Howard Bancorp Inc
Form 10-Q
November 16, 2015

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2015

OR

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

Commission File Number: 001-35489

HOWARD BANCORP, INC.

(Exact name of registrant as specified in its charter)

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

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

(410) 750-0020

(Registrant's telephone number, including area code)

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a small reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "small reporting company in Rule 12b-2 of the Exchange Act.

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

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

The number of outstanding shares of common stock outstanding as of October 31, 2015.

Common Stock, $0.01 par value – 6,955,097 shares

HOWARD BANCORP, INC.

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

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

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

- statements of our goals, intentions and expectations, particularly with respect to our business plan and strategies, including continuing to focus on commercial customers, continuing to increase our originations of one-to four-family residential mortgage loans, increasing our mortgage lending portfolio and selling loans into the secondary markets;
- statements regarding the asset quality of our investment portfolios and anticipated recovery and collection of unrealized losses on securities available for sale;
- statements with respect to our allowance for credit losses, and the adequacy thereof;
- our expectation regarding the amount and timing of system conversion costs related to the Patapsco Bancorp acquisition being incurred and the related impact on earnings in the fourth quarter of 2015;
- statement with respect to having adequate liquidity levels;
- our belief that we will retain a large portion of maturing certificates of deposit;
- the impact on us of recent changes to accounting standards; and
- future cash requirements and that we do not anticipate material losses relating to commitments to extend credit.

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

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

- general economic conditions, either nationally or in our market area, that are worse than expected;
- competition among depository and other financial institutions;
- inflation and changes in the interest rate environment that reduce our margins or reduce the fair value of financial instruments;
- adverse changes in the securities markets;
- changes in laws or government regulations or policies affecting financial institutions, including changes in regulatory fees and capital requirements;

- our ability to enter new markets successfully and capitalize on growth opportunities, and to otherwise implement our growth strategy;
- our ability to successfully integrate acquired entities, if any;
- changes in consumer spending, borrowing and savings habits;
- changes in accounting policies and practices, as may be adopted by the bank regulatory agencies, the Financial Accounting Standards Board, the Securities and Exchange Commission ("SEC") and the Public Company Accounting Oversight Board;
- changes in our organization, compensation and benefit plans;
- loss of key personnel; and
- other risk discussed in this report, in our annual report on Form 10-K for the year ended December 31, 2014, as filed with the SEC, and in other reports we may file.

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

PART I

Item 1. Financial Statements

Howard Bancorp, Inc. and Subsidiary

Consolidated Balance Sheets

(in thousands)	Unaudited September 30, 2015	December 31, 2014
ASSETS		
Cash and due from banks	$ 17,264	$ 23,598
Federal funds sold	1,083	919
Total cash and cash equivalents	18,347	24,517
Securities available-for-sale, at fair value	39,178	41,079
Nonmarketable equity securities	3,185	2,571
Loans held for sale, at fair value	64,427	42,881
Loans and leases, net of unearned income	755,500	552,917
Allowance for credit losses	(4,317)	(3,602)
Net loans and leases	751,183	549,315
Bank premises and equipment, net	20,428	12,122
Goodwill	1,132	-
Core deposit intangible	3,117	1,391
Bank owned life insurance	16,618	11,659
Other real estate owned	1,764	2,472
Interest receivable and other assets	5,114	3,409
Total assets	$ 924,493	$ 691,416
LIABILITIES		
Noninterest-bearing deposits	$ 171,349	$ 142,727
Interest-bearing deposits	571,417	411,312
Total deposits	742,766	554,039
Short-term borrowings	52,708	48,628
Long-term borrowings	27,851	19,000
Deferred tax liability	2,552	4,686
Accrued expenses and other liabilities	6,536	5,420
Total liabilities	832,413	631,773
COMMITMENTS AND CONTINGENCIES		

SHAREHOLDERS' EQUITY		
Preferred stock—par value $0.01 (liquidation preference of $1,000 per share) authorized 5,000,000; shares issued and outstanding 12,562 series AA at September 30, 2015 and December 31, 2014	12,562	12,562
Common stock - par value of $0.01 authorized 10,000,000 shares; issued and outstanding 6,921,378 shares at September 30, 2015 and 4,145,547 at December 31, 2014	69	41
Capital surplus	70,173	38,360
Retained earnings	9,257	8,696
Accumulated other comprehensive income (loss)	19	(16)
Total shareholders’ equity	92,080	59,643
Total liabilities and shareholders’ equity	$ 924,493	$ 691,416

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

Consolidated Statements of Operations

	Unaudited Nine months ended		Three months ended	
	September 30,		September 30,	
(in thousands)	2015	2014	2015	2014
INTEREST INCOME				
Interest and fees on loans	$23,177	$16,038	$8,405	$5,776
Interest and dividends on securities	179	86	68	28
Other interest income	43	30	16	9
Total interest income	23,399	16,154	8,489	5,813
INTEREST EXPENSE				
Deposits	1,866	1,485	693	560
Short-term borrowings	98	84	43	28
Long-term borrowings	188	162	72	60
Total interest expense	2,152	1,731	808	648
NET INTEREST INCOME	21,247	14,423	7,681	5,165
Provision for credit losses	1,015	2,570	230	2,068
Net interest income after provision for credit losses	20,232	11,853	7,451	3,097
NONINTEREST INCOME				
Service charges on deposit accounts	592	425	189	118
Realized and unrealized gains on mortgage banking activity	5,415	2,864	1,910	1,388
Income from bank owned life insurance	278	281	103	95
Loan fee income	2,140	1,005	848	485
Other operating income	619	282	207	89
Total noninterest income	9,044	4,857	3,257	2,175
NONINTEREST EXPENSE				
Compensation and benefits	12,441	8,456	4,652	2,790
Occupancy and equipment	2,810	1,545	931	489
Amortization of core deposit intangible	248	58	82	17
Marketing and business development	2,093	1,120	786	400
Professional fees	1,080	787	386	217
Data processing fees	902	488	348	174
Merger and restructuring	3,303	82	2,166	82
FDIC Assessment	315	301	106	101
Loan production expense	1,534	704	600	285
Provision for other real estate owned	736	-	736	-
Other operating expense	2,412	1,262	807	406
Total noninterest expense	27,874	14,803	11,600	4,961
INCOME (LOSS) BEFORE INCOME TAXES	1,402	1,907	(892)	311
Income tax expense (benefit)	747	668	(106)	75
NET INCOME (LOSS)	$655	$1,239	$(786)	$236

Preferred stock dividends	94	94	31	31
Net income (loss) available to common shareholders	$561	$1,145	$(817)	$205
NET INCOME (LOSS) PER COMMON SHARE				
Basic	$0.09	$0.28	$(0.13)	$0.05
Diluted	$0.09	$0.28	$(0.13)	$0.05

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

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Consolidated Statements of Comprehensive Income (Loss)

(in thousands)	Unaudited For the nine months ended September 30, 2015	 2014
Net Income	$ 655	$ 1,239
Other comprehensive income		
Investments available-for-sale:		
Net unrealized holding gains (losses)	54	(1)
Related income tax (expense) benefit	(19)	1
Comprehensive income	$ 690	$ 1,239

(in thousands)	Unaudited For the three months ended September 30, 2015	 2014
Net Income (loss)	$ (786)	$ 236
Other comprehensive income		
Investments available-for-sale:		
Net unrealized holding gains (losses)	14	(2)
Related income tax (expense) benefit	(4)	1
Comprehensive income (loss)	$ (776)	$ 235

Consolidated Statements of Changes in Shareholders' Equity (Unaudited)

(dollars in thousands, except share data)	Preferred stock	Number of shares	Common stock	Capital Surplus	Retained Earnings / (Accumulated deficit)	Accumulated other comprehensive income/(loss)	Total
Balances at January 1, 2014	$ 12,562	4,095,650	$ 41	$ 37,607	$ (1,590)	$ 4	$ 48,624
Net income	-	-	-	-	1,239	-	1,239
Dividends paid on preferred stock	-	-	-	-	(94)	-	(94)
Forfeited stock-based compensation	-	(6,668)	-	(34)	-	-	(34)
Issuance of common stock:							
Stock awards	-	4,139	-	41	-	-	41

Exercise of warrants	-	47,068	-	470	-	-	470
Stock-based compensation	-	-	-	133	-	-	133
Balances at September 30, 2014	$12,562	4,140,189	$ 41	$38,217	$ (445)	$ 4	$50,379
Balances at January 1, 2015	$12,562	4,145,547	$ 41	$38,360	$ 8,696	$ (16)	$59,643
Net income	-	-	-	-	655	-	655
Net unrealized gain on securities	-	-	-	-	-	35	35
Dividends paid on preferred stock	-	-	-	-	(94)	-	(94)
Issuance of common stock:							
Stock offering	-	2,173,913	22	23,096	-	-	23,118
Stock awards	-	5,560	-	72	-	-	72
Business combination	-	560,891	6	8,043			8,049
Exercise of options	-	21,465	-	217	-	-	217
Stock-based compensation	-	14,002	-	385	-	-	385
Balances at September 30, 2015	$12,562	6,921,378	$ 69	$70,173	$ 9,257	$ 19	$92,080

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

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Consolidated Statements of Cash Flows (unaudited)

(in thousands)	For the nine months ended September 30, 2015	2014
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$655	$1,239
Adjustments to reconcile net income to net cash from operating activities:		
Provision for credit losses	1,015	2,570
Deferred income (benefit) taxes	(2,153)	108
Provision for other real estate owned	736	-
Depreciation	712	537
Stock-based compensation	457	140
Net amortization of investment securities	(4)	-
Net amortization of intangible asset	248	58
Loans originated for sale	(464,584)	(201,462)
Proceeds from sale of loans originated for sale	448,453	168,956
Realized and unrealized gains on mortgage banking activity	(5,415)	(2,864)
Cash surrender value of BOLI	(278)	(281)
Decrease in interest receivable	(433)	(148)
Increase in interest payable	116	53
Decrease (increase) in other assets	235	(185)
(Decrease) increase in other liabilities	(1,626)	372
Net cash used in operating activities	(21,866)	(30,907)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of investment securities available-for-sale	(13,916)	(31,997)
Proceeds from maturities of investment securities available-for-sale	42,541	33,571
Net increase in loans and leases outstanding	(48,345)	(43,604)
Purchase of premises and equipment	(4,633)	(1,213)
Acquisition activity, net of cash received	8,348	2,096
Net cash used in investing activities	(16,005)	(41,147)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net increase in noninterest-bearing deposits	16,172	16,477
Net (decrease) increase in interest-bearing deposits	(2,850)	27,837
Net (decrease) increase in short-term borrowings	(1,313)	6,299
Proceeds from issuance of long-term debt	5,451	5,000
Repayment of long-term debt	(9,000)	(2,000)
Net proceeds from issuance of common stock, net of cost	23,335	470
Cash dividends on preferred stock	(94)	(94)
Net cash provided by financing activities	31,701	53,989
Net decrease in cash and cash equivalents	(6,170)	(18,065)

Cash and cash equivalents at beginning of period	24,517	35,736
Cash and cash equivalents at end of period	$18,347	$17,671
SUPPLEMENTAL INFORMATION		
Cash payments for interest	$2,035	$1,678
Cash payments for income taxes	2,690	370
Transferred from loans to other real estate owned	-	95
Assets acquired in branch acquisition (net of cash received)	$-	$16,841
Liabilities assumed in branch acquisition	-	18,826
Assets acquired in business combination (net of cash received)	195,237	-
Liabilities assumed in business combination	204,943	-

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

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Notes to Consolidated Financial Statements (unaudited)

Note 1: Summary of Significant Accounting Policies

Nature of Operations

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

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

On October 17, 2014, the Bank acquired certain assets and assumed substantially all deposits and certain other liabilities of NBRS Financial Bank ("NBRS"), which was closed on October 17, 2014 by the Commissioner (the "NBRS Acquisition"). The NBRS Acquisition was completed in accordance with the terms of the Purchase and Assumption Agreement with the Federal Deposit Insurance Corporation (the "FDIC"). The Bank did not acquire any of NBRS's other real estate owned.

On August 28, 2015, Bancorp completed its acquisition of Patapsco Bancorp, Inc. ("Patapsco Bancorp"), the parent company of The Patapsco Bank ("Patapsco Bank"), through the merger of Patapsco Bancorp with and into Bancorp (the "Merger"). The Merger was consummated pursuant to the Agreement and Plan of Merger dated as of March 2, 2015, by and between Bancorp and Patapsco Bancorp, as amended (the "Merger Agreement"). As a result of the Merger, each share of common stock of Patapsco Bancorp was converted into the right to receive, at the holder's election, $5.09 in cash or 0.3547 shares of the Bancorp's common stock, par value $0.01 per share ("Common Stock"), provided that (i) cash was paid in lieu of any fractional shares of Common Stock and (ii) 20% of the shares of common stock of Patapsco Bancorp outstanding at the time of the Merger was exchanged for cash in the Merger, with the remaining shares of Patapsco Bancorp common stock exchanged for 560,891 shares of Common Stock. The aggregate Merger consideration was $10.064 million. In connection with the Merger, the parties have caused Patapsco Bank to merge with and into the Bank, with the Bank the surviving bank.

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

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

Principles of Consolidation

The consolidated financial statements include the accounts of Bancorp, its subsidiary bank and the bank's subsidiaries. All significant intercompany accounts and transactions have been eliminated. Certain reclassifications may have been made to the prior year's consolidated financial statements to conform to current period presentation.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant changes in the near-term relate to the determination of the allowance for credit losses, other-than-temporary impairment of investment securities, deferred income taxes and share-based compensation.

Loans Held for Sale

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

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

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

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

Segment Information

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

New Accounting Pronouncements

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

1. The loan has a government guarantee that is not separable from the loan before foreclosure.

2. At the time of foreclosure, the creditor has the intent to convey the real estate property to the guarantor and make a claim on the guarantee, and the creditor has the ability to recover under that claim.

3. At the time of foreclosure, any amount of the claim that is determined on the basis of the fair value of the real estate is fixed. Upon foreclosure, the separate other receivable should be measured based on the amount of the loan balance (principal and interest) expected to be recovered from the guarantor.

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

ASU No. 2014-12, *Compensation—Stock Compensation (Topic 718): Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period.* The amendments require that a performance target that affects vesting and that could be achieved after the requisite service period be treated as a performance condition. Guidance in Topic 718 as it relates to awards with performance conditions that affect vesting should be applied to account for such awards. As such, the performance target should not be reflected in estimating the grant-date fair value of the award. Compensation cost should be recognized in the period in which it becomes probable that the performance target will be achieved and should represent the compensation cost attributable to the period(s) for which the requisite service has already been rendered. If the performance target becomes probable of being achieved before the end of the requisite service period, the remaining unrecognized compensation cost should be recognized prospectively over the remaining requisite service period. The total amount of compensation cost recognized during and after the requisite service period should reflect the number of awards that are expected to vest and should be adjusted to reflect those awards that ultimately vest. The requisite service period ends when the employee can cease rendering service and still be eligible to vest in the award if the performance target is achieved. As indicated in the definition of vest, the stated vesting period (which includes the period in which the performance target could be achieved) may differ from the requisite service period. The amendments of ASU 2014-12 are effective for interim and annual periods beginning after December 15, 2015. The Company will evaluate this amendment but does not believe it will have an impact on its financial position or results of operations.

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

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

Note 2: Business Combination

Patapsco Acquisition

On August 28, 2015, Bancorp completed its acquisition of Patapsco Bancorp through the merger of Patapsco Bancorp with and into Bancorp pursuant to the Merger Agreement. As a result of the Merger, each share of common stock of Patapsco Bancorp was converted into the right to receive, at the holder's election, $5.09 in cash or 0.3547 shares of Common Stock, provided that (i) cash was paid in lieu of any fractional shares of Common Stock and (ii) 20% of the shares of common stock of Patapsco Bancorp outstanding at the time of the Merger were exchanged for cash in the Merger, with the remaining shares of Patapsco Bancorp common stock exchanged for 560,891 shares of Common Stock. The aggregate Merger consideration was $10.064 million. In connection with the Merger, the parties have caused Patapsco Bank to merge with and into the Bank, with the Bank the surviving bank.

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

The acquired assets and assumed liabilities of Patapsco Bancorp were measured at estimated fair value. Management made significant estimates and exercised significant judgment in accounting for the acquisition of Patapsco Bancorp. Management judgmentally assigned risk ratings to loans based on appraisals and estimated collateral values, expected cash flows, prepayment speeds and estimated loss factors to measure fair values for loans. Deposits and borrowings were valued based upon interest rates, original and remaining terms and maturities, as well as current rates for similar funds in the same markets. Premises and equipment was valued based on recent appraised values. Management used quoted or current market prices to determine the fair value of investment securities.

The statement of net assets acquired and the resulting goodwill recorded is presented in the following tables. As explained in the notes that accompany the following table, the purchased assets, assumed liabilities and identifiable intangible assets were recorded at the acquisition date fair value.

	Acquired Balances as Recorded By Patapsco Bancorp	Fair Value Adjustments	Acquired Balances as Recorded by Bancorp
Cash and due from banks	$ 18,637	$ -	$ 18,637
Overnight investments	410	-	410
Investment securities	26,463	(208)	26,255
Loans	159,858	(2,951)	156,907
Allowance for credit losses	(2,492)	2,492	-
Interest receivable on loans	602	-	602
Fixed assets	2,864	1,321	4,185
Core deposit intangible	-	1,974	1,974
Other assets	5,005	(100)	4,905
Total assets	$ 211,347	$ 2,528	$ 213,875
Deposits - transaction accounts	$ 126,273	$ -	$ 126,273
Certificate of deposit	48,556	254	48,810
Total deposits	174,829	254	175,083
Borrowings	14,000	393	14,393
Junior subordinated debt	5,000	(1,656)	3,344
Other liabilities	2,079	10,044	12,123
Total liabilities	$ 195,908	$ 9,035	$ 204,943
Net assets acquired over/(under)			
Net liabilities assumed	$ 15,439	$ (6,507)	$ 8,932

The following table summarizes the acquired assets and assumed liabilities in the Merger as of the acquisition date, and the resulting goodwill of $1.1 million resulting from the transaction (in thousands):

Assets acquired at fair value:	
Cash and cash equivalents	$19,047
Investment securities available for sale	26,255
Loans	156,907
Accrued interest receivable	602
Other assets	9,090
Core deposit intangible	1,974

Total fair value of assets acquired	$213,875	
Liabilities assumed at fair value:		
Deposits	175,083	
Borrowings	17,737	
Accrued expenses and other liabilities	12,123	
Total fair value of liabilities assumed	$204,943	
Net assets assumed at fair value:		$8,932
Transaction consideration paid to Patapsco Bancorp		10,064
Amount of goodwill resulting from acquisition		$1,132

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Acquired loans

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

	Contractually Required Payments Receivable	Non-Accretable Credit Adjustments	Cash Flows Expected To Be Collected	Accretable FMV Adjustments	Carrying Value of Loans Receivable
Performing Loans Acquired	$ 156,393	$ -	$ 156,393	$ 866	$ 155,527
Impaired Loans Acquired	3,465	1,713	1,752	372	1,380
Total	$ 159,858	$ 1,713	$ 158,145	$ 1,238	$ 156,907

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

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

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

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

Note 3: Investment Securities

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

(in thousands)	September 30, 2015				December 31, 2014			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
U.S. Government Agencies	$37,992	$ 22	$ 2	$ 38,012	$37,010	$ -	$ 29	$ 36,981
Treasuries	-	-	-	-	4,000	-	3	3,997
Mortgage-backed	58	3	-	61	95	6	-	101
Other investments	1,100	5	-	1,105	-	-	-	-
	$39,150	$ 30	$ 2	$ 39,178	$41,105	$ 6	$ 32	$ 41,079

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Gross unrealized losses and fair value by investment category and length of time the individual securities have been in a continuous unrealized loss position at September 30, 2015 and December 31, 2014 are presented below:

September 30, 2015

(in thousands)	Less than 12 months		12 months or more		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
U.S. Government Agencies	$ 7,996	$ 2	$ -	$ -	$7,996	$ 2
Treasuries	-	-	-	-	-	-
Mortgage-backed	-	-	-	-	-	-
Other investments	-	-	-	-	-	-
	$ 7,996	$ 2	$ -	$ -	$7,996	$ 2

December 31, 2014

(in thousands)	Less than 12 months		12 months or more		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
U.S. Government Agencies	$ 26,477	$ 29	$ -	$ -	$26,477	$ 29
Treasuries	3,997	3	-	-	3,997	3
Mortgage-backed	-	-	-	-	-	-
	$ 30,474	$ 32	$ -	$ -	$30,474	$ 32

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

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

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

(in thousands)	September 30, 2015		December 31, 2014	
	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
Amounts maturing:				
One year or less	$ 30,990	$ 30,991	$ 33,516	$ 33,506
After one through five years	7,002	7,021	7,508	7,487
After five through ten years	58	61	81	86
After ten years	1,100	1,105	-	-
	$ 39,150	$ 39,178	$ 41,105	$ 41,079

Because of the composition of the securities portfolio acquired in the Patapsco Bancorp and NBRS acquisitions, management deemed it prudent for interest rate risk management purposes to liquidate both of the acquired portfolios. Thus, in the third quarter of 2015, the Bank both acquired and sold nearly $26.3 million in securities, with no gains or losses incurred upon the liquidation, as the sales were executed within days of the Patapsco Bancorp acquisition. Similarly in the fourth quarter of 2014, the Bank both acquired and sold nearly $31.7 million in securities, which resulted in a net loss on the sale of the securities of $228 thousand. At September 30, 2015 and December 31, 2014, $27.2 million and $30.9 million fair value of securities, respectively, were pledged as collateral for repurchase agreements and for public funds. No single issuer of securities, except for U. S. Government agency securities, had outstanding balances that exceeded ten percent of shareholders' equity.

Note 4: Loans and Leases

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

The loan portfolio segment balances at September 30, 2015 and December 31, 2014 are presented in the following table:

	September 30, 2015			December 31, 2014		
(in thousands)	Legacy	Acquired	Total	Legacy	Acquired	Total
Real estate						
Construction and land	$64,874	$7,535	$72,409	$57,898	$6,260	$64,158
Residential - first lien	86,143	97,610	183,753	68,768	19,525	88,293
Residential - junior lien	12,523	14,069	26,592	11,762	7,539	19,301
Total residential real estate	98,666	111,679	210,345	80,530	27,064	107,594
Commercial - owner occupied	109,351	37,756	147,107	75,307	37,519	112,826
Commercial - non-owner occupied	95,565	60,340	155,905	90,937	33,021	123,958
Total commercial real estate	204,916	98,096	303,012	166,244	70,540	236,784
Total real estate loans	368,456	217,310	585,766	304,672	103,864	408,536
Commercial loans and leases	124,539	40,639	165,178	120,924	18,745	139,669
Consumer	1,170	3,386	4,556	1,878	2,834	4,712
Total loans	$494,165	$261,335	$755,500	$427,474	$125,443	$552,917

There were $64.4 million and $42.9 million in loans held for sale at September 30, 2015 and at December 31, 2014, respectively.

Note 5: Credit Quality Assessment

<u>Allowance for Credit Losses</u>

The following table provides information on the activity in the allowance for credit losses by the respective loan portfolio segment for the nine months and three months ended September 30, 2015 and September 30, 2014:

	September 30, 2015							
(in thousands)	Construction and land	Residential first lien	Residential junior lien	Commercial owner occupied	Commercial non-owner occupied	Commercial loans and leases	Consumer loans	Total
Allowance for credit losses:								
Nine months ended:								
Beginning balance	$174	$ 272	$ 55	$ 160	$ 562	$ 2,366	$ 13	$3,602
Charge-offs	-	-	-	-	-	(640)	(4)	(644)
Recoveries	-	3	1	-	319	18	3	344
Provision for credit losses	302	77	(15)	119	(200)	727	5	1,015
Ending balance	$476	$ 352	$ 41	$ 279	$ 681	$ 2,471	$ 17	$4,317
Three months ended:								
Beginning balance	$504	$ 328	$ 40	$ 266	$ 605	$ 2,439	$ 17	$4,199
Charge-offs	-	-	-	-	-	(146)	-	(146)
Recoveries	-	-	1	-	28	1	4	34
Provision for credit losses	(28)	24	-	13	48	177	(4)	230
Ending balance	$476	$ 352	$ 41	$ 279	$ 681	$ 2,471	$ 17	$4,317

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	September 30, 2014							
(in thousands)	Construction and land	Residential first lien	Residential junior lien	Commercial owner occupied	Commercial non-owner occupied	Commercial loans and leases	Consumer loans	Total
Allowance for credit losses:								
Nine months ended:								
Beginning balance	$122	$ 200	$ 34	$ 131	$ 541	$ 1,464	$ 14	$2,506
Charge-offs	-	-	-	-	-	(2,115)	-	(2,115)
Recoveries	-	-	-	-	4	53	-	57
Provision for credit losses	(13)	5	(11)	195	4	2,393	(3)	2,570
Ending balance	$109	$ 205	$ 23	$ 326	$ 549	$ 1,795	$ 11	$3,018
Three months ended:								
Beginning balance	$159	$ 196	$ 17	$ 138	$ 661	$ 1,871	$ 11	$3,053
Charge-offs	-	-	-	-	-	(2,115)	-	(2,115)
Recoveries	-	-	-	-	-	12	-	12
Provision for credit losses	(50)	9	6	188	(112)	2,027	-	2,068
Ending balance	$109	$ 205	$ 23	$ 326	$ 549	$ 1,795	$ 11	$3,018

The following table provides additional information on the allowance for credit losses by segment:

	September 30, 2015							
(in thousands)	Construction and land	Residential first lien	Residential junior lien	Commercial owner occupied	Commercial non-owner occupied	Commercial loans and leases	Consumer loans	Total
Allowance allocated to:								
Legacy Loans:								
individually evaluated for impairment	$238	$ -	$ 10	$ -	$ -	$ 222	$ -	$470
collectively evaluated for impairment	232	210	31	279	651	2,179	17	3,599
Acquired Loans:								
individually evaluated for impairment	-	-	-	-	30	48	-	78
collectively evaluated for impairment	6	142	-	-	-	22	-	170
Loans:								
Legacy Loans:								
Ending balance	$64,874	$ 86,143	$ 12,523	$ 109,351	$ 95,565	$ 124,539	$ 1,170	$494,165
individually evaluated for impairment	810	655	74	-	2,702	2,585	151	6,977
	64,064	85,488	12,449	109,351	92,863	121,954	1,019	487,188

collectively evaluated for impairment								
Acquired Loans:								
Ending balance	7,535	97,610	14,069	37,756	60,340	40,639	3,386	261,335
individually evaluated for impairment	-	380	-	238	205	1,195	-	2,018
collectively evaluated for impairment	7,535	97,230	14,069	37,518	60,135	39,444	3,386	259,317

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	December 31, 2014							
(in thousands)	Construction and land	Residential first lien	Residential junior lien	Commercial owner occupied	Commercial non-owner occupied	Commercial loans and leases	Consumer loans	Total
Allowance allocated to:								
Legacy Loans:								
individually evaluated for impairment	$60	$ -	$ -	$ -	$ -	$ 483	$ -	$543
collectively evaluated for impairment	108	271	25	142	502	1,745	13	2,806
Acquired Loans:								
individually evaluated for impairment	-	-	30	-	-	55	-	85
collectively evaluated for impairment	6	1	-	18	60	83	-	168
Loans:								
Legacy Loans:								
Ending balance	$56,490	$ 58,904	$ 11,006	$ 85,824	$ 100,589	$ 113,176	$ 1,485	$427,474
individually evaluated for impairment	1,144	308	-	-	2,700	2,073	-	6,225
collectively evaluated for impairment	55,346	58,596	11,006	85,824	97,889	111,103	1,485	421,249
Acquired Loans:								
Ending balance	6,260	19,525	7,539	37,519	33,021	18,745	2,834	125,443
individually evaluated for impairment	-	411	57	-	-	405	92	965
collectively evaluated for impairment	6,260	19,114	7,482	37,519	33,021	18,340	2,742	124,478

When potential losses are identified, a specific provision and/or charge-off may be taken, based on the then current likelihood of repayment, that is at least in the amount of the collateral deficiency, and any potential collection costs, as determined by the independent third party appraisal.

All loans that are considered impaired are subject to the completion of an impairment analysis. This analysis highlights any potential collateral deficiencies. A specific amount of impairment is established based on the Company’s calculation of the probable loss inherent in the individual loan. The actual occurrence and severity of losses involving impaired credits can differ substantially from estimates.

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

September 30, 2015

(in thousands)	Construction and land	Residential first lien	Residential junior lien	Commercial owner occupied	Commercial non-owner occupied	Commercial loans and leases	Consumer loans	Total
Credit quality indicators:								
Legacy Loans:								
Not classified	$64,064	$ 85,488	$ 12,449	$ 109,351	$ 92,716	$ 119,718	$ 1,019	$484,805
Special mention	-	-	-	-	-	1,528	-	1,528
Substandard	-	301	-		2,230	1,613	-	4,144
Doubtful	810	354	74	-	619	1,680	151	3,688
Total	$64,874	$ 86,143	$ 12,523	$ 109,351	$ 95,565	$ 124,539	$ 1,170	$494,165
Acquired Loans:								
Not classified	$7,535	$ 97,230	$ 14,069	$ 37,517	$ 59,613	$ 38,732	$ 3,386	$258,082
Special mention	-	-	-	-	-	-	-	-
Substandard	-	-	-	-	522	712	-	1,234
Doubtful	-	380	-	239	205	1,195	-	2,019
Total	$7,535	$ 97,610	$ 14,069	$ 37,756	$ 60,340	$ 40,639	$ 3,386	$261,335

	December 31, 2014							
(in thousands)	Construction and land	Residential first lien	Residential junior lien	Commercial owner occupied	Commercial non-owner occupied	Commercial loans and leases	Consumer loans	Total
Credit quality indicators:								
Legacy Loans:								
Not classified	$55,346	$ 58,439	$ 10,932	$ 85,580	$ 97,889	$ 111,312	$ 1,485	$420,983
Special mention	-	-	-	-	-	-	-	-
Substandard	1,144	465	74	244	2,700	1,864	-	6,491
Doubtful	-	-	-	-	-	-	-	-
Total	$56,490	$ 58,904	$ 11,006	$ 85,824	$ 100,589	$ 113,176	$ 1,485	$427,474
Acquired Loans:								
Not classified	$6,260	$ 18,567	$ 7,482	$ 37,519	$ 33,021	$ 17,611	$ 2,742	$123,202
Special mention	-	-	-	-	-	-	-	-
Substandard	-	546	-	-	-	729	-	1,275
Doubtful	-	412	57	-	-	405	92	966
Total	$6,260	$ 19,525	$ 7,539	$ 37,519	$ 33,021	$ 18,745	$ 2,834	$125,443

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

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

An aged analysis of past due loans are as follows:

	September 30, 2015				
			Commercial	Commercial	Commercial

(in thousands)	Construction and land	Residential first lien	Residential junior lien	owner occupied	non-owner occupied	loans and leases	Consumer loans	Total
Analysis of past due loans:								
Legacy Loans:								
Accruing loans current	$64,036	$ 85,747	$ 12,400	$ 109,351	$ 94,946	$ 121,705	$ 999	$489,184
Accruing loans past due:								
31-59 days past due	-	-	49	-	-	80	-	129
60-89 days past due	-	42	-	-	-	85	-	127
Greater than 90 days past due	28	-	-	-	-	989	20	1,037
Total past due	28	42	49	-	-	1,154	20	1,293
Non-accrual loans	810	354	74	-	619	1,680	151	3,688
Total loans	$64,874	$ 86,143	$ 12,523	$ 109,351	$ 95,565	$ 124,539	$ 1,170	$494,165
Acquired Loans:								
Accruing loans current	$7,535	$ 97,220	$ 13,996	$ 37,008	$ 59,523	$ 35,456	$ 3,376	$254,114
Accruing loans past due:								
31-59 days past due	-	-	73	274	-	85	5	437
60-89 days past due	-	-	-	-	612	-	-	612
Greater than 90 days past due	-	-	-	236	-	3,903	5	4,144
Total past due	-	-	73	510	612	3,988	10	5,193
Non-accrual loans	-	390	-	238	205	1,195	-	2,028
Total loans	$7,535	$ 97,610	$ 14,069	$ 37,756	$ 60,340	$ 40,639	$ 3,386	$261,335

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

Total loans either in non-accrual status or in excess of ninety days delinquent totaled $10.9 million or 1.44% of total loans outstanding at September 30, 2015, which represents an increase from $5.2 million or 0.94% at December 31, 2014.

The impaired loans at September 30, 2015 and December 31, 2014 are as follows:

	September 30, 2015							
(in thousands)	Construction & land	Residential first lien	Residential junior lien	Commercial owner occupied	Commercial non-owner occupied	Commercial loans and leases	Consumer loans	Total
Impaired loans:								
Legacy Loans:								
Recorded investment	$810	$ 655	$ 74	$ -	$ 2,702	$ 2,585	$ 151	$6,977
With an allowance recorded	810	-	74	-	-	250	-	1,134
With no related allowance recorded	-	655	-	-	2,702	2,335	151	5,843
Related allowance	238	-	10	-	-	222	-	470
Unpaid principal	810	655	74	-	2,702	2,585	151	6,977
Nine months ended								
Average balance of impaired loans	810	603	74	-	3,409	3,020	151	8,067
Interest income recognized	-	19	-	-	78	82	-	179
Three months ended								
Average balance of impaired loans	810	679	74	-	2,880	2,947	151	7,541
Interest income recognized	-	7	-	-	18	20	-	45
Acquired Loans:								
Recorded investment	$-	$ 380	$ -	$ 238	$ 205	$ 1,195	$ -	$2,018
With an allowance recorded	-	-	-	-	82	48	-	130
With no related allowance recorded	-	380	-	238	123	1,147	-	1,888
Related allowance	-	-	-	-	30	48	-	78
Unpaid principal	-	473	-	414	389	3,101	-	4,377
Nine months ended								
Average balance of impaired loans	-	473	-	414	389	3,101	-	4,377
Interest income recognized	-	5	-	4	-	3	-	12
Three months ended								
Average balance of impaired loans	-	483	-	421	480	3,103	-	4,487
Interest income recognized	-	4	-	4	-	-	-	8

December 31, 2014

Commercial Commercial Commercial

(in thousands)	Construction & land	Residential first lien	Residential junior lien	owner occupied	non-owner occupied	loans and leases	Consumer loans	Total
Impaired loans:								
Legacy Loans:								
Recorded investment	$1,144	$ 308	$ -	$ -	$ 2,700	$ 2,073	$ -	$6,225
With an allowance recorded	334	-	-	-	-	690	-	1,024
With no related allowance recorded	810	308	-	-	2,700	1,383	-	5,201
Related allowance	60	-	-	-	-	483	-	543
Unpaid principal	1,144	308	-	-	2,700	2,127	-	6,279
Average balance of impaired loans	1,108	329	-	-	2,713	2,558	-	6,708
Interest income recognized	37	18	-	-	166	167	-	388
Acquired Loans:								
Recorded investment	$-	$ 411	$ 57	$ -	$ -	$ 405	$ 92	$965
With an allowance recorded	-	-	57	-	-	55	-	112
With no related allowance recorded	-	411	-	-	-	350	92	853
Related allowance	-	-	30	-	-	55	-	85
Unpaid principal	-	565	83	-	530	825	327	2,330
Average balance of impaired loans	-	568	83	-	560	829	379	2,419
Interest income recognized	-	-	-	-	-	-	-	-

Included in the total impaired loans above were non-accrual loans of $5.7 million and $4.0 million at September 30, 2015 and December 31, 2014, respectively. Interest income that would have been recorded if non-accrual loans had been current and in accordance with their original terms was $115 thousand for the first nine months of 2015.

Management routinely evaluates other real estate owned ("OREO") based upon periodic appraisals. For the nine months ended September 30, 2015 the Bank recorded a valuation allowance of $736 thousand in non-interest expense for properties where the current appraised values of which were less than the carrying amounts. For the same period of 2014 there was no additional valuation allowances recorded as the current appraised value less estimated cost to sell was higher than the recorded OREO amount. In conjunction with the Patapsco Bancorp acquisition we added one existing property to OREO in the amount of $20 thousand. For the nine months ended September 30, 2015 there were no new loans transferred from loans to OREO and for the same period in 2014 one loan was transferred to OREO. For the first nine months of 2015 and 2014, the Bank did not sell any properties held as OREO.

The trouble debt restructured loans ("TDRs") at September 30, 2015 and December 31, 2014 are as follows:

	September 30, 2015				
(dollars in thousands)	Number of Loans	Non-Accrual Status	Number of Loans	Accrual Status	Total TDRs
Legacy Loans:					
Residential real estate - first lien	-	$ -	1	$ 301	$ 301
Commercial - non-owner occupied	1	594	1	2,083	2,677
	1	$ 594	2	$ 2,384	$ 2,978

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

A summary of TDR modifications outstanding and performing under modified terms are as follows:

September 30, 2015
Performing

(in thousands)	Not Performing to Modified Terms	to Modified Terms	Total TDRs
Legacy Loans:			
Residential real estate (RE) - first lien			
Forbearance	$-	$ 301	$301
Commercial RE - non-owner occupied			
Rate modification	594	2,083	2,677
Total trouble debt restructure loans	$594	$ 2,384	$2,978

	December 31, 2014		
(in thousands)	Not Performing to Modified Terms	Performing to Modified Terms	Total TDRs
Legacy Loans:			
Residential real estate - first lien			
Forbearance	$308	$ -	$308
Commercial loans			
Forbearance	723	-	723
Extension or other modification	-	226	226
Total trouble debt restructure loans	$1,031	$ 226	$1,257

There was one commercial real estate loan restructured in the first nine months of 2015. Performing TDRs were in compliance with their modified terms and there are no further commitments associated with these credits. One performing commercial TDR has been in compliance with its modified term for over 12 consecutive months and was removed from a TDR status during the nine months ended September 30, 2015.

Note 6: Goodwill and Other Intangible Assets

As of September 30, 2015 the Company recorded $1.1 million in goodwill relating to the Patapsco Bancorp acquisition. Goodwill is evaluated for impairment yearly or as events occur or circumstances change that would more-likely-than-not reduce the fair value below the carrying amount. Fair value is determined by using discounted cash flow analyses. Carrying value is determined using an equity allocation methodology considering both regulatory risk-based capital and tangible equity relative to tangible assets.

The Bank has one segment, which is the core banking operations. The table below shows goodwill balances at September 30, 2015. There was no goodwill at December 31, 2014.

(in thousands)	September 30, 2015
Goodwill	
Banking	$ 1,132

The gross carrying amount and accumulated amortization of intangible assets are as follows:

	September 30, 2015			Weighted
(in thousands)	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Average Remaining Life (Years)
Amortizing intangible assets:				
Core deposit intangible	$3,540	$ 423	$ 3,117	7.88

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

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

(in thousands)	
2015	$176
2016	663
2017	513
2018	401
2019	318
Thereafter	1,046
Total amortizing intangible assets	$3,117

In the third quarter of 2015 we recorded $2.0 million in additional core deposit intangible (“CDI”) from the Patapsco Bancorp acquisition. For 2014, we acquired CDI totaling $513 thousand for the Havre de Grace branch acquisition, and $677 thousand from the NBRS Acquisition.

Note 7: Deposits

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

(dollars in thousands)	September 30, 2015		December 31, 2014	
	Amount	% of Total	Amount	% of Total
Noninterest-bearing demand	$ 171,349	23 %	$ 142,727	26 %
Interest-bearing checking	62,979	8	49,988	9
Money market accounts	227,074	31	140,426	25
Savings	51,872	7	31,354	6
Certificates of deposit $100,000 and over	131,349	18	108,904	19
Certificates of deposit under $100,000	98,143	13	80,640	15
Total deposits	$ 742,766	100 %	$ 554,039	100 %

The acquisition of Patapsco Bancorp added approximately $172.7 million in additional deposits at September 30, 2015.

Note 8: Stock Options and Other Equity Awards

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

Stock awards may also be granted to non-employee members of the Board of Directors as compensation for attendance and participation at meetings of the Board of Directors and meetings of the various committees of the Board. For the nine months ended September 30, 2015 directors were issued 5,560 shares of stock as compensation for their service.

Stock Options

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

	September 30, 2015		December 31, 2014	
	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price
Balance at January 1,	264,652	$ 11.75	387,101	$ 11.19
Granted	-	-	-	-
Exercised	(21,465)	10.11	(4,139)	8.79
Forfeited	(21,711)	10.98	(118,310)	10.02
Balance at period end	221,476	$ 11.99	264,652	$ 11.75
Exercisable at period end	221,476	$ 11.99	264,652	$ 11.75
Weighted average fair value of options granted during the year		$ -		$ -

The intrinsic value of a stock option is the amount that the market value of the underlying stock exceeds the exercise price of the option. Based upon a fair market value of $14.20 at September 30, 2015 the options outstanding had an aggregate intrinsic value of $490 thousand. At December 31, 2014, based upon fair market value of $11.40, the options outstanding had an aggregate intrinsic value of $175 thousand.

Restricted Stock

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

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

	September 30, 2015		December 31, 2014	
	Shares	Weighted Average Grant Date Fair Value	Shares	Weighted Average Grant Date Fair Value
Balance at January 1,	33,330	$ 6.89	50,000	$ 6.89
Granted	-	-	-	-
Vested	(18,336)	6.89	(10,002)	6.91
Forfeited	(1,666)	-	(6,668)	6.85
Balance at period end	13,328	$ 6.89	33,330	$ 6.89

At September 30, 2015, based on restricted stock awards outstanding at that time, the total unrecognized pre-tax compensation expense related to unvested restricted stock awards was $46 thousand. This expense is expected to be recognized through 2016.

Restricted Stock Units

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

In 2014, 44,500 RSUs were granted, with 19,500 of the RSUs subject to a three year vesting schedule with one-third of the RSUs vesting each year on the grant date anniversary. The remaining 25,000 awarded RSUs also are subject to a three year vesting schedule; however, they only vest if certain annual performance measures are satisfactorily achieved. During the first nine months of 2015, 73,500 RSUs were granted, with 43,500 of the RSUs subject to a three year vesting schedule with one-third of the RSUs vesting each year on the grant date anniversary. The remaining 30,000 awarded RSUs also are subject to a three year vesting schedule; however, they only vest if certain annual performance measures are satisfactorily achieved.

The following table presents a summary of the activity for the Company’s RSUs for the periods ended:

	September 30, 2015		December 31, 2014	
	Shares	Weighted Average Grant Date Fair Value	Shares	Weighted Average Grant Date Fair Value
Balance at January 1,	44,500	$ 11.21	-	$ -
Granted	73,500	14.00	44,500	11.21
Vested	(19,836)	11.64	-	-
Forfeited	(8,333)	(12.92)	-	-
Balance at period ended	89,831	$ 13.23	44,500	$ 11.21

At September 30, 2015, based on RSU awards outstanding at that time, the total unrecognized pre-tax compensation expense related to unvested RSU awards was $990 thousand. This expense is expected to be recognized through 2018.

Stock-Based Compensation Expense: Stock-based compensation is recognized as compensation cost in the statement of operations based on the fair values on the measurement date, which, for the Company, is the date of the grant. The Company recognized stock-based compensation expense related to the issuance of restricted stock and restricted stock units of $385 thousand as well as $72 thousand for director compensation paid in stock for the period ended September 30, 2015.

Valuation of Stock-Based Compensation: The fair value of the Company's stock options granted as compensation is estimated on the measurement date, which, for the Company, is the date of grant. The fair value of stock options was calculated using the Black-Scholes option-pricing model. There were no stock options granted during the nine months ended September 30, 2015 or in 2014.

Note 9: Benefit Plans

Profit Sharing Plan

The Company sponsors a defined contribution retirement plan through a Section 401(k) profit sharing plan. Employees may contribute up to 15% of their pretax compensation. Participants are eligible for matching Company contributions up to 4% of eligible compensation dependent on the level of voluntary contributions. The Company's matching contributions increased to $391 thousand for the nine months ended September 30, 2015 up from $204 thousand for the nine months ended September 30, 2014, as a result of a large increase in the number of participants in the plan during the 12 months ended September 30, 2015. The Company's matching contributions vest immediately.

Supplemental Executive Retirement Plan (SERP)

In 2014, the Bank created a SERP for the Chief Executive Officer. Under the defined benefit SERP, Ms. Scully will receive $100,000 each year for 15 years after attainment of the Normal Retirement Age (as defined in the SERP). Ms. Scully will earn vesting on a graduated schedule in which she will become fully vested on August 25, 2019, which has been established for purposes of the SERP as her retirement date. Expense related to this plan totaled $68 thousand for the nine month period ending September 30, 2015.

Note 10: Income per Common Share

The table below shows the presentation of basic and diluted income per common share for the periods ended:

	Nine months ended September 30,		Three months ended September 30,	
(dollars in thousands, except per share data)	2015	2014	2015	2014
Net income (loss)	$655	$1,239	$(786)	$236
Preferred stock dividends	(94)	(94)	(31)	(31)
Net income (loss) available to common shareholders (numerator)	$561	$1,145	$(817)	$205
BASIC				
Basic average common shares outstanding (denominator)	5,897,325	4,061,598	6,493,987	4,081,685
Basic income (loss) per common share	$0.09	$0.28	$(0.13)	$0.05
DILUTED				
Average common shares outstanding	5,897,325	4,061,598	6,493,987	4,081,685
Dilutive effect of common stock equivalents	127,648	75,865	0	91,916
Diluted average common shares outstanding (denominator)	6,024,973	4,137,463	6,493,987	4,173,601

Diluted income (loss) per common share	$0.09	$0.28	$(0.13)	$0.05
Common stock equivalents outstanding that are anti-dilutive and thus excluded from calculation of diluted number of shares presented above	2,150	209,347	156,270	209,347

Note 11: Risk-Based Capital

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

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

In addition, under revised prompt corrective action requirements effective January 1, 2015, in order to be considered "well-capitalized," Bancorp and the Bank must have CET 1 ratios of 6.5%, Tier 1 ratios of 8.0%, total risk-based capital ratios of 10.0% and leverage ratios of 5.0%.

Management believes that, as of September 30, 2015 and December 31, 2014, Bancorp and the Bank met all capital adequacy requirements to which they are subject.

(dollars in thousands)	Actual Amount	Ratio	For capital adequacy purposes Amount	Ratio	To be well capitalized under the FDICIA prompt corrective action provisions Amount	Ratio
As of September 30, 2015:						
Total capital (to risk-weighted assets)						
Howard Bank	$86,843	11.14%	$ 62,365	8.00 %	$77,956	10.00 %
Howard Bancorp	$94,303	12.12%	$ 62,263	8.00 %	**N/A**	
Common equity tier 1 capital (to risk-weighted assets)						
Howard Bank	$82,524	10.59%	$ 35,080	4.50 %	$50,671	6.50 %
Howard Bancorp	$89,986	11.56%	$ 35,023	4.50 %	**N/A**	
Tier 1 capital (to risk-weighted assets)						
Howard Bank	$82,524	10.59%	$ 46,774	6.00 %	$62,365	8.00 %
Howard Bancorp	$89,986	11.56%	$ 46,698	6.00 %	**N/A**	
Tier 1 capital (to average assets)						
(Leverage ratio)						
Howard Bank	$82,524	10.25%	$ 32,199	4.00 %	$40,248	5.00 %
Howard Bancorp	$89,986	11.16%	$ 32,250	4.00 %	**N/A**	
As of December 31, 2014:						
Total capital (to risk-weighted assets)						
Howard Bank	$61,393	10.69%	$ 45,932	8.00 %	$57,415	10.00 %
Howard Bancorp	$61,811	10.73%	$ 46,067	8.00 %	N/A	
Tier 1 capital (to risk-weighted assets)						
Howard Bank	$57,791	10.07%	$ 22,966	4.00 %	$34,449	6.00 %
Howard Bancorp	$58,208	10.11%	$ 23,033	4.00 %	N/A	
Tier 1 capital (to average assets)						

(Leverage ratio)				
Howard Bank	$57,791	8.54 %	$ 27,073	4.00 %	$33,842	5.00 %
Howard Bancorp	$58,208	8.60 %	$ 27,072	4.00 %	N/A	

The Bank is currently prohibited from paying dividends without the prior approval of the Commissioner.

Note 12: Preferred Stock

On September 22, 2011, we entered into a Securities Purchase Agreement with the Secretary of the Treasury, pursuant to which Bancorp issued and sold to the Treasury 12,562 shares of our Senior Non-Cumulative Perpetual Preferred Stock, Series AA, having a liquidation preference of $1,000 per share, for aggregate proceeds of $12,562,000. The issuance was pursuant to the Treasury's Small Business Lending Fund (SBLF) program, a $30 billion fund established under the Small Business Jobs Act of 2010, which encourages lending to small businesses by providing capital to qualified community banks with assets of less than $10 billion. The Series AA Preferred Stock holders are entitled to receive non-cumulative dividends payable quarterly on each January 1, April 1, July 1 and October 1, beginning October 1, 2011. The dividend rate, which is calculated on the aggregate Liquidation Amount, had been initially set at 5% per annum based upon the current level of "Qualified Small Business Lending" ("QSBL") by the Bank and is currently set at 1%. The dividend rate for future dividend periods will be set based upon the percentage change in qualified lending between each dividend period and the baseline QSBL level established at the time the Agreement was entered into. Such dividend rate may vary from 1% per annum to 5% per annum for the second through tenth dividend periods and from 1% per annum to 7% per annum for the eleventh through the eighteenth dividend periods and through March 22, 2016 with respect to the nineteenth dividend period. If the Series AA Preferred Stock remains outstanding for more than four-and-one-half years, the dividend rate will be fixed at 9%. Prior to that time, in general, the dividend rate decreases as the level of the Bank's QSBL increases. Such dividends are not cumulative, but Bancorp may only declare and pay dividends on its common stock (or any other equity securities junior to the Series AA Preferred Stock) if it has declared and paid dividends for the current dividend period on the Series AA Preferred Stock, and will be subject to other restrictions on its ability to repurchase or redeem other securities. In addition, if (i) we have not timely declared and paid dividends on the Series AA Preferred Stock for six dividend periods or more, whether or not consecutive, the Treasury (or any successor holder of Series AA Preferred Stock) may designate a representative to attend all meetings of Bancorp's Board of Directors in a nonvoting observer capacity and Bancorp must give such representative copies of all notices, minutes, consents and other materials that Bancorp provide to its directors in connection with such meetings.

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

Note 13: Fair Value

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

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

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

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

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

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

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

Recurring Fair Value Measurements

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

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

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

Non-recurring Fair Value Measurements

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

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

Other real estate owned acquired through, or in lieu of, foreclosure are held for sale and are initially recorded at fair value, less selling costs. Any write-downs to fair value at the time of transfer to OREO are charged to the allowance for credit losses subsequent to foreclosure. Values are derived from appraisals of underlying collateral and discounted cash flow analysis. There was a $736 thousand valuation loss recognized in the third quarter of 2015. During the nine months ended September 30, 2014 there was no valuation loss recognized.

The following table sets forth the Company's financial assets and liabilities that were accounted for or disclosed at fair value on a recurring basis at September 30, 2015 and December 31, 2014:

September 30, 2015 (in thousands)	Carrying Value (Fair Value)	Quoted Price in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Investment securities:				
U.S. Goverment agencies	$ 38,012	$ -	$ 38,012	$ -
Mortgage-backed securities	61	-	61	-
Other investments	1,105	-	1,105	-
Loans held for sale	64,427	-	64,427	-
Rate lock commitments	560	-	560	-

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

Assets under fair value option:

September 30, 2015 (in thousands)	Carrying Fair Value Amount	Aggregate Unpaid Principal	Difference
Loans held for sale	$ 64,427	$ 62,674	$ 1,753

25

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

There were no loans held for sale that were non-accrual or 90 days or more past due and still accruing interest at the end of either period presented. Net gain from the changes included in earnings in fair value of loans held for sale was $540 thousand and $1.2 million during the periods ended September 30, 2015 and December 31, 2014, respectively.

The following table sets forth the Company's financial assets and liabilities that were accounted for or disclosed at fair value on a nonrecurring basis at September 30, 2015 and December 31, 2014. OREO is carried at fair value less anticipated costs to sell. Impaired loans are measured using the fair value of collateral, if applicable.

September 30, 2015 (in thousands)	Carrying Value (Fair Value)	Quoted Price in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Other real estate owned	$ 1,764	$ -	$ -	$ 1,764
Impaired loans:				
Construction and land	572	-	-	572
Residential - first lien	1,035	-	-	1,035
Residential - junior lien	64	-	-	64
Commercial - owner occupied	238	-	-	238
Commercial - non-owner occupied	2,877	-	-	2,877
Commercial loans and leases	3,510	-	-	3,510
Consumer	151	-	-	151

December 31, 2014 (in thousands)	Carrying Value (Fair Value)	Quoted Price in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Other real estate owned	$ 2,472	$ -	$ -	$ 2,472
Impaired loans:				
Construction and land	1,084	-	-	1,084
Residential - first lien	719	-	-	719
Residential - junior lien	27	-	-	27
Commercial - owner occupied	-	-	-	-
Commercial - non-owner occupied	2,700	-	-	2,700
Commercial loans and leases	1,940	-	-	1,940

Consumer	92	-	-	92

At September 30, 2015 OREO consisted of the outstanding balance of $4.6 million, less valuation allowance of $2.9 million and at December 31, 2014 balance was $4.6 million with a valuation allowance of $2.1 million. Impaired loans had a recorded investment of $8.9 million and $7.2 million at September 30, 2015 and December 31, 2014, respectively. Related allowance on impaired loans for the period ended September 30, 2015 and year ended December 31, 2014 was $0.5 million and $0.6 million, respectively.

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

The following table presents required information in accordance with ASC Topic 825 “Financial Instruments” at September 30, 2015 and December 31, 2014. The fair value of a financial instrument is the amount at which the instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale. Fair value estimates are based on quoted market prices where available or calculated using present value techniques. Since quoted market prices are not available on many of our financial instruments, estimates may be based on the present value of estimated future cash flows and estimated discount rates. These financial assets and liabilities have not been recorded at fair value.

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

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

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

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

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

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

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

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

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

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

	September 30, 2015				
(in thousands)	Carrying Amount	Fair Value	Quoted Price in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Financial Assets					
Investment securities	$39,178	$39,178	$ -	$ 39,178	$ -
Nonmarketable equity securities	3,185	3,185	-	3,185	-
Loans held for sale	64,427	64,427	-	64,427	-
Rate lock commitments	560	560	-	560	-
Loans and leases	751,183	751,939	-	-	751,939
Financial Liabilities					
Deposits	742,766	742,236	-	-	742,236
Short-term borrowings	52,708	52,708	-	52,708	-
Long-term borrowings	27,851	28,161	-	28,161	-

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

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

This section is intended to help our stockholders and potential investors understand our financial performance through a discussion of the factors affecting our consolidated financial condition at September 30, 2015 and December 31, 2014 and our consolidated results of operations for the periods ended September 30, 2015 and September 30, 2014. This section should be read in conjunction with the consolidated financial statements and notes to the consolidated financial statements.

Overview

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

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

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

Our results of operations depend mainly on our net interest income, which is the difference between the interest income we earn on our loan and investment portfolios and the interest expense we pay on deposits and borrowings. Results of operations are also affected by provisions for credit losses, noninterest income and noninterest expense. Our noninterest expense consists primarily of compensation and employee benefits, as well as office occupancy, deposit insurance and general administrative and data processing expenses. Our operations are significantly affected by general economic and competitive conditions, particularly with respect to changes in interest rates, government policies and actions of regulatory authorities. Future changes in applicable laws, regulations or government policies may materially affect our financial condition and results of operations.

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

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

On June 2, 2015, Bancorp sold 2,173,913 shares of its common stock, par value $0.01 per share, at a purchase price of $11.50 per share or an aggregate of $25 million, to certain institutional accredited investors pursuant to investment agreements between Bancorp and such institutional investors dated as of March 2, 2015, in a private placement offering.

On August 28, 2015, Bancorp completed its acquisition of Patapsco Bancorp, the parent company of The Patapsco Bank, through the merger of Patapsco Bancorp with and into the Company. The Merger was consummated pursuant to the Agreement and Plan of Merger dated as of March 2, 2015, by and between the Company and Patapsco Bancorp, as amended.

Total assets increased $233.1 million or 33.7% when comparing September 30, 2015 assets of $924.5 million to the $691.4 million at December 31, 2014. Total loans outstanding of $755.5 million at the end of September 2015 showed an increase of $202.6 million or 36.6% compared to total loans of $552.9 million on December 31, 2014. Total deposits grew by $188.7 million or 34.1% when comparing September 30, 2015 to December 31, 2014.

The first nine months of 2015 net income was $655 thousand, which represents a decrease of $584 thousand or 47.1% over net income for the same period of 2014. Net interest income for the nine months ended September 30, 2015 was $21.2 million versus $14.4 million for the first nine months of 2014, an increase of approximately $6.8 million or 47.3%. Total noninterest income was $9.0 million for the first nine months of 2015, compared to a total of $4.9 million for the same period in 2014. Total noninterest expenses increased to $27.9 million from $14.8 million for the nine months ended September 30, 2015 and 2014, respectively.

Critical Accounting Policies

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

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

We cannot predict with certainty the amount of loan charge-offs that we will incur. We do not currently determine a range of loss with respect to the allowance for credit losses. In addition, our regulatory agencies, as an integral part of their examination processes, periodically review our allowance for credit losses. Such agencies may require that we recognize additions to the allowance for credit losses based on their judgments about information available to them at the time of their examination. To the extent that actual outcomes differ from management's estimates, additional provisions to the allowance for credit losses may be required that would adversely impact earnings in future periods.

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

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

Balance Sheet Analysis and Comparison of Financial Condition

A comparison between September 30, 2015 and December 31, 2014 balance sheets is presented below.

Assets

Total assets increased $233.1 million, or 33.7%, to $924.5 million at September 30, 2015 compared to $691.4 million at December 31, 2014. This asset growth was primarily due to growth of $202.9 million in total loans and leases and $21.5 million in loans held for sale, partially offset by decreases of $6.2 million in cash and cash equivalents and $1.9 million in investment securities. The main catalyst of balance sheet growth relates to the Patapsco Bancorp acquisition, which provided additional assets of $177.0 million at September 30, 2015.

The increase in loans held for sale is attributable to the Bank's continuing expansion of the mortgage banking division. The loan portfolio growth resulted primarily from the Patapsco Bancorp acquisition contributing $157 million while organic growth added $46 million, for a $755.5 million balance of loans and leases at September 30, 2015, which compares to $552.9 million at December 31, 2014. The decrease of $8.1 million in cash and cash equivalents and investment securities was used to provide funding for the growth in loans.

The asset growth was funded primarily from increases in customer deposits and increased borrowings. Deposits increased from $554.0 million at December 31, 2014 to $742.8 million at September 30, 2015, an increase of $188.7 million or 34.6%. The Patapsco Bancorp acquisition provided additional deposits of $173 million while organic growth represented $16 million or 8.3% of total deposit growth. Noninterest-bearing deposits represented 23.1% of total deposits at September 30, 2015, down slightly from 25.8% at December 31, 2014. The decrease in the percentage of noninterest-bearing deposits to total deposits was partially due to the mix of deposits acquired from Patapsco Bank, as Patapsco Bank's noninterest-bearing deposits represented just 7.5% of their total deposits we acquired in the Merger. Borrowing levels increased $13.0 million or 19.2% from $67.6 million at December 31, 2014 to $80.6 million at September 30, 2015. Included in long-term borrowing is $3.3 million Junior Subordinated Debentures associated with the Patapsco Bancorp acquisition that mature in December 2035.

Securities Available for Sale

We currently hold U.S. agency securities, mortgage backed securities and mutual fund instruments in our securities portfolio, all of which are categorized as available for sale. The investment in a mutual fund is a supplement to our community reinvestment program activities. We use our securities portfolio to provide the required collateral for funding via commercial customer repurchase agreements as well as to provide sufficient liquidity to fund our loans and provide funds for withdrawals of deposited funds. At September 30, 2015 and December 31, 2014 we held an investment in stock of the Federal Home Loan Bank of Atlanta (“FHLB”) of $3.2 million and $2.6 million, respectively. This investment is required for continued FHLB membership and is based partially upon the amount of borrowings outstanding from the FHLB. These investments are carried at cost. We have never held stock in Fannie Mae or Freddie Mac.

The following tables set forth the composition of our investment securities portfolio at the dates indicated.

(in thousands)	**September 30, 2015**		December 31, 2014	
	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
U.S. Government				
Agencies	$ 37,992	$ 38,012	$ 37,010	$ 36,981
Treasuries	-	-	4,000	3,997
Mortgage-backed	58	61	95	101
Other investments	1,100	1,105	-	-
	$ 39,150	$ 39,178	$ 41,105	$ 41,079

We had securities available for sale of $39.2 million and $41.1 million at September 30, 2015 and December 31, 2014, respectively, which were recorded at fair value. This represents a decrease of $1.9 million, or 4.6%, from the prior year end. The decrease in our securities portfolio resulted solely from scheduled maturities. The funds received upon maturity were used to fund the growth in both portfolio loans and loans held for sale, while maintaining an appropriate amount of securities to collateralize our repurchase agreements. We did not record any gains or losses on the sales or calls of securities for the nine months ended September 30, 2015, even though we did liquidate the entire investment portfolio acquired in the Patapsco Bancorp acquisition. Similar to Patapsco Bancorp, because of the composition of the securities portfolio acquired in the NBRS Acquisition, management deemed it prudent for interest rate risk management purposes to liquidate the entire acquired portfolio. Thus, in the fourth quarter of 2014, the Bank both acquired and sold nearly $31.7 million in securities, which resulted in a net loss on the sale of the securities of $228 thousand.

With respect to our portfolio of securities available for sale, the portfolio contained five securities with unrealized losses of $2 thousand and 14 securities with unrealized losses of $32 thousand at September 30, 2015 and December 31, 2014, respectively. Changes in the fair value of these securities resulted primarily from interest rate fluctuations. We do not intend to sell these securities nor is it more likely than not that we would be required to sell these securities before their anticipated recovery, and we believe the collection of the investment and related interest is probable. Based on this analysis, we consider all of the unrealized losses to be temporary in nature.

Loan and Lease Portfolio

Total loans and leases increased by $202.6 million or 36.6%, to $755.5 million at September 30, 2015 from $552.9 million at December 31, 2014. Included in this growth is $157 million in loans associated with the Patapsco Bancorp acquisition and $46 million in organic growth. Approximately 17% of the growth in residential real estate is reflective of our mortgage banking activities. At September 30, 2015, total loans were 81.7% of total assets, up from 80.0% of total assets at December 31, 2014. The composition of loans acquired in the Patapsco Bancorp acquisition consisted of the following at September 30, 2015:

- $4 million in construction and land
- $81 million in residential first lien
- $5 million in residential junior lien
- $38 million in commercial real estate
- $28 million in commercial and industrial
- $1 million in consumer credit

The following table sets forth the composition of our loan and lease portfolio at the dates indicated. In addition to the loan amounts below, we had loans held for sale of $64.4 million at September 30, 2015, and $42.9 million at December 31, 2014.

(dollars in thousands)	September 30, 2015		December 31, 2014	
	Amount	Percent	Amount	Percent
Real Estate				
Construction and land	$ 72,409	9.6 %	$ 64,158	11.6 %
Residential - first lien	183,753	24.3	88,293	16.0
Residential - junior lien	26,592	3.5	19,301	3.5
Total residential real estate	210,345	27.8	107,594	19.5
Commercial - owner occupied	147,107	19.5	112,826	20.4
Commercial - non-owner occupied	155,905	20.6	123,958	22.4
Total commercial real estate	303,012	40.1	236,784	42.8
Total real estate loans	585,766	77.5	408,536	73.9
Commercial loans and leases	165,178	21.9	139,669	25.2
Consumer loans	4,556	0.6	4,712	0.9
Total loans and leases	$ 755,500	100.0 %	$ 552,917	100.0 %

Deposits

Our deposits increased from $554.0 million at December 31, 2014 to $742.8 million at September 30, 2015, an increase of $188.7 million or 34.1%. Included in this deposit growth is $173 million associated with the Patapsco Bancorp acquisition, which consisted of the following at September 30, 2015:

- $13 million in non-interest bearing demand accounts
- $18 million in interest bearing demand accounts
- $76 million in money market accounts
- $18 million in saving accounts
- $48 million in certificate of deposit accounts

Eliminating the effect of the Patapsco Bancorp acquisition on deposit growth, interest-bearing checking and certificates of deposit decreased from December 31, 2014 levels while all other categories of deposits increased from the year ended December 31, 2014. When comparing organic growth at September 30, 2015 to December 31, 2014, noninterest-bearing deposits experienced a $15.9 million or 11.2% increase, money market accounts a $10.1 million or 7.2% increase and savings accounts a $2.6 million or 8.2% increase. Offsetting these increases were decreases in interest-bearing checking accounts of $5.4 million or 10.8% and certificates of deposit of $7.7 million or 4.1%.

The following tables set forth the distribution of total deposits, by account type, at the dates indicated.

(dollars in thousands)	September 30, 2015	December 31, 2014

	Amount	% of Total	Amount	% of Total
Noninterest-bearing demand	$ 171,349	23 %	$ 142,727	26 %
Interest-bearing checking	62,979	8	49,988	9
Money market accounts	227,074	31	140,426	25
Savings	51,872	7	31,354	6
Certificates of deposit $100,000 and over	131,349	18	108,904	19
Certificates of deposit under $100,000	98,143	13	80,640	15
Total deposits	$ 742,766	100 %	$ 554,039	100 %

Borrowings

Customer deposits remain the primary source utilized to meet funding needs. Borrowings consist of overnight unsecured master notes, overnight securities sold under agreement to repurchase ("repurchase agreements"), FHLB advances, and a junior subordinated debenture assumed in the acquisition of Patapsco Bancorp. Our borrowings totaled $80.6 million at September 30, 2015 and $67.6 million at December 31, 2014. Short-term borrowings totaled $52.7 million at September 30, 2015 and $48.6 million at December 31, 2014. We had eight long-term FHLB advances outstanding totaling $24.5 million at September 30, 2015 compared to seven FHLB advances outstanding totaling $19.0 million at December 31, 2014.

Shareholders' Equity

Total shareholders' equity increased by $32.4 million, or 54.4%, from $59.6 million at December 31, 2014 to $92.1 million at September 30, 2015. The increase in shareholders' equity is primarily the result of the proceeds from our private placement of 2,173,913 shares of common stock in June 2015, which added over $23.1 million to equity, and the Patapsco Bancorp acquisition pursuant to which we issued 560,891 shares of common stock representing additional common equity of over $8.0 million.

Total shareholders' equity at September 30, 2015 represents a capital to asset ratio of 10.0%, while the total shareholders' equity at December 31, 2014 represents a capital to asset ratio of 8.6%. At September 30, 2015 the Bank's regulatory capital ratios substantially exceed levels required to be considered "well-capitalized" under applicable regulatory guidelines.

Average Balance and Yields

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

	Nine months ended September 30,					
	2015			2014		
(dollars in thousands)	Average Balance	Income / Expense	Yield / Rate	Average Balance	Income / Expense	Yield / Rate
Earning assets						
Loans and leases: [1]						
Commercial loans and leases	$140,432	$5,158	4.91 %	$103,232	$3,749	4.86 %
Commercial real estate	257,428	10,068	5.23	203,002	7,573	4.99
Construction and land	64,216	2,274	4.73	57,346	2,195	5.12
Residential real estate	123,080	4,188	4.55	56,889	1,924	4.52
Consumer	4,192	181	5.76	1,082	47	5.79
Total loans and leases	589,348	21,869	4.96	421,551	15,488	4.91
Loans held for sale [2]	48,690	1,308	3.59	20,945	550	3.51
Federal funds sold	23,122	43	0.25	20,384	30	0.19
Securities: [2]						
U.S. Treasury	2,769	12	0.58	88	1	0.77
U.S Gov agencies	31,630	77	0.33	19,636	14	0.10
Mortgage-backed	1,686	3	0.21	141	5	4.51
Other investments	3,314	87	3.50	2,448	66	3.63
Total securities	39,399	179	0.61	22,312	86	0.52
Total earning assets	700,559	23,399	4.47	485,192	16,154	4.45
Cash and due from banks	6,984			5,627		
Bank premises and equipment, net	14,645			11,345		
Other assets	17,755			17,598		
Less: allowance for credit losses	(4,024)			(2,818)		
Total assets	$735,919			$516,944		
Interest-bearing liabilities						
Deposits:						
Interest-bearing demand accounts	$45,007	$71	0.21 %	$31,610	$59	0.25 %
Money market	153,695	552	0.48	107,488	369	0.46
Savings	36,295	40	0.15	12,609	22	0.23
Time deposits	211,929	1,203	0.76	161,161	1,035	0.86
Total interest-bearing deposits	446,926	1,866	0.56	312,868	1,485	0.63
Short-term borrowings	47,406	98	0.28	38,002	84	0.30

Long-term borrowings	20,507	188	1.23	20,237	162	1.07
Total interest-bearing funds	514,839	2,152	0.56	371,107	1,731	0.62
Noninterest-bearing deposits	143,239			95,669		
Other liabilities and accrued expenses	7,223			911		
Total liabilities	665,300			467,687		
Shareholders' equity	70,618			49,257		
Total liabilities & shareholders' equity	$735,919			$516,944		
Net interest rate spread [3]		$21,247	3.91 %		$14,423	3.83 %
Effect of noninterest-bearing funds			0.14			0.15
Net interest margin on earning assets [4]			4.05 %			3.97 %

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

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

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

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

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	Three months ended September 30,					
	2015			2014		
(dollars in thousands)	Average Balance	Income / Expense	Yield / Rate	Average Balance	Income / Expense	Yield / Rate
Earning assets						
Loans and leases: [1]						
Commercial loans and leases	$149,237	$ 1,798	4.78 %	$107,984	$ 1,301	4.78 %
Commercial real estate	271,633	3,563	5.20	203,037	2,685	5.25
Construction and land	68,284	816	4.74	61,674	734	4.72
Residential real estate	146,785	1,611	4.35	66,304	754	4.51
Consumer	4,111	56	5.42	1,211	17	5.66
Total loans and leases	640,050	7,844	4.86	440,210	5,491	4.95
Loans held for sale [2]	62,555	561	3.56	32,157	285	3.51
Federal funds sold	25,434	16	0.25	19,354	9	0.18
Securities: [2]						
U.S. Treasury	478	10		261	-	-
U.S. Gov agencies	37,040	26	0.28	16,782	3	0.08
Mortgage-backed	4,832	1	0.06	123	1	4.46
Other investments	4,002	31	3.05	2,566	24	3.68
Total securities	46,352	68	0.58	19,732	28	0.57
Total earning assets	774,391	8,489	4.35	511,453	5,813	4.51
Cash and due from banks	7,163			6,242		
Bank premises and equipment, net	17,260			11,532		
Other assets	13,844			17,737		
Less: allowance for credit losses	(4,334)			(3,059)		
Total assets	$808,324			$543,905		
Interest-bearing liabilities						
Deposits:						
Interest-bearing demand accounts	$47,017	$ 25	0.21 %	$31,123	$ 20	0.25 %
Money market	176,851	211	0.47	118,246	158	0.53
Savings	41,236	16	0.15	12,510	7	0.21
Time deposits	222,690	441	0.79	166,404	375	0.89
Total interest-bearing deposits	487,794	693	0.56	328,283	560	0.68
Short-term borrowings	53,554	43	0.32	40,755	28	0.27
Long-term borrowing	23,163	72	1.23	22,728	60	1.05
Total interest-bearing funds	564,511	808	0.57	391,766	648	0.66
Noninterest-bearing deposits	151,410			101,168		
Other liabilities and accrued expenses	6,792			1,168		
Total liabilities	722,713			494,102		
Shareholders' equity	85,611			49,803		
Total liabilities & shareholders' equity	$808,324			$543,905		
Net interest rate spread [3]		$ 7,681	3.78 %		$ 5,165	3.85 %
Effect of noninterest-bearing funds			0.16			0.14
Net interest margin on earning assets [4]			3.94 %			4.01 %

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

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

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

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

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Rate/Volume Analysis

The following table presents the effects of changing rates and volumes on our net interest income for the periods indicated. The rate column shows the effects attributable to changes in rate (changes in rate multiplied by prior volume). The volume column shows the effects attributable to changes in volume (changes in volume multiplied by prior rate). The total column is further broken down to show the impact of changes in either rates or volumes. For purposes of this table, changes attributable to both rate and volume, which cannot be segregated, have been allocated proportionately, based on the changes due to rate and the changes due to volume.

	Nine months ended September 30, 2015 vs. 2014			Three months ended September 30, 2015 vs. 2014		
		Due to variances in			Due to variances in	
(in thousands)	Total	Rates	Volumes [1]	Total	Rates	Volumes [1]
Interest earned on:						
Loans and leases:						
Commercial loans and leases	$ 1,409	$ 43	$ 1,366	$ 497	$ 0	$ 497
Commercial real estate	2,495	366	2,129	878	(22)	900
Construction and land	79	(164)	243	82	3	79
Residential real estate	2,264	12	2,252	857	(26)	883
Consumer	134	(0)	134	39	(1)	40
Loans held for sale	758	13	745	276	4	272
Taxable securities	93	15	78	40	1	39
Federal funds sold	13	9	4	7	3	4
Total interest income	7,245	294	6,951	2,676	(38)	2,714
Interest paid on:						
Savings deposits	18	(8)	26	9	(2)	11
Checking plus interest deposits	12	(9)	21	5	(3)	8
Money market accounts	183	17	166	53	(17)	70
Time deposits	168	(120)	288	66	(46)	112
Short-term borrowings	14	(5)	19	15	5	10
Long-term borrowing	26	24	2	12	11	1
Total interest expense	421	(101)	522	160	(52)	212
Net interest earned	$ 6,824	$ 395	$ 6,429	$ 2,516	$ 14	$ 2,502

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

Comparison of Results of Operations

A comparison between the nine months ended September 30, 2015 and September 30, 2014 is presented below.

General

Net income available to common shareholders decreased $584 thousand, or 51.0%, to $561 thousand for the nine months ended September 30, 2015 compared to $1.1 million for the nine months ended September 30, 2014. This decrease was largely due to the approximately $3.3 million in merger and restructuring expenses included in noninterest expenses for the nine months ended September 30, 2015, compared to $82 thousand during the same period of 2014. These non-recurring expenses were related to the acquisitions of both Patapsco Bancorp that closed on August 28, 2015 and NBRS that closed on October 17, 2014. Total revenues (net interest income plus non-interest income) increased $11.0 million or 57.0% to $30.3 million for the first nine months of 2015 from $19.3 million for the same period in 2014. Much of this revenue growth is attributable to our continued strategic and organic growth initiatives. These revenue sources were only minimally influenced by the Patapsco Bancorp acquisition. Because certain components of the merger and restructuring expenses are not deductible for tax purposes, our effective tax rate of 53% for the nine month period in 2015 was much higher than the statutory tax rates.

Interest Income

Interest income increased $7.2 million, or 44.9%, to $23.4 million for the nine months ended September 30, 2015 compared to $16.2 million for the same period in 2014. This increase was due to a $7.1 million or 44.5% increase in interest income on loans and leases, which includes $1.3 million in interest on mortgage loans held for sale. The increase in loan and lease interest income was due primarily to a nearly $168 million or 39.8% increase in the average balance of the loan portfolio during the nine months ended September 30, 2015 compared to the nine months ended September 30, 2014. In addition to the growth in our portfolio of loans, an increase of $27.7 million or over 132% in the average balance of loans held for sale and an increase of $17.1 million or 76.6% in our average securities portfolio aided in the increase in interest income. Further improving interest income, average yields on interest-bearing assets increased for the nine months ended September 30, 2015 compared to the same period of 2014. Loans and leases yield increased to 4.96% from 4.91%, loans held for sale yield increased to 3.59% from 3.51% and the yield on investments securities increased to 0.61% from 0.52% during the nine months ended September 30, 2015 compared to the same period in 2014

Interest Expense

Interest expense increased $421 thousand, or 24.3%, to $2.2 million for the nine months ended September 30, 2015, compared to $1.7 million for the same period in 2014. While average interest bearing deposits grew $134.1 million or 42.8% for the first nine months of 2015 compared to the first nine months of 2014, total interest expense on deposits only rose 25.7% as the average rates paid on deposits decreased from 0.63% to 0.56% when comparing the two periods, primarily as a result of a continuing shift in the composition of our deposits towards lower cost deposit products including noninterest-bearing deposits, the average balance of which grew $47.6 million on average when comparing the nine months ended September 30, 2015 to the same period of the prior year. In addition, interest expense increased $40 thousand as a result of a $9.7 million increase in average balance of borrowings, yet the interest rate on these borrowings remained constant at 0.56%.

Net Interest Income

Net interest income is our largest source of operating revenue. Net interest income is affected by various factors including changes in interest rates and the composition of interest-earning assets and interest-bearing liabilities and maturities. Net interest income is determined by the interest rate spread (i.e., the difference between the yields earned on interest-earning assets and the rates paid on interest-bearing liabilities) and the relative amounts of interest-earning assets and interest-bearing liabilities. Net interest income increased $6.8 million, or 47.3%, during the nine months ended September 30, 2015 compared to the nine months ended September 30, 2014. As noted above, the increase in net interest income was primarily due to an increase in interest income of $7.2 million, reduced by an increase of $421 thousand in interest expense.

Provision for Credit Losses

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

Based on management's evaluation of the above factors, we had a provision for credit losses of $1.0 million for the nine months ended September 30, 2015 compared to $2.6 million for the same period in 2014, a decrease of $1.6 million. The substantial provision for credit losses during the 2014 period resulted primarily from one large commercial customer that closed its business during the third quarter of 2014 and did not fulfill its commitments under existing contracts. The provision for the 2015 period reflects general provisions that are required given our continued growth in the size of the loan portfolio, as well as any specific provisions required on loans that are individually evaluated and deemed to be impaired.

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

Noninterest Income

Noninterest income was $9.0 million for the nine months ended September 30, 2015 compared to $4.9 million for the nine months ended September 30, 2014, a $4.2 million or 86.2% increase. The largest increase was generated from mortgage banking activities. Due to higher loan origination volumes, realized and unrealized gains from these activities increased from $2.9 million in the first nine months of 2014 to $5.4 million in the first nine months of 2015. Included is the effect of the fair value method for mortgage loans held for sale which accelerated mortgage related revenues $71 thousand for the period ended September 30, 2015 compared to $931 thousand for the same period last year. Loan fee income is derived from mortgage banking processing and underwriting as well as other portfolio loan fees. Noninterest income from these activities increased $1.1 million to $2.1 million for the first nine months of 2015 from $1.0 million for the first nine months of 2014. Service charges on deposit accounts, which consist of account activity fees and other traditional banking fees, increased 39.2% to $592 thousand for the nine months ended September 30, 2015 from $425 thousand for the same period in 2014 due mostly to the growth in deposit balances and our customer base as well as the retail-oriented deposit mix acquired with the 2014 NBRS transaction. Other operating income, which consists mainly of non-depository account fees such as wire, merchant card and ATM services, increased $335 thousand during the nine months ended September 30, 2015 compared to the same period of 2014 due to the same factors that increased service charges income.

Our acquisition of Patapsco Bancorp did not have a material impact on non-interest income during the nine months ended September 30, 2015 given that the Merger closed at the end of August.

Noninterest Expenses

Noninterest expenses increased $13.1 million or 88.3%, to $27.9 million for the nine months ended September 30, 2015 from $14.8 million for the nine months ended September 30, 2014. Merger and restructuring costs associated with the Patapsco Bancorp acquisition as well as system integration costs relating to the late 2014 NBRS Acquisition were $3.3 million for the first nine months of 2015, compared to less than $100 thousand for the same period of 2014. For the Patapsco Bancorp acquisition, these costs represented legal and investment banking fees, as well as compensation costs for severance and other payments provided for in employment agreements. We expect to incur an estimated $600 thousand to $800 thousand in systems conversion costs for Patapsco Bancorp in the fourth quarter of 2015. In addition to the Patapsco Bancorp-related costs, we also incurred data processing and conversion-related expenses as we integrated the former NBRS data platform into our systems in April of 2015.

Compensation and benefits expenses grew by $4.0 million or 47.1% when comparing the first nine months of 2015 to the same period in 2014. This increase resulted primarily from the increase in the number of staff, including staff at new locations we operate, as we continued to expand our markets further into the Greater Baltimore market. As we have grown our balance sheet and geographic footprint, we have also increased our business development, customer service and infrastructure staffing to ensure appropriate support levels, risk oversight, information technology platforms, and human resource initiatives. Occupancy related costs increased by $1.3 million or 81.9%, primarily as the result of the previously discussed expansion resulting from both organic and acquired growth. We have altered the mix of owned versus leased locations to better manage this expense component and will continue to evaluate facility and branch utilization, efficiencies and opportunities. Marketing and business development expenses increased $973 thousand, loan production expense increased $830 thousand, and other operating expense increased $1.2 million during the 2015 period compared to the prior year period. These increases pertained to expanding markets, increases in loan-related costs associated with the additional volume in processing mortgage requests, and a variety of general expenses such as phone and data lines, print materials and supplies that have increased to support our expanding infrastructure. Additionally, we recorded a valuation write-down of $736 thousand in the third quarter of 2015 related to OREO properties that we currently hold, in comparison to no valuation adjustments recorded in the same period of 2014.

Net Income Available to Common Shareholders

Net income available to common shareholders during the nine months ended September 30, 2015 decreased $584 thousand or 51.0% to $561 thousand compared to $1.1 million during the nine months ended September 30, 2014. The decrease in net income available to common shareholders is attributable to the increase in non-interest expenses. As discussed above, most of the increase in noninterest expenses is directly attributable to the growth that we have experienced in the last twelve months, including non-recurring merger and restructuring costs and increases in compensation and benefits and occupancy expenses. Earnings per common share for the first nine months of 2015 were $0.09 per share compared to $0.28 for the same period of 2014. The non-recurring expenses, referred to above, and the increase in the average number of shares outstanding compared to the same period in 2014 due to the previously-discussed private placement and the Patapsco Bancorp acquisition, had a negative impact on reported earnings per share. The majority of these non-recurring costs were recorded in the third quarter but we anticipate that as systems conversions are scheduled for the fourth quarter of 2015, the remainder of the non-recurring charges attributable to the Patapsco Bancorp merger will impact fourth quarter earnings. Excluding these non-recurring items from core operating performance, net income, earnings per share and return measures compare favorably to the prior year.

A comparison between the three months ended September 30, 2015 and September 30, 2014 is presented below.

General

Net income (loss) available to common shareholders decreased $1.0 million to a net loss of $817 thousand for the three months ended September 30, 2015 compared to net income of $204 thousand for the three months ended September 30, 2014. This resulted in a loss per share of $0.13 for the third quarter of 2015 compared to earnings per share of $.05 in the same period of 2014. The primary reason for the decrease in earnings was a $6.6 million increase in noninterest expenses.

Interest Income

Interest income increased $2.7 million, or 46.0%, to $8.5 million for the three months ended September 30, 2015 compared to $5.8 million for the same period of 2014. The increase was primarily due to a $2.6 million, or 45.5%, increase in interest income and fees on loans and loans held for sale. This increase was due to a $230.2 million or 48.7% increase in the average balance of loans and loans held for sale compared to the three months ended September 30, 2014. Partially offsetting this increase was a slight decline of nine basis points in the average yield on loans and leases, which decreased from $4.95% to 4.86%. In addition, interest and dividends on securities increased $40 thousand or 142.9% during the third quarter of 2015 compared to the same period last year primarily as a result of a $26.6 million increase in the average balance of investment securities quarter over quarter. Interest income on federal funds sold for the three months ended September 30, 2015 increased $7 thousand or 77.8% over the same period in 2014 as a result of a seven basis point increase in the yield and a 31.4% increase in the average balance.

Interest Expense

Interest expense increased $160 thousand, or 24.7%, to $808 thousand for the three months ended September 30, 2015, compared to $648 thousand for the same period of 2014, primarily as a result of an increase in the average balance of our interest-bearing deposits, primarily time deposits, partially offset by a decrease in the rate paid on interest-bearing deposits, primarily time deposits. Our average balance of interest-bearing deposits increased $159.5 million, or 48.6%, during the three months ended September 30, 2015 compared to the same period of 2014, while the average rate paid on interest-bearing deposits decreased 12 basis points to 0.56% from 0.68% over the same period. The average balance of our time deposits increased $56.2 million or 33.8% and the rate paid on time deposits decreased ten basis points, to 0.79%, during the three months ended September 30, 2015 compared to the same period of 2014. In addition, a $13.2 million increase in the average balance of our borrowings and a 5 basis point increase in the average rate paid on such borrowings also contributed to the increase in interest expense.

Net Interest Income

Net interest income increased $2.5 million, or 48.7%, during the three months ended September 30, 2015 compared to the three months ended September 30, 2014. As noted above, the increase in net interest income was due to a $2.7 million increase in interest income partially offset by a $160 thousand increase in interest expense.

Provision for Credit Losses

Based on management's evaluation, we had a provision for credit losses of $230 thousand for the three months ended September 30, 2015 compared to $2.1 million for the same period in 2014. The provision for the third quarter of 2014 was primarily due to a single credit, as discussed above. The provision for both periods reflects a general provision required given continued growth in the size of our loan portfolio, as well as any specific provisions required on loans that are individually evaluated and deemed to be impaired.

Noninterest Income

Noninterest income was $3.3 million for the three months ended September 30, 2015 compared to $2.2 million for the three months ended September 30, 2014, a $1.1 million or 49.7% increase. This increase was primarily due to the $1.9 million of income generated from the mortgage banking activities during the third quarter of 2015, an increase of $522 thousand or 37.6% over the same period last year. Additionally, fees collected on these mortgage activities and in our portfolio loan processing increased to $848 thousand from $485 thousand when comparing third quarter 2015 to third quarter 2014. Other operating income increased $116 thousand quarter over quarter due to higher transaction fees given our larger deposit base.

Noninterest Expenses

Noninterest expenses increased $6.6 million or 133.8%, during the three months ended September 30, 2015 compared to the three months ended September 30, 2014. Similar to the year to date results discussed above, the third quarter 2015 results were dramatically impacted by one-time non-recurring charges. These one-time non-recurring costs amounted to $2.2 million for the third quarter of 2015 compared to $82 thousand for the same period of 2014. As noted above these charges stem from activities related to the acquisitions of NBRS and Patapsco Bancorp mainly related to compensation costs, professional services and data processing conversions. Expanding regional markets and infrastructure related to growth initiatives were the greatest factors impacting the increase in other categories of noninterest expenses. Compensation and employee benefits increased $1.9 million, occupancy and equipment expenses increased $442 thousand, and marketing and business development increased $386 thousand. The $401 thousand increase in other operating expense for the three months ended September 30, 2015 compared to the same period of 2014 related to general increases in supplies, communication systems and postage and related expenses needed to support our expanded operations. We recorded an OREO valuation expense of $736 thousand during the quarter ended September 30, 2015 as updated appraisals came in with values less than the carrying values. No such valuation adjustments were necessary during the quarter ended September 30, 2014.

Nonperforming and Problem Assets

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

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

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

(in thousands)	September 30, 2015	December 31, 2014
Non-accrual loans:		
Real estate loans:		
Construction and land	$ 810	$ 1,144
Residential - first lien	744	719
Residential - junior lien	74	57
Commercial	1,062	-
Commercial and leases	2,875	2,015
Consumer	151	92
Total non-accrual loans	5,716	4,027
Accruing troubled debt restructure loans:		
Real estate loans:		
Residential - first lien	301	-
Commercial	2,083	-
Commercial and leases	-	226
Total accruing troubled debt restructure loans	2,384	226
Total non-performing loans	8,100	4,253
Other real estate owned:		
Land	338	595
Residential - first lien	21	-

Commercial		1,405			1,877	
Total other real estate owned		1,764			2,472	
Total non-performing assets	$	9,864		$	6,725	
Ratios:						
Non-performing loans to total gross loans		1.07	%		0.77	%
Non-performing assets to total assets		1.07	%		0.97	%

Included in total non-accrual loans at September 30, 2015 was one trouble debt restructured loan in the amount of $594 thousand that was not performing in accordance with the modified terms, and the accrual of interest has ceased. There were two troubled debt restructured loans totaling $2.4 million currently performing in accordance with their modified terms. There were 11 loans 90 days or more past due and still accruing interest at September 30, 2015 - one land loan of $28 thousand, two commercial real estate credit totaling $236 thousand, six commercial loans totaling $4.9 million and two consumer loans totaling $25 thousand.

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

Nonperforming assets amounted to $9.9 million, or 1.07% of total assets, at September 30, 2015 compared to $6.7 million or 0.77% of total assets at December 31, 2014. Total nonperforming assets have increased $3.1 million during 2015, with one property reflected in OREO as a result of the Patapsco Bancorp acquisition, no current properties sold and $736 thousand in additional valuation adjustments required on current assets during the nine months ended September 30, 2015. The increase in non-accrual loans was impacted by the addition of 12 credit-impaired loans acquired in the Patapsco Bancorp acquisition and partially offsetting this increase were several non-accrual loan principal payments received from the borrowers during the period and applied to reduce the non-accrual balance.

The composition of our nonperforming loans at September 30, 2015 is further described below:

Non-Accrual Loans:

- One construction and land loan for $810 thousand with a specific reserve.
- Six commercial non-owner occupied real estate loans totaling $824 thousand.
- Three commercial owner occupied real estate loans totaling $238 thousand.
- Seven residential first lien loans totaling $744 thousand.
- One residential junior lien in the amount of $74 thousand with a specific reserve.
- Twenty five commercial loans totaling $2.9 million, two with Small Business Administration (“SBA”) guarantees and three that include a specific reserve.
- One consumer loan in the amount of $151 thousand

Trouble Debt Restructured Loans:

- One residential first lien loan for $301 thousand.
- One non-owner occupied commercial real estate loan for $2.1 million.

Allowance for Credit Losses

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

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

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

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

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

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

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

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

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

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

Generally, we underwrite commercial loans based on cash flow and business history and receive personal guarantees from the borrowers where appropriate. We generally underwrite commercial real estate loans and residential real estate loans at a loan-to-value ratio of 85% or less at origination. Accordingly, in the event that a loan becomes past due and, randomly with respect to performing loans, we will conduct visual inspections of collateral properties and/or review publicly available information, such as online databases, to ascertain property values. We will also obtain formal appraisals on a regular basis even if we are not considering liquidation of the property to repay a loan. It is our practice to obtain updated appraisals if there is a material change in market conditions or if we become aware of new or additional facts that indicate a potential material reduction in the value of any individual property collateral.

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

At September 30, 2015 and December 31, 2014, impaired loans amounted to $9.0 million and $7.2 million, respectively. The amount of impaired loans requiring specific reserves totaled $1.3 million and $1.1 million at September 30, 2015 and December 31, 2014, respectively. The amount of impaired loans with no specific valuation allowance totaled $7.7 million and $6.1 million, respectively, at such dates.

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

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

The following table sets forth activity in our allowance for credit losses for the indicated periods:

(in thousands)	Nine months ended September 30, 2015			Twelve months ended December 31, 2014		
Balance at beginning of period	$	3,602		$	2,506	
Charge-offs:						
Real estate loans						
Commercial non-owner occupied		-			(160	)
Commercial loans and leases		(640	)		(2,054	)
Consumer loans		(4	)		(5	)
		(644	)		(2,219	)
Recoveries:						
Real estate loans						
Residential first lien		3			1	
Residential junior lien		1			-	
Commercial non-owner occupied loans		319			4	
Commercial loans and leases		18			55	
Commercial loans and leases		3			-	
		344			60	
Net charge-offs		(300	)		(2,159	)
Provision for credit losses		1,015			3,255	
Balance at end of period	$	4,317		$	3,602	
Net charge-offs to average loans and leases		0.051	%		0.479	%

Allocation of Allowance for Credit Losses

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

(dollars in thousands)	September 30, 2015 Amount	Percent [1]	December 31, 2014 Amount	Percent [1]
Real estate				
Construction and land loans	$ 476	9.6 %	$ 174	11.6 %
Residential first lien loans	352	24.3	272	16.0
Residential junior lien loans	41	3.5	55	3.5
Commercial owner occupied laons	279	19.5	160	20.4
Commercial non-owner occupied loans	681	20.6	562	22.4
Commercial loans and leases	2,471	21.9	2,366	25.2
Consumer loans	17	0.6	13	0.9
Total	$ 4,317	100.0 %	$ 3,602	100.0 %

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

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Liquidity and Capital Resources

Liquidity is the ability to meet current and future financial obligations. Our primary sources of funds consist of deposit inflows, loan repayments, advances from the FHLB, principal repayments and the sale of securities available for sale. While maturities and scheduled amortization of loans and securities are predictable sources of funds, deposit flows and loan prepayments are greatly influenced by general interest rates, economic conditions and competition. Our Asset Liability Committee is responsible for establishing and monitoring our liquidity targets and strategies in order to ensure that sufficient liquidity exists for meeting the borrowing needs and deposit withdrawals of our customers as well as unanticipated contingencies. We believe that we have enough sources of liquidity to satisfy our short- and long-term liquidity needs as of September 30, 2015 and December 31, 2014. We regularly monitor and adjust our investments in liquid assets based upon our assessment of:

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

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

Our most liquid assets are cash and cash equivalents. The level of these assets is dependent on our operating, financing, lending and investing activities during any given period. At September 30, 2015 and December 31, 2014, cash and cash equivalents totaled $18.3 million and $24.5 million, respectively.

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

At September 30, 2015 and December 31, 2014, we had $109.1 million and $115.3 million, respectively, in loan commitments outstanding, including commitments issued to originate loans of $77.6 million and $64.4 million at September 30, 2015 and December 31, 2014, respectively, and $31.6 million and $50.9 million in unused lines of credit to borrowers at September 30, 2015 and December 31, 2014, respectively. In addition to commitments to originate loans and unused lines of credit we had $8.5 million and $12.4 million in letters of credit at September 30, 2015 and December 31, 2014, respectively. Certificates of deposit due within one year of September 30, 2015 totaled $151.2 million, or 20.4% of total deposits. Should these deposits not remain with us, we may be required to seek other sources of funds, including loan and securities sales, and FHLB advances. Depending on market conditions, we may be required to pay higher rates on our deposits or other borrowings than we currently pay on the certificates of deposit. We believe, however, based on historical experience and current market interest rates that we will retain upon maturity a large portion of our certificates of deposit with maturities of one year or less.

Our primary investing activity is originating loans. During the nine months ended September 30, 2015 cash was utilized to increase our portfolio of loans by $48.3 million and increase our loans held for sale portfolio by $21.5 million. For the nine month period ended September 30, 2014, these amounts were $43.6 million and $35.4 million, respectively. During the first nine months of 2015 we utilized cash to purchase additional securities totaling $13.9 million while receiving $42.5 million as a result of securities maturing. For the same period in 2014 we used cash to purchase $32.0 million in securities and we received $33.6 million in security maturities.

Financing activities consist primarily of activity in deposit accounts and FHLB advances. We experienced a net increase in deposits (exclusive of acquired deposits) of $13.4 million during the nine months ended September 30, 2015. Deposit flows are affected by the overall level of interest rates, the interest rates and products offered by us and our local competitors, and by other factors.

Liquidity management is both a daily and long-term function of business management. If we require funds beyond our ability to generate them internally, borrowing agreements exist with the FHLB, which provide an additional source of funds. FHLB advances were $55.5 million at September 30, 2015 compared to $43.0 million at December 31, 2014. At September 30, 2015, we had the ability to borrow up to a total of $182.7 million based upon our credit availability at the FHLB, subject to collateral requirements.

The Bank is subject to various regulatory capital requirements, including a risk-based capital measure. The risk-based capital guidelines include both a definition of capital and a framework for calculating risk-weighted assets by assigning balance sheet assets and off-balance sheet items to broad risk categories. At September 30, 2015 and December 31, 2014, the Bank exceeded all regulatory capital requirements. The Bank is considered “well capitalized” under regulatory guidelines.

Commitments, Contingent Liabilities, and Off-Balance Sheet Arrangements

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

Outstanding loan commitments and lines of credit at September 30, 2015 and December 31, 2014 are as follows:

(in thousands)	September 30, 2015	December 31, 201
Unfunded loan commitments	$ 77,574	$ 64,375
Unused lines of credit	31,554	50,889
Letters of credit	8,535	12,397

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

The credit risk involved in these financial instruments is essentially the same as that involved in extending loan facilities to customers. No amount has been recognized in the statement of financial condition at September 30, 2015 or December 31, 2014 as a liability for credit loss related to these commitments.

Impact of Inflation and Changing Prices

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

Item 3. Quantitative and Qualitative Disclosures about Market Risk

Not applicable

Item 4. Controls and Procedures

As of the end of the period covered by this quarterly report on Form 10-Q Bancorp's Chief Executive Officer and Chief Financial Officer evaluated the effectiveness of Bancorp's disclosure controls and procedures as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act"). Based upon that evaluation, Bancorp's Chief Executive Officer and Chief Financial Officer concluded that Bancorp's disclosure controls and procedures are effective as of September 30, 2015. Disclosure controls and procedures are controls and other procedures that are designed to ensure that information required to be disclosed by Bancorp in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms.

In addition, there were no changes in Bancorp's internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) during the quarter ended September 30, 2015, that have materially affected, or are reasonably likely to materially affect Bancorp's internal control over financial reporting.

PART II - Other Information

Item 1. Legal Proceedings

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

Item 1A. Risk Factors

There have been no material changes in the risk factors from those disclosed in our Annual Report on Form 10-K for the year ended December 31, 2014, as filed with the SEC on March 27, 2015.

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

None

Item 3. Defaults upon Senior Securities

None

Item 4. Mine Safety Disclosures

Not applicable

Item 5. Other Information

None

Item 6. Exhibits

31(a)	Certification of Chief Executive Officer pursuant to Rule 13a-14(a) or 15d-14(a) of the Exchange Act pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 - filed herewith
31(b)	Certification of Chief Financial Officer pursuant to Rule 13a-14(a) or 15d-14(a) of the Exchange Act pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 - filed herewith
32	Certifications pursuant to 18 U.S.C. Section 1350, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 – filed herewith
101	Extensible Business Reporting Language ("XBRL") – filed herewith
101.INS	XBRL Instance File

101.SCH	XBRL Schema File
101.CAL	XBRL Calculation File
101.DEF	XBRL Definition File
101.LAB	XBRL Label File
101.PRE	XBRL Presentation File

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.

	HOWARD BANCORP, INC. (Registrant)
November 13, 2015	/s/ Mary Ann Scully
Date	MARY ANN SCULLY PRESIDENT AND CEO
November 13, 2015	/s/ George C. Coffman
Date	GEORGE C. COFFMAN EVP AND CFO