million and \$358.9 million, respectively. The remainder of our deposits could be susceptible to attrition due to interest rate movements.

Borrowings

Our borrowings consist of short-term promissory notes issued to certain qualified investors, short-term and long-term advances from the Federal Home Loan Bank (FHLB), and a mortgage loan. Our short-term promissory notes are in the form of commercial paper, which reprice daily and have maturities of 270 days or less. Our advances from the FHLB may be in the form of short-term or long-term obligations. Short-term advances have maturities for one year or less and may contain prepayment penalties. Long-term borrowings through the FHLB have original maturities up to 15 years and generally contain prepayment penalties.

The FHLB advances are available under a specific collateral pledge and security agreement, which requires that we maintain collateral for all of our borrowings equal to 125% of advances. We may pledge as collateral specific first- and second-lien mortgage loans or commercial mortgages up to 10% of the Bank's total assets. Long-term FHLB advances are fixed-rate instruments with various call provisions. Generally, short-term advances are in the form of overnight borrowings with rates changing daily. At June 30, 2013, our total available credit line with the FHLB was \$130.0 million. Our outstanding FHLB advance balance at June 30, 2013 and December 31, 2012 was \$40.0 million and \$117.0 million, respectively.

Long-term borrowings, which totaled \$40.0 million at June 30, 2013, consist of long-term advances from the FHLB. At December 31, 2012, long-term borrowings consisted of a mortgage loan on our former headquarters building (\$8.5 million) that was paid off during 2013 and \$65.0 million in long-term FHLB advances.

Short-term borrowings consist of short-term promissory notes and short-term advances from the FHLB. These borrowings decreased from \$53.5 million at December 31, 2012 to \$1.7 million at June 30, 2013 due to the payoff of our short-term FHLB advances. We held \$52.0 million in short-term FHLB advances at December 31, 2012.

In the past, to further our funding and capital needs, we raised capital by issuing Trust Preferred Securities through statutory trusts (the Trusts), which are wholly-owned by First Mariner Bancorp. The Trusts used the proceeds from the sales of the Trust Preferred Securities, combined with First Mariner Bancorp's equity investment in these Trusts, to purchase subordinated deferrable interest debentures from First Mariner Bancorp. The debentures are the sole assets of the Trusts. Aggregate debentures outstanding as of both June 30, 2013 and December 31, 2012 totaled \$52.1 million.

The Trust Preferred Securities are mandatorily redeemable, in whole or in part, upon repayment of their underlying subordinated debentures at their respective maturities or their earlier redemption date at our option. All redemption dates have passed and we have not opted to redeem any of the junior subordinated interest debentures.

Edgar Filing: FIRST MARINER BANCORP - Form 10-Q

In 2009, we elected to defer interest payments on the debentures. This deferral is permitted by the terms of the debentures and does not constitute an event of default thereunder. Interest on the debentures and dividends on the related Trust Preferred Securities continue to accrue and will have to be paid in full prior to the expiration of the deferral period. The total deferral period may not exceed 20 consecutive quarters and expires with the last quarter of 2013. First Mariner is currently prohibited from paying such interest under the terms of the agreements with the Federal Reserve Bank of Richmond (FRB). (See discussion of the agreements below under Capital Resources).

First Mariner Bancorp has fully and unconditionally guaranteed all of the obligations of the Trusts.

Under applicable regulatory guidelines, a portion of the Trust Preferred Securities may qualify as Tier I capital, and the remaining portion may qualify as Tier II capital, with certain limitations. At June 30, 2013, none of our outstanding Trust Preferred Securities qualify as either Tier I or Tier II capital due to limitations.

Capital Resources

Our stockholders' deficit deteriorated by \$4.9 million in 2013 to a deficit of \$13.3 million from a deficit of \$8.4 million as of December 31, 2012.

Common stock and additional paid-in-capital increased by \$426,000 due to the change in the fair value of the warrants and the issuance of stock to certain officers. Accumulated other comprehensive loss, which is derived from the fair value calculations for AFS securities, increased by \$1.6 million. Accumulated deficit increased by our 2013 net loss of \$3.8 million.

Banking regulatory authorities have implemented strict capital guidelines directly related to the credit risk associated with an institution's assets. Banks and bank holding companies are required to maintain capital levels based on their risk-adjusted assets so that categories of assets with higher defined credit risks will require more capital support than assets with lower risk. Additionally, capital must be maintained to support certain off-balance sheet instruments.

Table of Contents

Capital is classified as Tier I capital (common stockholders' deficit less certain intangible assets) and Total Capital (Tier I plus the allowed portion of the allowance for loan losses plus any off-balance sheet reserves). Minimum required levels must at least equal 4% for Tier I capital and 8% for Total Capital. In addition, institutions must maintain a minimum 4% leverage capital ratio (Tier I capital to average quarterly assets).

We regularly monitor the Company's capital adequacy ratios to assure that the Bank meets its regulatory capital requirements. As of both June 30, 2013 and December 31, 2012, the Bank was undercapitalized under the regulatory framework for prompt corrective action, although, as of both December 31, 2012 and June 30, 2013, the Bank's Tier I capital ratio met minimal adequacy requirements.

The regulatory capital ratios are shown below:

	June 30, 2013	December 31, 2012	Minimum Regulatory Requirements
Regulatory capital ratios:			
Leverage:			
Consolidated	(0.8)%	(0.5)%	4.0%
Bank	3.8%	3.8%	4.0%
Tier I capital to risk-weighted assets:			
Consolidated	(1.4)%	(0.8)%	4.0%
Bank	6.6%	6.1%	4.0%
Total capital to risk-weighted assets:			
Consolidated	(1.4)%	(0.8)%	8.0%
Bank	7.8%	7.3%	8.0%

On September 18, 2009, the Bank entered into an agreement with the FDIC and the Commissioner of Financial Regulation for the state of Maryland (the "Commissioner"), pursuant to which it consented to the entry of an Order to Cease and Desist (the "September Order"), which directs the Bank to (i) increase its capitalization, (ii) improve earnings, (iii) reduce nonperforming loans, (iv) strengthen management policies and practices, and (v) reduce reliance on noncore funding. The September Order required the Bank to adopt a plan to achieve and maintain a leverage capital ratio of at least 7.5% and a total risk-based capital ratio of at least 11% by June 30, 2010. We did not meet the requirements at June 30, 2010, December 31, 2010, December 31, 2011, December 31, 2012, or June 30, 2013. The failure to achieve these capital requirements could result in further action by our regulators.

As part of the September Order, within 30 days after the end of each calendar year, the Bank must submit an annual budget and profit plan and a plan that takes into account the Bank's pricing structure, the Bank's cost of funds and how this can be reduced, and the level of provision expense for adversely classified loans. To address reliance on noncore funding, the Bank has adopted and submitted a liquidity plan to reduce the Bank's reliance on noncore funding, wholesale funding sources, and high-cost rate-sensitive deposits. While the September Order is in effect, the Bank may not pay dividends or management fees without the FDIC's prior consent, may not accept, renew, or roll over any brokered deposits, or pay effective yields on deposits that are greater than those generally paid in its markets.

First Mariner is also a party to the FRB Agreements which require it to: (i) develop and implement a strategic business plan that includes (a) actions that will be taken to improve our operating performance and reduce the level of parent company leverage, (b) a comprehensive budget and an expanded budget review process, (c) a description of the operating assumptions that form the basis for major projected income and expense components and provisions needed to maintain an adequate loan loss reserve, and (d) a capital plan incorporating all capital needs,

Edgar Filing: FIRST MARINER BANCORP - Form 10-Q

risks, and regulatory guidelines; and (ii) submit plans to improve enterprise-wide risk management and effectiveness of internal audit programs. First Mariner has also agreed to provide the FRB with advance notice of any significant capital transactions. The FRB Agreements also prohibit First Mariner and the Bank from taking any of the following actions without the FRB's prior written approval: (i) declaring or paying any dividends; (ii) taking dividends from the Bank; (iii) making any distributions of interest, principal, or other sums on First Mariner's subordinated debentures or trust preferred securities; (iv) incurring, increasing, or guaranteeing any debt; or (v) repurchasing or redeeming any shares of its stock. To satisfy the FRB's minimum capital requirements, First Mariner's consolidated leverage, Tier I capital to risk-weighted assets, and total capital to risk-weighted assets ratios at each quarter end must be at least 4.0%, 4.0%, and 8.0%, respectively. At June 30, 2013, those capital ratios were (0.8)%, (1.4)%, and (1.4)%, respectively, which were not in compliance with the minimum requirements. The failure to achieve these capital requirements could result in further action by our regulators.

The foregoing will subject us to increased regulatory scrutiny and may have an adverse impact on our business operations. Failure to comply with the provisions of these regulatory requirements may result in more restrictive actions from our regulators, including more severe and restrictive enforcement actions.

Table of Contents

Results of Operations

Net (Loss) Income

Three Months Ended June 30

For the three months ended June 30, 2013, we realized a net loss of \$1.5 million compared to net income of \$5.7 million for the three month period ended June 30, 2012. Basic and diluted losses per share for 2013 totaled \$0.08 and basic and diluted earnings per share totaled \$0.30 for 2012.

Six Months Ended June 30

For the six months ended June 30, 2013, we realized a net loss of \$3.8 million compared to net income of \$7.5 million for the six month period ended June 30, 2012. Basic and diluted losses per share for 2013 totaled \$0.20 and basic and diluted earnings per share totaled \$0.40 for 2012.

Net Interest Income

Net interest income is the difference between the interest income we earn on interest-earning assets, such as loans and investment securities, and the interest expense we pay on interest-bearing sources of funds, such as deposits and borrowings. Net interest income is a function of several factors, including changes in the volume and mix of interest-earning assets and funding sources and market interest rates. While management policies influence these factors, external forces, including customer needs and demands, competition, the economic policies of the federal government, and the monetary policies of the FRB, are also determining factors.

Three Months Ended June 30

Net interest income for the second quarter of 2013 totaled \$6.4 million, compared to \$7.3 million for the three months ended June 30, 2012. The decrease in net interest income was primarily due to a decrease in the volume of interest-earning assets. Our net interest margin decreased to 2.89% for 2013 from 3.07% for 2012.

Interest Income

Edgar Filing: FIRST MARINER BANCORP - Form 10-Q

Total interest income decreased from \$11.2 million for the three months ended June 30, 2012 to \$9.9 million for the three months ended June 30, 2013. We experienced a decrease in the yield on average interest-earning assets from 4.69% for the three months ended June 30, 2012 to 4.51% for the three months ended June 30, 2013. Average interest-earning assets decreased from \$946.8 million for the three months ended June 30, 2012 to \$875.1 million for the three months ended June 30, 2013. Yields on earning assets continue to be affected by a relatively low rate environment and interest reversals on nonaccrual loans.

We experienced decreased average balances in all loan segments during 2013, with the exception of consumer construction loans, which increased \$1.9 million, primarily due to our efforts to improve asset quality.

Average LHFS decreased \$19.1 million primarily due to lower pricing caused by the increasing mortgage rate environment. Average securities increased by \$31.9 million due to the purchase of securities during the quarter in order to utilize some of our excess liquidity.

Interest Expense

Interest expense decreased from \$3.8 million for the three months ended June 30, 2012 to \$3.5 million for the three months ended June 30, 2013. We experienced a decrease in the average rate paid on average interest-bearing liabilities from 1.42% for the three months ended June 30, 2012 to 1.22% for the three months ended June 30, 2013, slightly offset by an increase in the level of interest-bearing liabilities of \$78.6 million. The decrease in the average rate paid on interest-bearing deposits from 1.27% in 2012 to 1.05% in 2013 was due primarily to our reduction in rates paid on deposits due to our high level of liquidity.

Average interest-bearing deposits increased by \$155.3 million due primarily to increases in savings, money market, and time deposit accounts. Average savings and money market accounts increased as a result of successful marketing campaigns. The increase in average time deposit accounts was due to increased nonbrokered national deposits (see Deposits above for more information on this program). We experienced an increase in the costs of borrowed funds from 2.21% for the three months ended June 30, 2012 to

Table of Contents

3.15% for the three months ended June 30, 2013 due to the change in the mix of types of average borrowed funds during 2013. We paid off a significant amount of our long-term FHLB advances and our mortgage loan during the second quarter of 2013.

Six Months Ended June 30

Net interest income for the first half of 2013 totaled \$13.5 million, compared to \$14.9 million for the six months ended June 30, 2012. The decrease in net interest income was primarily due to a decline in yields on average interest-earning assets. Our net interest margin decreased to 2.77% for 2013 from 3.11% for 2012.

Interest Income

Total interest income decreased from \$22.8 million for the six months ended June 30, 2012 to \$21.1 million for the six months ended June 30, 2013. We experienced a decrease in the yield on average interest-earning assets from 4.77% for the six months ended June 30, 2012 to 4.34% for the six months ended June 30, 2013. Average interest-earning assets increased from \$949.5 million for the six months ended June 30, 2012 to \$968.7 million for the six months ended June 30, 2013.

We experienced decreased average balances in all loan segments during 2013, with the exception of consumer construction loans, which increased \$2.5 million.

Average LHFS increased \$88.0 million due to higher origination volume, primarily in the earlier part of 2013. Average securities increased by \$32.0 million due to the purchase of securities during 2013.

Interest Expense

Interest expense decreased to \$7.5 million for the six months ended June 30, 2013 from \$7.9 million for the same period of 2012. We experienced a decrease in the average rate paid on average interest-bearing liabilities from 1.46% for the six months ended June 30, 2012 to 1.27% for the six months ended June 30, 2013, slightly offset by an increase in the level of interest-bearing liabilities of \$111.4 million. The decrease in the average rate paid on interest-bearing deposits from 1.32% in 2012 to 1.07% in 2013 was due primarily to our reduction in rates paid on deposits due to our high level of liquidity.

Average interest-bearing deposits increased by \$167.1 million due primarily to increases in savings and money market accounts (successful marketing campaigns) and time deposit accounts (nonbrokered national deposits - see above). We experienced an increase in the costs of borrowed funds from 2.21% for the six months ended June 30, 2012 to 3.05% for the six months ended June 30, 2013 due to the change in the mix of types of average borrowed funds during 2013.

The following tables set forth, for the periods indicated, information regarding the average balances of interest-earning assets and interest-bearing liabilities and the resulting yields on average interest-earning assets and rates paid on average interest-bearing liabilities. Average balances are also provided for noninterest-earning assets and noninterest-bearing liabilities.

Table of Contents

	Three Months Ended June 30,					
	Average Balance (1)	2013 Interest (2)	Yield/ Rate (dollars in thousands)	Average Balance (1)	2012 Interest (2)	Yield/ Rate
ASSETS						
Loans:						
Commercial	\$ 48,906	\$ 656	5.31%	\$ 51,706	\$ 646	4.94%
Commercial mortgage	252,712	3,764	5.89%	306,197	4,505	5.82%
Commercial construction	48,146	668	5.49%	53,150	722	5.38%
Consumer construction	18,545	258	5.57%	16,682	156	3.74%
Residential mortgage	108,322	1,536	5.67%	115,855	1,512	5.22%
Consumer	112,899	1,349	4.79%	125,406	1,335	4.28%
Total loans	589,530	8,231	5.55%	668,996	8,876	5.27%
LHFS	186,031	1,238	2.66%	205,126	1,919	3.74%
AFS securities	63,083	229	1.45%	31,149	305	3.92%
Interest-bearing deposits	32,901	194	2.36%	34,589	70	0.80%
Restricted stock investments, at cost	3,517	30	3.39%	6,967		
Total earning assets	875,062	9,922	4.51%	946,827	11,170	4.69%
Allowance for loan losses	(11,190)			(13,741)		
Cash and other nonearning assets	403,704			242,445		
Total assets	\$ 1,267,576	9,922		\$ 1,175,531	11,170	
LIABILITIES AND STOCKHOLDERS DEFICIT						
Interest-bearing deposits:						
NOW	\$ 5,015	4	0.32%	\$ 5,910	14	0.97%
Savings	64,752	29	0.18%	59,421	29	0.20%
Money market	166,234	164	0.40%	135,487	180	0.54%
Time	825,222	2,575	1.25%	705,072	2,648	1.51%
Total interest-bearing deposits	1,061,223	2,772	1.05%	905,890	2,871	1.27%
Borrowings	96,430	758	3.15%	173,184	952	2.21%
Total interest-bearing liabilities	1,157,653	3,530	1.22%	1,079,074	3,823	1.42%
Noninterest-bearing demand deposits	104,325			101,718		
Other noninterest-bearing liabilities	14,693			14,604		
Stockholders deficit	(9,095)			(19,865)		
Total liabilities and stockholders deficit	\$ 1,267,576	3,530		\$ 1,175,531	3,823	
Net interest income/net interest spread		\$ 6,392	3.29%		\$ 7,347	3.27%
Net interest margin			2.89%			3.07%

(1) Nonaccrual loans are included in average loans.

(2) There are no tax equivalency adjustments.

Edgar Filing: FIRST MARINER BANCORP - Form 10-Q

Table of Contents

	Six Months Ended June 30,					
	2013			2012		
	Average Balance (1)	Interest (2)	Yield/ Rate (dollars in thousands)	Average Balance (1)	Interest (2)	Yield/ Rate
ASSETS						
Loans:						
Commercial	\$ 47,782	\$ 1,265	5.27%	\$ 53,058	\$ 1,357	5.06%
Commercial mortgage	258,063	7,205	5.55%	312,870	9,192	5.81%
Commercial construction	48,917	1,340	5.45%	54,166	1,527	5.58%
Consumer construction	18,859	476	5.04%	16,380	340	4.14%
Residential mortgage	109,420	2,839	5.19%	118,657	3,298	5.56%
Consumer	115,213	2,679	4.67%	128,005	2,766	4.34%
Total loans	598,254	15,804	5.27%	683,136	18,480	5.37%
LHFS	279,446	4,458	3.19%	191,416	3,597	3.76%
AFS securities	59,008	449	1.52%	26,965	584	4.33%
Interest-bearing deposits	27,529	274	1.99%	40,904	127	0.62%
Restricted stock investments, at cost	4,425	70	3.14%	7,064		
Total earning assets	968,662	21,055	4.34%	949,485	22,788	4.77%
Allowance for loan losses	(11,496)			(13,898)		
Cash and other nonearning assets	347,469			240,758		
Total assets	\$ 1,304,635	21,055		\$ 1,176,345	22,788	
LIABILITIES AND STOCKHOLDERS DEFICIT						
Interest-bearing deposits:						
NOW	\$ 4,810	4	0.17%	\$ 5,822	28	0.98%
Savings	63,450	55	0.18%	58,251	55	0.19%
Money market	163,543	402	0.50%	131,383	343	0.52%
Time	843,197	5,264	1.26%	712,471	5,533	1.56%
Total interest-bearing deposits	1,075,000	5,725	1.07%	907,927	5,959	1.32%
Borrowings	118,419	1,793	3.05%	174,109	1,917	2.21%
Total interest-bearing liabilities	1,193,419	7,518	1.27%	1,082,036	7,876	1.46%
Noninterest-bearing demand deposits	105,326			102,221		
Other noninterest-bearing liabilities	14,300			14,290		
Stockholders deficit	(8,410)			(22,202)		
Total liabilities and stockholders deficit	\$ 1,304,635	7,518		\$ 1,176,345	7,876	
Net interest income/net interest spread		\$ 13,537	3.07%		\$ 14,912	3.31%
Net interest margin			2.77%			3.11%

(1) Nonaccrual loans are included in average loans.

(2) There are no tax equivalency adjustments.

The Rate/Volume Analysis below indicates the changes in our net interest income as a result of changes in volume and rates. We maintain an asset and liability management policy designed to provide a proper balance between rate-sensitive assets and rate-sensitive liabilities to attempt to optimize interest margins while providing adequate liquidity for our anticipated needs. Changes in interest income and interest expense that

result from variances in both volume and rates have been allocated to rate and volume changes in proportion to the absolute dollar amounts of the change in each.

Edgar Filing: FIRST MARINER BANCORP - Form 10-Q

Table of Contents

	Three Months Ended June 30, 2013 vs. 2012			Six Months Ended June 30, 2013 vs. 2012		
	Rate	Due to Variances in		Rate	Due to Variances in	
		Volume	Total		Volume	Total
	(dollars in thousands)					
Interest earned on:						
Loans:						
Commercial	\$ 166	\$ (156)	\$ 10	\$ 128	\$ (220)	\$ (92)
Commercial mortgage	364	(1,105)	(741)	(402)	(1,585)	(1,987)
Commercial construction	86	(140)	(54)	(36)	(151)	(187)
Consumer construction	83	19	102	80	56	136
Residential mortgage	463	(439)	24	(211)	(248)	(459)
Consumer	589	(575)	14	444	(531)	(87)
Total loans	1,751	(2,396)	(645)	3	(2,679)	(2,676)
LHFS	(515)	(166)	(681)	(1,425)	2,286	861
AFS securities	(982)	906	(76)	(1,029)	894	(135)
Interest-bearing deposits	148	(24)	124	273	(126)	147
Restricted stock investments, at cost	30		30	70		70
Total interest income	432	(1,680)	(1,248)	(2,108)	375	(1,733)
Interest paid on:						
Interest-bearing deposits:						
NOW	(8)	(2)	(10)	(20)	(4)	(24)
Savings	(9)	9		(9)	9	
Money market	(184)	168	(16)	(50)	109	59
Time	(1,857)	1,784	(73)	(2,238)	1,969	(269)
Total interest-bearing deposits	(2,058)	1,959	(99)	(2,317)	2,083	(234)
Borrowings	1,565	(1,759)	(194)	1,270	(1,394)	(124)
Total interest expense	(493)	200	(293)	(1,047)	689	(358)
Net interest income	\$ 925	\$ (1,880)	\$ (955)	\$ (1,061)	\$ (314)	\$ (1,375)

Noninterest Income

We derive noninterest income principally from mortgage-banking activities, service fees on our deposit accounts, ATM fees, commissions on sales of nondeposit investment products (brokerage fees), and income from bank-owned life insurance (BOLI).

Three Months Ended June 30

Our noninterest income for the three months ended June 30, 2013 totaled \$10.3 million, compared to \$12.8 million for the three months ended June 30, 2012, a decrease of \$2.5 million, primarily due to decreased mortgage-banking revenue.

Mortgage-banking revenue decreased from \$11.1 million for the three months ended June 30, 2012 to \$5.4 million for the three months ended June 30, 2013 due primarily to lower pricing on loan sales due to higher mortgage rates. Application volume also decreased for the three months

Edgar Filing: FIRST MARINER BANCORP - Form 10-Q

ended June 30, 2013 to \$679.8 million from \$716.5 million for the same period of 2012.

During 2013, we recognized a gain of \$2.9 million on the sale of our 5% remaining interest in the former Mariner Finance entity.

Six Months Ended June 30

Our noninterest income for the six months ended June 30, 2013 totaled \$21.9 million, compared to \$23.2 million for six months ended June 30, 2012, a decrease of \$1.3 million, primarily due to decreased mortgage-banking revenue.

Mortgage-banking revenue decreased from \$20.1 million for the six months ended June 30, 2012 to \$15.2 million for the six months ended June 30, 2013 due to decreased pricing. Application volume was relatively stable at \$1.4 billion for both 2013 and 2012.

Table of Contents

During 2013, we did not recognize any net OTTI charges on AFS securities, compared to \$460,000 recorded in 2012. See Securities discussion previously in this Item for more information on these OTTI charges and the related securities. We recognized a gain of \$2.9 million on the sale of our portion of the former Mariner Finance entity.

*Noninterest Expense*Three Months Ended June 30

For the three months ended June 30, 2013, noninterest expenses increased \$3.2 million to \$18.2 million compared to \$14.9 million for the same period of 2012.

Additional compensation was incurred during the quarter in connection with mortgage-banking activities. Additionally, postage expense increased as a result of direct-mail campaigns of the mortgage division. Occupancy costs decreased due to the relocation of a substantial amount of our operations from a leased space to a building we own. We continue to incur significant professional fees for regulatory compliance and capital raise efforts. Corporate insurance expense increased as the renewal rates increased in late 2012.

Six Months Ended June 30

For the six months ended June 30, 2013, noninterest expenses increased \$7.6 million to \$37.9 million compared to \$30.3 million for the same period of 2012.

Additional compensation, advertising expense, and postage expense was incurred during the period in connection with mortgage-banking activities. We continue to incur significant professional fees for regulatory compliance and capital raise efforts. Write-downs, losses, and costs of real estate acquired through foreclosure increased \$1.5 million as we continued to take write-downs and aggressively dispose of foreclosed assets. Corporate insurance expense increased as the renewal rates increased in late 2012.

The following table shows the breakout of other noninterest expenses:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
	(dollars in thousands)			
Office supplies	\$ 212	\$ 127	\$ 348	\$ 248
Printing	20	140	94	218
Marketing/promotion	31	234	256	558
Overnight delivery/courier	167	135	302	270

Edgar Filing: FIRST MARINER BANCORP - Form 10-Q

Security	41	41	115	119
Dues and subscriptions	144	107	260	212
Director fees	81	70	162	164
Employee education and training	31	19	114	53
Automobile expense	49	26	78	54
Travel and entertainment	69	64	178	126
Other	714	496	1,390	929
	\$ 1,559	\$ 1,459	\$ 3,297	\$ 2,951

Income Taxes

We have set up a valuation allowance against the full amount of our deferred taxes as of both June 30, 2013 and December 31, 2012. The \$205,000 tax benefit recorded in 2012 represents an anticipated recovery of state taxes paid in 2010 as a result of a net operating loss carryback.

Liquidity

Liquidity describes our ability to meet financial obligations, including lending commitments and contingencies, which arise during the normal course of business. Liquidity is primarily needed to meet the borrowing and deposit withdrawal requirements of our customers, to fund the operations of our mortgage-banking business, as well as to meet current and planned expenditures. These cash requirements are met on a daily basis through the inflow of deposit funds, the maintenance of short-term overnight investments, maturities and calls in our securities portfolio, and available lines of credit with the FHLB, which requires pledged collateral. Fluctuations in deposit and short-term borrowing balances may be influenced by the interest rates paid, general consumer confidence, and the overall economic environment. There can be no assurances that deposit withdrawals and loan fundings will not exceed all

Table of Contents

available sources of liquidity on a short-term basis. Such a situation would have an adverse effect on our ability to originate new loans and maintain reasonable loan and deposit interest rates, which would negatively impact earnings.

The borrowing requirements of customers include commitments to extend credit and the unused portion of lines of credit (collectively commitments), which totaled \$299.5 million at June 30, 2013. Historically, many of the commitments expire without being fully drawn; therefore, the total commitment amounts do not necessarily represent future cash requirements. Commitments for real estate development and construction, which totaled \$8.2 million, are generally short-term in nature, satisfying cash requirements with principal repayments as construction properties financed are generally repaid with permanent financing. Available credit lines represent the unused portion of credit previously extended and available to the customer as long as there is no violation of material contractual conditions. Commitments to extend credit for residential mortgage loans of \$219.4 million at June 30, 2013 generally expire within 60 days. Commercial commitments to extend credit and unused lines of credit of \$4.2 million at June 30, 2013 generally do not extend for more than 12 months. Consumer commitments to extend credit and unused lines of credit of \$10.9 million at June 30, 2013 are generally open ended. At June 30, 2013, available home equity lines totaled \$56.8 million. Home equity credit lines generally extend for a period of 10 years.

Capital expenditures for various branch locations and equipment can be a significant use of liquidity. As of June 30, 2013, we anticipate expending approximately \$1.5 million in the next 12 months on our premises and equipment.

Customer withdrawals are also a principal use of liquidity, but are generally mitigated by growth in customer funding sources, such as deposits and short-term borrowings.

The Bank's principal sources of liquidity are cash and cash equivalents (which are cash on hand and amounts due from financial institutions, federal funds sold, money market mutual funds, and interest bearing deposits), AFS securities, deposit accounts, and borrowings. The levels of such sources are dependent on the Bank's operating, financing and investing activities at any given time. We attempt to primarily rely on core deposits from customers to provide stable and cost-effective sources of funding to support our loan growth. We also seek to augment such deposits with longer term and higher yielding certificates of deposit. Cash and cash equivalents, which totaled \$274.2 million at June 30, 2013, have immediate availability to meet our short-term funding needs. Our entire securities portfolio is classified as AFS, is highly marketable (excluding our holdings of pooled trust preferred securities), and available to meet our liquidity needs. LHFS, which totaled \$177.5 million at June 30, 2013, are committed to be sold into the secondary market and generally are funded within 60 days. Our residential real estate portfolio includes loans that are underwritten to secondary market criteria and provide us an additional source of liquidity. Additionally, our residential construction loan portfolio provides a source of liquidity as construction periods generally range from 9-12 months, and these loans are subsequently financed with permanent first-lien mortgages and sold into the secondary market. We may also, from time to time, sell commercial or consumer loans to enhance our liquidity position and/or improve asset quality. Our loan to deposit ratio stood at 51.7% at June 30, 2013 and 51.4% at December 31, 2012.

We also have the ability to utilize established credit lines with the FHLB and the FRB as additional sources of liquidity. To utilize the vast majority of our credit lines, we must pledge certain loans and/or securities before advances can be obtained. At June 30, 2013, our total available credit line with the FHLB was \$130.0 million. Our outstanding FHLB advance balance was \$40.0 million at June 30, 2013 and \$117.0 million at December 31, 2012.

We are not permitted to purchase brokered deposits without first obtaining a regulatory waiver. We are also required to comply with restrictions on deposit rates that we may offer. These factors could significantly affect our ability to fund normal operations. Our ability to acquire deposits or borrow could also be impaired by factors that are not specific to us, such as a severe disruption of the financial markets or negative views and

Edgar Filing: FIRST MARINER BANCORP - Form 10-Q

expectations about the prospects for the financial services industry as a whole. At June 30, 2013, management considered the Bank's liquidity level to be sufficient for the purposes of meeting the Bank's cash flow requirements.

First Mariner Bancorp is a separate entity and apart from First Mariner Bank and must provide for its own liquidity. In addition to its operating expenses, First Mariner Bancorp is responsible for the payment of any dividends that may be declared for its shareholders and interest and principal on outstanding debt. A significant amount of First Mariner Bancorp's revenues are obtained from subsidiary service fees and dividends. Payment of such dividends to First Mariner Bancorp by First Mariner Bank is limited under Maryland law. As noted earlier, First Mariner and its bank subsidiary have entered into agreements with the FRB, FDIC, and the Commissioner that, among other things, require First Mariner and the Bank to obtain the prior approval of regulators before paying interest on the junior subordinated deferrable interest debentures or a dividend or otherwise making a distribution on stock. First Mariner has elected to defer regularly scheduled quarterly interest payments on its junior subordinated debentures issued in connection with its Trust Preferred Securities offerings. First Mariner is prohibited from paying any dividends or making any other distribution on its common stock for so long as interest payments are being deferred.

We are not aware of any undisclosed known trends, demands, commitments, or uncertainties that are reasonably likely to result in material changes in our liquidity.

Table of Contents

Inflation

The consolidated financial statements and related consolidated financial data presented herein have been prepared in accordance with GAAP and practices within the banking industry, which generally require the measurement of financial condition and operating results in terms of historical dollars, without considering the changes in the relative purchasing power of money over time due to inflation. As a financial institution, virtually all of our assets and liabilities are monetary in nature and interest rates have a more significant impact on our performance than the effects of general levels of inflation. A prolonged period of inflation could cause interest rates, wages, and other costs to increase and could adversely affect our results of operations unless mitigated by increases in our revenues correspondingly. However, we believe that the impact of inflation on our operations was not material for 2013 or 2012.

Off-Balance Sheet Arrangements

We enter into off-balance sheet arrangements in the normal course of business. These arrangements consist primarily of commitments to extend credit, lines of credit, and letters of credit. In addition, the Company has certain operating lease obligations.

Credit Commitments

Credit commitments 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 rates fixed at current market amounts, 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.

Our exposure to credit loss in the event of nonperformance by the borrower is the contract amount of the commitment. Loan commitments, lines of credit, and letters of credit are made on the same terms, including collateral, as outstanding loans. We are not aware of any accounting loss we would incur by funding our commitments.

See detailed information on credit commitments above under *Liquidity*.

Derivatives

We maintain and account for derivatives, in the form of IRLCs and forward sales commitments, in accordance with FASB guidance on accounting for derivative instruments and hedging activities. We recognize gains and losses on IRLCs and forward sales commitments on the loan pipeline through mortgage-banking revenue in the Consolidated Statements of Operations.

The Bank, through First Mariner Mortgage, enters into IRLCs, under which we originate residential mortgage loans with interest rates determined prior to funding. IRLCs on mortgage loans that we intend to sell in the secondary market are considered derivatives. The period of time between issuance of a loan commitment and closing and sale of the loan generally ranges from 14 days to 60 days. For these IRLCs, we attempt to protect the Company from changes in interest rates through the use of forward sales of to be issued (TBA) mortgage-backed securities.

We are exposed to price risk from the time a mortgage loan closes until the time the loan is sold. To manage this risk, we utilize forward sales of TBA mortgage-backed securities. During the period of the rate lock commitment and from the time a loan is closed with the borrowers and sold to investors, we remain exposed to basis (execution, timing, and/or volatility) risk in that the changes in value of our hedges may not equal or completely offset the changes in value of the rate commitments being hedged. This can result due to changes in the market demand for our mortgage loans brought about by supply and demand considerations and perceptions about credit risk relative to the agency securities. We also mitigate counterparty risk by entering into commitments with proven counterparties and pre-approved financial intermediaries.

The market value of IRLCs is not readily ascertainable with precision because they are not actively traded in stand-alone markets. The Bank determines the fair value of IRLCs by measuring the change in the value of the underlying asset, while taking into consideration the probability that the IRLCs will close.

Table of Contents

Information pertaining to the carrying amounts of our derivative financial instruments follows:

	June 30, 2013		December 31, 2012	
	Notional Amount	Estimated Fair Value (dollars in thousands)	Notional Amount	Estimated Fair Value
IRLCs	\$ 219,419	\$ 218,734	\$ 404,645	\$ 410,192
Forward contracts to sell mortgage-backed securities	261,855	267,143	308,067	306,682

Changes in interest rates could materially affect the fair value of the IRLCs or the forward commitments. In the case of the loan related derivatives, fair value is also impacted by the probability that the rate lock commitment will close (fallout factor). In addition, changes in interest rates could result in changes in the fallout factor, which might magnify or counteract the sensitivities. This is because the impact of an interest rate shift on the fallout ratio is nonsymmetrical and nonlinear.

Subsequent Event

On July 1, 2013, we became self-insured with respect to employee-related health insurance claims. We use commercial insurance above our self-insured retentions to reduce our risk of catastrophic loss. Our reserves for self-insured losses are estimated based on employee claim history.

Item 3 - Quantitative and Qualitative Disclosures About Market Risk

Results of operations for financial institutions, including us, may be materially and adversely affected by changes in prevailing economic conditions, including declines in real estate values, rapid changes in interest rates, and the monetary and fiscal policies of the federal government. Our loan portfolio is concentrated primarily in central Maryland and portions of Maryland's Eastern Shore and is, therefore, subject to risks associated with these local economies.

Interest Rate Risk

Our profitability is in part a function of the spread between the interest rates earned on assets and the interest rates paid on deposits and other interest-bearing liabilities (net interest income), including advances from the FHLB and other borrowings. Interest rate risk arises from mismatches (i.e., the interest sensitivity gap) between the dollar amount of repricing or maturing assets and liabilities and is measured in terms of the ratio of the interest rate sensitivity gap to total assets. More assets repricing or maturing than liabilities over a given time period is considered asset-sensitive and is reflected as a positive gap, and more liabilities repricing or maturing than assets over a given time period is considered liability-sensitive and is reflected as negative gap. An asset-sensitive position (i.e., a positive gap) will generally enhance earnings in a rising interest rate environment and will negatively impact earnings in a falling interest rate environment, while a liability-sensitive position (i.e., a negative gap) will generally enhance earnings in a falling interest rate environment and negatively impact earnings in a rising interest rate environment. Fluctuations in interest rates are not predictable or controllable. We have attempted to structure our asset and liability

management strategies to mitigate the impact on net interest income of changes in market interest rates. However, there can be no assurance that we will be able to manage interest rate risk so as to avoid significant adverse effects on net interest income. At June 30, 2013, we had a one-year cumulative positive gap of approximately \$407.9 million compared to a one-year cumulative positive gap of approximately \$5.0 million at December 31, 2012.

While we monitor interest rate sensitivity gap reports, we primarily test our interest rate sensitivity through the deployment of simulation analysis. We use earnings simulation models to estimate what effect specific interest rate changes would have on our net interest income and net income. Simulation analysis provides us with a more rigorous and dynamic measure of interest sensitivity. Changes in prepayments have been included where changes in behavior patterns are assumed to be significant to the simulation, particularly mortgage related assets. Call features on certain securities and borrowings are based on their call probability in view of the projected rate change, and pricing features such as interest rate floors are incorporated. Our fee income produced by mortgage-banking operations may also be impacted by changes in rates. As long-term rates increase, the volume of fixed-rate mortgage loans originated for sale in the secondary market may decline and reduce our revenues generated by this line of business. We attempt to structure our asset and liability management strategies to mitigate the impact on net interest income by changes in market interest rates. However, there can be no assurance that we will be able to manage interest rate risk so as to avoid significant adverse effects on net interest income. At June 30, 2013, the simulation model provided the following profile of our interest rate risk measured over a one-year time horizon, assuming a parallel shift in a yield curve based off the U.S. dollar forward swap curve adjusted for certain pricing assumptions:

Table of Contents

	Immediate Rate Change	
	+200BP	-200BP
Net interest income	3.91%	(6.53)%

Both of the above tools used to assess interest rate risk have strengths and weaknesses. Because the gap analysis reflects a static position at a single point in time, it is limited in quantifying the total impact of market rate changes which do not affect all

earning assets and interest-bearing liabilities equally or simultaneously. In addition, gap reports depict the existing structure, excluding exposure arising from new business. While the simulation process is a powerful tool in analyzing interest rate sensitivity,

many of the assumptions used in the process are highly qualitative and subjective and are subject to the risk that past historical activity may not generate accurate predictions of the future. The model also assumes parallel movements in interest rates, which means both short-term and long-term rates will change equally. Nonparallel changes in interest rates (short-term rates changing differently from

long-term rates) could result in significant differences in projected income amounts when compared to parallel tests. Both

measurement tools taken together, however, provide an effective evaluation of our exposure to changes in interest rates, enabling management to better control the volatility of earnings.

We are party to mortgage rate lock commitments to fund mortgage loans at interest rates previously agreed (locked) by both us and the borrower for specified periods of time. When the borrower locks an interest rate, we effectively extend a put option to the borrower, whereby the borrower is not obligated to enter into the loan agreement, but we must honor the interest rate for the specified time period. We are exposed to interest rate risk during the accumulation of IRLCs and loans prior to sale. We utilize forward sales commitments to economically hedge the changes in fair value of the loan due to changes in market interest rates.

Item 4 - Controls and Procedures

(a) Evaluation of disclosure controls and procedures. The Company maintains disclosure controls and procedures that are designed to ensure that information required to be disclosed in our reports filed under the Securities Exchange Act of 1934, such as this Quarterly Report, is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission rules and forms, and that such information is accumulated and communicated to the Company's management, including the Principal Executive Officer and Chief Financial Officer (CFO), as appropriate, to allow for timely decisions regarding required disclosure. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the control. The design of any system of controls also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions; over time, controls may become inadequate because of changes in conditions, or the degree of compliance with the policies or procedures may deteriorate.

An evaluation of the effectiveness of these disclosure controls, as of the end of the period covered by this Quarterly Report on Form 10-Q, was carried out under the supervision and with the participation of the Company's management, including the Principal Executive Officer and CFO. Based on that evaluation, the Company's management, including the Principal Executive Officer and CFO, has concluded that the Company's disclosure controls and procedures are in fact effective at the reasonable assurance level.

(b) Changes in Internal Control Over Financial Reporting. There were no significant changes in our internal control over financial reporting during our last fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II OTHER INFORMATION

Item 1 - Legal Proceedings

None

Item 1A Risk Factors

The risks and uncertainties to which our financial condition and operations are subject are discussed in detail in Item 1A of Part I of the Annual Report of First Mariner Bancorp on Form 10-K for the year ended December 31, 2012.

Table of Contents

Item 2 - Unregistered Sales of Equity Securities and Use of Proceeds

There were no repurchases of the Company's common stock during the three months ended June 30, 2013.

Item 3 - Defaults Upon Senior Securities

None

Item 4 - Mine Safety Disclosures

Not Applicable.

Item 5 - Other Information

None

Item 6 - Exhibits

- 10.1 Retention and Success Bonus Agreement between First Mariner Bank and Mark Keidel (Filed herewith)
- 10.2 Retention and Success Bonus Agreement between First Mariner Bank and Paul Susie (Filed herewith)
- 31.1 Certifications of Principal Executive Officer pursuant to Rule 13a-14(a) and Rule 15d-14(a), promulgated under the Securities Exchange Act of 1934, as amended, filed herewith
- 31.2 Certifications of Chief Financial Officer pursuant to Rule 13a-14(a) and Rule 15d-14(a), promulgated under the Securities Exchange Act of 1934, as amended, filed herewith
- 32.1 Certification of Principal Executive Officer pursuant to 18 U.S.C. Section 1350 as adopted pursuant to section 906 of the Sarbanes-Oxley Act of 2002, furnished herewith
- 32.2 Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350 as adopted pursuant to section 906 of the Sarbanes-Oxley Act of 2002, furnished herewith

Edgar Filing: FIRST MARINER BANCORP - Form 10-Q

101.0* The following materials from the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2013 formatted in XBRL (Extensible Business Reporting Language): (i) Consolidated Statements of Financial Condition; (ii) Consolidated Statements of Operations; (iii) Consolidated Statements of Comprehensive (Loss) Income; (iv) Consolidated Statements of Changes in Stockholders' Deficit; (v) Consolidated Statements of Cash Flows; and (vi) related notes.

* Furnished, not filed.

Table of Contents

SIGNATURES

Pursuant to the requirements 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.

FIRST MARINER BANCORP

Date: August 14, 2013

By: /s/ Mark A. Keidel
Mark A. Keidel
Principal Executive Officer

Date: August 14, 2013

By: /s/ Paul B. Susie
Paul B. Susie
Chief Financial Officer and Principal Accounting
Officer

Table of Contents

Exhibit Index

- 10.1 Retention and Success Bonus Agreement between First Mariner Bank and Mark Keidel (Filed herewith)
- 10.2 Retention and Success Bonus Agreement between First Mariner Bank and Paul Susie (Filed herewith)
- 31.1 Certifications of Principal Executive Officer pursuant to Rule 13a-14(a) and Rule 15d-14(a), promulgated under the Securities Exchange Act of 1934, as amended, filed herewith
- 31.2 Certifications of Chief Financial Officer pursuant to Rule 13a-14(a) and Rule 15d-14(a), promulgated under the Securities Exchange Act of 1934, as amended, filed herewith
- 32.1 Certification of Principal Executive Officer pursuant to 18 U.S.C. Section 1350 as adopted pursuant to section 906 of the Sarbanes-Oxley Act of 2002, furnished herewith
- 32.2 Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350 as adopted pursuant to section 906 of the Sarbanes-Oxley Act of 2002, furnished herewith
- 101.0* The following materials from the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2013 formatted in XBRL (Extensible Business Reporting Language): (i) Consolidated Statements of Financial Condition; (ii) Consolidated Statements of Operations; (iii) Consolidated Statements of Comprehensive (Loss) Income; (iv) Consolidated Statements of Changes in Stockholders' Deficit; (v) Consolidated Statements of Cash Flows; and (vi) related notes.

* Furnished, not filed.