GLEN BURNIE BANCORP
Form 10-K
March 29, 2013

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

x Annual report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the fiscal year ended December 31, 2012 or

¨ Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the transition period from ______ to ________.

**Commission file number: 0-24047**

**GLEN BURNIE BANCORP**

(Exact name of registrant as specified in its charter)

| | |
|---|---|
| MARYLAND<br>(State or other jurisdiction<br>of incorporation or organization) | 52-1782444<br>(I.R.S. Employer<br>Identification No.) |
| 101 Crain Highway, S.E., Glen Burnie, Maryland<br>(Address of principal executive offices) | 21061<br>(Zip Code) |

Registrant’s telephone number, including area code (410) 766-3300

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

| Title of Class | Name of Each Exchange on Which Registered |
|---|---|
| None | None |

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

Title of Class

Common Stock, $1.00 par value

Common Stock Purchase Rights

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes ¨ No x

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

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes x No ¨

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

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

Large Accelerated Filer ¨ Accelerated Filer ¨ Non-Accelerated Filer ¨ Smaller Reporting Company x

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes ¨ No x

The aggregate market value of the voting stock held by non-affiliates of the registrant as of June 30, 2012 was $22,533,087.

The number of shares of common stock outstanding as of March 29, 2013 was 2,736,978

documents incorporated by reference

To the extent specified, Part III of this Form 10-K incorporates information by reference to the Registrant's definitive proxy statement for its 2013 Annual Meeting of Shareholders (to be filed).

**GLEN BURNIE BANCORP**

2012 ANNUAL REPORT ON FORM 10-K

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**PART I**

**ITEM 1. BUSINESS**

General

Glen Burnie Bancorp (the "Company") is a bank holding company organized in 1990 under the laws of the State of Maryland. The Company owns all the outstanding shares of capital stock of The Bank of Glen Burnie (the "Bank"), a commercial bank organized in 1949 under the laws of the State of Maryland, serving northern Anne Arundel County and surrounding areas from its main office and branch in Glen Burnie, Maryland and branch offices in Odenton, Riviera Beach, Crownsville, Severn (two locations), Linthicum and Severna Park, Maryland. The Bank also maintains a remote Automated Teller Machine ("ATM") location in Pasadena, Maryland. The Bank maintains a website at www.thebankofglenburnie.com. The Bank is the oldest independent commercial bank in Anne Arundel County. The Bank is engaged in the commercial and retail banking business as authorized by the banking statutes of the State of Maryland, including the acceptance of demand and time deposits, and the origination of loans to individuals, associations, partnerships and corporations. The Bank's real estate financing consists of residential first and second mortgage loans, home equity lines of credit and commercial mortgage loans. Commercial lending consists of both secured and unsecured loans. The Bank also originates automobile loans through arrangements with local automobile dealers. The Bank's deposits are insured up to applicable limits by the Federal Deposit Insurance Corporation ("FDIC").

The Company's principal executive office is located at 101 Crain Highway, S.E., Glen Burnie, Maryland 21061. Its telephone number at such office is (410) 766-3300.

Information on the Company and its subsidiary Bank may be obtained from the Company's website www.thebankofglenburnie.com. Copies of the Company's annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and all amendments thereto are available free of charge on the website as soon as they are filed with the SEC through a link to the SEC's EDGAR reporting system. Simply select the "Investor Relations" menu item, then click on the "All SEC Filings" or "Insider Transactions" link.

Economic and Credit Turmoil from 2009 to 2012

The turmoil and economic downturn, which began in, and has continued since 2009, has engulfed the United States and world financial services industry. The ensuing overall consequences to numerous industries and the U.S. economy is well known and discussed daily in the media. The Bank and, as a result, the Company, have not been immune to the impact of these difficult economic times. While, due to conservative lending decisions, the Bank has no exposure to the credit issues affecting the sub-prime residential mortgage market, the economic slowdown resulted in the necessity of our contributing $2,442,976 to the provision for loan losses in 2009, $1,050,000 in 2010, $663,000 for 2011 and $250,000 for 2012, primarily due to valuation issues in our commercial mortgage portfolio and continuing delinquency in our indirect automobile portfolio combined with adjustments we made to the risk factors in our calculation of required loan loss reserves. In addition, the economic downturn also resulted in an FDIC insurance premium assessment rising from $35,544 in 2008 to $549,716 in 2009, a more than 1,400% increase. For 2010 and 2011, our FDIC assessments were $464,585 and $572,425 respectively. The increases in FDIC insurance premium assessments during the 2009-2011 period were due to FDIC reserves becoming depleted as a result of the economic crisis. For 2012, our FDIC assessment declined to $39,622 reflecting the improved financial condition of the FDIC reserves. Despite the economic downturn and these events, which are unusual for us in any year, we realized net income of $1,262,462, $2,064,785, $2,993,093 and $2,665,080 for 2009, 2010, 2011 and 2012, respectively. The Bank and others believe that the economy showed some signs of improvement beginning in 2010, although economic weakness continues in the real estate and other markets. We remain well capitalized and did not need to apply for any funding from the U.S. Department of Treasury’s Troubled Asset Relief Program (TARP). During the past four years, we continued to lend money and, we believe, meet the needs of our customers and neighbors through a difficult time. We believe we are a sound, conservatively run financial institution that has been profitable each year during this turmoil despite the deterioration in the economic environment and the outside forces that have affected us these past four years.

Market Area

The Bank considers its principal market area for lending and deposit products to consist of Anne Arundel County, Maryland. Anne Arundel County includes mature suburbs of the City of Baltimore, which in recent years have experienced modest population growth and are characterized by an aging population. Management believes that the majority of the working population in its market area either commutes to Baltimore or is employed at businesses located at or around the nearby Baltimore Washington International Airport. Anne Arundel County is generally considered to have more affordable housing than other suburban Baltimore areas and attracts younger persons and minorities on this basis. This inflow, however, has not been sufficient to affect current population trends.

Lending Activities

The Bank offers a full range of consumer and commercial loans. The Bank's lending activities include residential and commercial real estate loans, construction loans, land acquisition and development loans, commercial loans and consumer installment lending including indirect automobile lending. Substantially all of the Bank's loan customers are residents of Anne Arundel County and surrounding areas of Central Maryland. The Bank solicits loan applications for commercial loans from small to medium sized businesses located in its market area. The Company believes that this is a market in which a relatively small community bank, like the Bank, has a competitive advantage in personal service and flexibility. The Bank's consumer lending currently consists primarily of indirect automobile loans originated through arrangements with local dealers.

The Company's total loan portfolio decreased in 2010 and increased during the 2012, 2011, 2009, and 2008 fiscal years. In 2012, the increase in the loan portfolio was primarily due to increases in indirect loans, commercial and industrial mortgages, home equity and purchase money mortgages, partially offset by decreases in refinance mortgage loans, construction loans for commercial and industrial loans and demand secured business loans. In 2012, mortgage participations purchased also decreased. In 2011, the increase in the loan portfolio was primarily due to increases in indirect loans, residential mortgages, and installment loans, partially offset by a decrease in commercial mortgages. In 2011, mortgage participations purchased decreased but so did mortgage participations sold. In 2010, the decrease in the loan portfolio was primarily due to decreases in indirect loans, commercial mortgages, secured demand commercial loans and commercial loans, partially offset by increases in refinance and purchase money mortgage loans and land development loans. Mortgage participations purchased decreased but so did mortgage participations sold. In 2009, the increase in the loan portfolio was primarily due to increases in refinanced mortgage loans, purchase money mortgage loans, home equity and commercial mortgages, partially offset by a decrease in indirect loans and mortgage participations purchased. In 2008, the increase in the loan portfolio was primarily due to increases in refinanced mortgage loans, commercial and residential construction loans and mortgage participations purchased, partially offset by additional mortgage participations sold and a decrease in indirect loans.

The following table provides information on the composition of the loan portfolio at the indicated dates.

| | At December 31, | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | 2012 | | 2011 | | 2010 | | 2009 | | 2008 | |
| (Dollars in Thousands) | $ | % | $ | % | $ | % | $ | % | $ | |
| Mortgage: | | | | | | | | | | |
| Residential | $107,729 | 42.41 % | $107,664 | 45.29 % | $102,199 | 43.62 % | $95,683 | 39.81 % | $87,708 | |
| Commercial | 71,381 | 28.10 | 67,656 | 28.46 | 72,670 | 31.02 | 79,845 | 33.23 | 76,153 | |
| Construction and land development | 3,915 | 1.54 | 5,092 | 2.14 | 5,363 | 2.29 | 1,743 | 0.73 | 6,590 | |
| Consumer: | | | | | | | | | | |
| Installment | 18,504 | 7.28 | 18,048 | 7.59 | 16,407 | 7.00 | 15,965 | 6.64 | 16,451 | |
| Credit card | 165 | 0.06 | 163 | 0.07 | 168 | 0.07 | 166 | 0.07 | 173 | |
| Indirect automobile | 47,427 | 18.67 | 31,907 | 13.42 | 30,286 | 12.93 | 37,092 | 15.44 | 43,970 | |
| Commercial | 4,901 | 1.94 | 7,193 | 3.03 | 7,193 | 3.07 | 9,801 | 4.08 | 6,974 | |
| Gross loans | 254,022 | 100.00% | 237,723 | 100.00% | 234,286 | 100.00% | 240,295 | 100.00% | 238,019 | |
| Unearned income on loans | (1,083 ) | | (1,058 ) | | (1,035 ) | | (839 ) | | (864 ) | |
| Gross loans net of unearned income | 252,939 | | 236,665 | | 233,251 | | 239,456 | | 237,155 | |
| Allowance for credit losses | (3,308 ) | | (3,931 ) | | (3,400 ) | | (3,573 ) | | (2,022 ) | |
| Loans, net | $249,631 | | $232,734 | | $229,851 | | $235,883 | | $235,133 | |

The following table sets forth the maturities for various categories of the loan portfolio at December 31, 2012. Demand loans and loans which have no stated maturity, are treated as due in one year or less. At December 31, 2012, the Bank had $27,358,852 in loans due after one year with variable rates and $198,596,212 in such loans with fixed rates.

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| | Due Within One Year | Due Over One To Five Years | Due Over Five Years | Total |
|---|---|---|---|---|
| | (In Thousands) | | | |
| Real Estate - mortgage: | | | | |
| Residential | $10,409 | $ 4,230 | $93,090 | $107,729 |
| Commercial | 12,228 | 22,481 | 36,672 | 71,381 |
| Construction and land development | 1,175 | 1,078 | 1,662 | 3,915 |
| Installment | 339 | 8,925 | 9,240 | 18,504 |
| Credit Card | 3 | 43 | 119 | 165 |
| Indirect automobile | 728 | 29,518 | 17,181 | 47,427 |
| Commercial | 3,185 | - | 1,716 | 4,901 |
| | $28,067 | $ 66,275 | $159,680 | $254,022 |

**Real Estate Lending.** The Bank offers long-term mortgage financing for residential and commercial real estate as well as shorter term construction and land development loans. Residential mortgage and residential construction loans are originated with fixed rates, while commercial mortgages may be originated on either a fixed or variable rate basis. Commercial construction loans may be originated on either a fixed or a variable rate basis. Substantially all of the Bank's real estate loans are secured by properties in Anne Arundel County, Maryland**.** Under the Bank's loan policies, the maximum permissible loan-to-value ratio for owner-occupied residential mortgages is 80% of the lesser of the purchase price or appraised value. For residential investment properties, the maximum loan-to-value ratio is 80%. The maximum permissible loan-to-value ratio for residential and residential construction loans is 80%. The maximum loan-to-value ratio for permanent commercial mortgages is 75%. The maximum loan-to-value ratio for land development loans is 70% and for unimproved land is 65%. The Bank also offers home equity loans secured by the borrower's primary residence, provided that the aggregate indebtedness on the property does not exceed 80% of its value. Because mortgage lending decisions are based on conservative lending policies, the Company has no exposure to the credit issues affecting the sub-prime residential mortgage market.

**Commercial Lending.** The Bank's commercial loan portfolio consists of demand, installment and time loans for commercial purposes. The Bank's business demand, installment and time lending includes various working capital loans, equipment, vehicles, lines of credit and letters of credit for commercial customers. Demand loans require the payment of interest until called, while installment loans require a monthly payment of principal and interest, and time loans require at maturity a single payment of principal and interest due monthly. Such loans may be made on a secured or an unsecured basis. All such loans are underwritten on the basis of the borrower's creditworthiness rather than the value of the collateral.

**Installment Lending.** The Bank makes consumer and commercial installment loans for the purchase of automobiles, boats, other consumer durable goods, capital goods and equipment. Such loans provide for repayment in regular installments and are secured by the goods financed. Also included in installment loans are overdraft loans and other credit repayable in installments. As of December 31, 2012, approximately 52.91% of the installment loans in the Bank's portfolio (other than indirect automobile lending) had been originated for commercial purposes and 47.09% had been originated for consumer purposes.

**Indirect Automobile Lending.** The Bank commenced its indirect automobile lending program in January 1998. The Bank finances new automobiles for terms of up to 72 months and used automobiles for terms of up to 72 months. The Bank will lend a maximum of 110% of invoice on new vehicles. On used vehicles, the Bank will not lend more than 120% of the clean wholesale as published in a nationally recognized used vehicle pricing guide. The Bank requires all borrowers to obtain vendor's single interest coverage protecting the Bank against loss in the case a borrower's automobile insurance lapses. The Bank originates indirect loans through a network of approximately 60 dealers which are primarily new car dealers located in Anne Arundel County and the surrounding counties. Participating dealers take loan applications from their customers and transmit them to the Bank for approval.

**Other Loans.** The Bank offers overdraft protection lines of credit, tied to checking accounts, as a convenience to qualified customers.

Although the risk of non-payment for any reason exists with respect to all loans, certain other specific risks are associated with each type of loan. The primary risks associated with commercial loans, including commercial real estate loans, are the quality of the borrower's management and a number of economic and other factors which induce business failures and depreciate the value of business assets pledged to secure the loan, including competition, insufficient capital, product obsolescence, changes in the borrowers' cost, environmental hazards, weather, changes in laws and regulations and general changes in the marketplace. Primary risks associated with residential real estate loans include fluctuating land and property values and rising interest rates with respect to fixed-rate, long-term loans. Residential construction lending exposes the Company to risks related to builder performance. Consumer loans, including indirect automobile loans, are affected primarily by domestic economic instability and a variety of factors that may lead to the borrower's unemployment, including deteriorating economic conditions in one or more segments of a local or broader economy. Because the Bank deals with borrowers through an intermediary on indirect automobile loans, this form of lending potentially carries greater risks of defects in the application process for which claims may be made against the Bank. Indirect automobile lending may also involve the Bank in consumer disputes under state "lemon" or other laws. The Bank seeks to control these risks by following strict underwriting and documentation guidelines. In addition, dealerships are contractually obligated to indemnify the Bank for such losses for a limited period of time.

The Bank's lending activities are conducted pursuant to written policies approved by the Board of Directors intended to ensure proper management of credit risk. Loans are subject to a well defined credit process that includes credit evaluation of borrowers, establishment of lending limits and application of lending procedures, including the holding of adequate collateral and the maintenance of compensating balances, as well as procedures for on-going identification and management of credit deterioration. Regular portfolio reviews are performed by the Bank's Senior Credit Officer to identify potential underperforming loans and other credit facilities, estimate loss exposure and to ascertain compliance with the Bank's policies. On a quarterly basis, the Bank's Internal Auditor performs an independent loan review in accordance with the Bank's loan review policy. For significant problem loans, management review consists of evaluation of the financial strengths of the borrower and any guarantor, the related collateral, and the effects of economic conditions.

The Bank's loan approval policy provides for various levels of individual lending authority. The maximum aggregate lending authority granted by the Bank to any one Lending Officer is $750,000. A combination of approvals from certain officers may be used to lend up to an aggregate of $1,000,000. The Bank's Executive Committee is authorized to approve loans up to $3.0 million. Larger loans must be approved by the full Board of Directors.

Under Maryland law, the maximum amount which the Bank is permitted to lend to any one borrower and their related interests may generally not exceed 10% of the Bank's unimpaired capital and surplus, which is defined to include the Bank's capital, surplus, retained earnings and 50% of its allowance for possible loan losses. Under this authority, the Bank would have been permitted to lend up to $3.24 million to any one borrower at December 31, 2012. By interpretive ruling of the Commissioner of Financial Regulation, Maryland banks have the option of lending up to the amount that would be permissible for a national bank which is generally 15% of unimpaired capital and surplus (defined to include a bank's total capital for regulatory capital purposes plus any loan loss allowances not included in regulatory capital). Under this formula, the Bank was permitted to lend up to $4.62 million to any one borrower from and after January 1, 2012. Based on the September 30, 2012 Call Report, the Bank's lending limit was increased to

$5.15 million for the remainder of the year. At December 31, 2012, the largest amount outstanding to any one borrower and its related interests was $4,929,000. From and after January 1, 2013, the Bank is permitted to lend up to $5.11 million to any one borrower.

Non-Performing Loans

It will be the policy of The Bank of Glen Burnie that any loan that is ninety (90) days or more delinquent in the payment of principal and/or interest be placed into non-accrual status. Notwithstanding the aforementioned, if it is determined that there appears to be a substantial amount of risk of not collecting all of the agreed upon interest that would normally accrue to a loan, the loan should be placed into Non-Accrual status even if the determination is made prior to ninety (90) days delinquent. A variance to this rule would be if the asset is both well secured and in the process of collection. An asset is "well secured" if it is secured by (1) by collateral in the form of liens on or pledges of real or personal property, including securities that have a realizable value sufficient to discharge the debt (including accrued interest) in full, or (2) by the guarantee of a financially responsible party. An asset is "in the process of collection" if collection of the asset is proceeding in due course either (1) through legal action, including judgment enforcement procedures, or (2) in appropriate circumstances, through collection efforts not involving legal action which are reasonably expected to result in prepayment of the debt or in its restoration to a current status in the near future.

The Bank seeks to control delinquencies through diligent collection efforts. For consumer loans, the Bank sends out payment reminders on the seventh and twelfth days after a payment is due. If a consumer loan becomes 15 days past due, the account is transferred to the Bank's collections department, which will contact the borrower by telephone and/or letter before the account becomes 30 days past due. If a consumer loan becomes more than 30 days past due, the Bank will continue its collection efforts and will move to repossession or foreclosure by the 45th day if the Bank has reason to believe that the collateral may be in jeopardy or the borrower has failed to respond to prior communications. The Bank may move to repossess or foreclose in all instances in which a consumer loan becomes more than 60 days delinquent. After repossession of a motor vehicle, the borrower has a 15-day statutory right to redeem the vehicle and is entitled to 10 days' notice before the sale of a repossessed vehicle. The Bank sells the vehicle as promptly as feasible after the expiration of these periods. If the amount realized from the sale of the vehicle is less than the loan amount, the Bank may seek a deficiency judgment against the borrower. The Bank follows similar collection procedures with respect to commercial loans.

While the economy remained weak in 2012, the Bank remained strong and experienced a continued decrease in non-accrual loans as of December 31, 2012. The following table sets forth the amount of the Bank's restructured loans, non-accrual loans and accruing loans 90 days or more past due at the dates indicated:

| | At December 31, | | | | |
|---|---|---|---|---|---|
| | 2012 | 2011 | 2010 | 2009 | 2008 |
| | (Dollars In Thousands) | | | | |
| Restructured Loans | $2,202 | $4,108 | $2,844 | $87 | $- |
| | | | | | |
| Non-accrual loans: | | | | | |
| Real estate – mortgage: | | | | | |
| Residential | $1,109 | $481 | $976 | $215 | $- |
| Commercial | 1,370 | 3,192 | 4,522 | 2,626 | 659 |
| Installment | 237 | 75 | 125 | 176 | 208 |
| Commercial | 1,293 | 1,313 | 1,360 | - | - |
| Total non-accrual loans | 4,009 | 5,061 | 6,983 | 3,017 | 867 |
| | | | | | |
| Accruing loans past due 90 days or more | | | | | |
| Real estate – mortgage: | | | | | |
| Residential | 259 | 19 | - | 8 | 3 |
| Real estate - construction | - | - | - | - | 5 |
| Installment | - | - | - | 1 | 26 |
| Commercial | 1,354 | - | - | 12 | - |
| Total accruing loans past due 90 days or more | 1,613 | 19 | - | 21 | 34 |
| Total non-accrual and past due loans | $5,622 | $5,080 | $6,983 | $3,038 | $901 |
| Non-accrual and past due loans to gross loans | 2.22 % | 2.15 % | 2.99 % | 1.26 % | 0.38 % |
| Allowance for credit losses to non-accrual and past due loans | 58.84% | 77.38% | 48.69% | 117.61% | 224.42% |

For the year ended December 31, 2012, interest of $273,974 would have been accrued on non-accrual loans if such loans had been current in accordance with their original terms. During that period, interest on non-accrual loans was not included in income. $3,782,376, or 94.4%, of the Bank's total $4,008,665 non-accrual loans at December 31, 2012 were attributable to 5 borrowers. One of these borrowers was in bankruptcy at that date. Because of the legal protections afforded to borrowers in bankruptcy, collections on such loans are difficult and the Bank anticipates that such loans may remain delinquent for an extended period of time.

At December 31, 2012, there were loans outstanding, totaling $1,804,166, not reflected in the above table as to which known information about the borrower's possible credit problems caused management to have serious doubts as to the ability of the borrowers to comply with present loan repayment terms. These loans consist of loans which were not 90 days or more past due but where the borrower is in bankruptcy or has a history of delinquency or the loan to value ratio is considered excessive due to deterioration of the collateral or other factors.

At December 31, 2012, the Company had $478,000 in real estate acquired in partial or total satisfaction of debt, compared to $1,111,000 and $215,000 in such properties at each of December 31, 2011 and 2010. This decrease for 2012 was the result of the sale of units in the property acquired in 2011, offset by properties acquired in 2012. One of the three properties acquired in 2012 was sold in 2012. This increase for 2011 was the result of a property acquired in 2011, offset by the sale of units in that property, and a write-down on the property acquired in 2010. All such properties are recorded at the lower of cost or fair value at the date acquired and carried on the balance sheet as other real estate owned. Losses arising at the date of acquisition are charged against the allowance for credit losses. Subsequent write-downs that may be required and expense of operation are included in non-interest expense. Gains and losses realized from the sale of other real estate owned are included in non-interest income or expense. For a description of the properties comprising other real estate owned at December 31, 2012, see "Item 2. — Properties."

Allowance For Credit Losses

The Bank's allowance for credit losses is based on the probable estimated losses that may be sustained in its loan portfolio. The allowance is based on two basic principles of accounting. (1) ASC Topic 450, "Accounting for Contingencies", which requires that losses be accrued when they are probable of occurring and estimable, and (2) ASC Topic 310, "Accounting by Creditors for Impairment of a Loan", which requires that losses be accrued based on the differences between the value of collateral, present value of future cash flows or values that are observable in the secondary market and the loan balance.

The allowance for credit losses is established through a provision for credit losses charged to expense. Loans are charged against the allowance for credit losses when management believes that the collectability of the principal is unlikely. The allowance, based on evaluations of the collectability of loans and prior loan loss experience, is an amount that management believes will be adequate to absorb possible losses on existing loans that may become uncollectible. The evaluations take into consideration such factors as changes in the nature and volume of the loan portfolio, overall portfolio quality, review of specific problem loans, value of collateral, and current economic conditions and trends that may affect the borrower's ability to pay. Because mortgage lending decisions are based on conservative lending policies, the Company has no exposure to the credit issues affecting the sub-prime residential mortgage market.

In 2012, the Bank was able to decrease its provision for credit losses due to specific reserves that were put in place in previous years as well as improvements in the value of underlying collateral of commercial real estate.

Transactions in the allowance for credit losses during the last five fiscal years were as follows:

| | Year Ended December 31, | | | | |
|---|---|---|---|---|---|
| | 2012 | 2011 | 2010 | 2009 | 2008 |
| | (Dollars In Thousands) | | | | |
| Beginning Balance | $3,931 | $3,400 | $3,573 | $2,022 | $1,604 |
| | | | | | |
| Loans charged off | | | | | |
| Real estate - mortgage: | | | | | |
| Residential | 735 | 4 | 66 | 85 | - |
| Commercial | - | - | 825 | - | - |
| Installment | 475 | 606 | 959 | 1,070 | 1,079 |
| Commercial | 55 | 6 | 12 | 133 | 2 |
| Total | 1,265 | 616 | 1,862 | 1,288 | 1,081 |
| | | | | | |
| Recoveries | | | | | |

| | | | | | |
|---|---|---|---|---|---|
| Real estate - mortgage: | | | | | |
| Residential | 6 | 1 | 85 | - | - |
| Commercial | 89 | 70 | 11 | - | - |
| Installment | 287 | 409 | 497 | 359 | 333 |
| Commercial | 10 | 4 | 46 | 37 | 20 |
| Total | 392 | 484 | 639 | 396 | 353 |
| Net charge offs | 873 | 132 | 1,223 | 892 | 728 |
| Provisions charged to operations | 250 | 663 | 1,050 | 2,443 | 1,146 |
| Ending balance | $3,308 | $3,931 | $3,400 | $3,573 | $2,022 |
| Average loans | $244,905 | $233,011 | $234,495 | $239,788 | $219,485 |
| Net charge-offs to average loans | 0.36 % | 0.06 % | 0.53 % | 0.37 % | 0.33 % |

The following table shows the allowance for credit losses broken down by loan category as of December 31, 2012, 2011, 2010, 2009, and 2008:

| Portfolio | At December 31, 2012 Allowance For Each Category | Percentage Of Loans In Each Category To Total Loans | 2011 Allowance For Each Category | Percentage Of Loans In Each Category To Total Loans |
|---|---|---|---|---|
| | (Dollars In Thousands) | | | |
| Real Estate - mortgage: | | | | |
| Residential | $382 | 42.41% | $584 | 45.29% |
| Commercial | 1,183 | 28.10 | 2,013 | 28.46 |
| Real Estate — construction | 10 | 1.54 | 12 | 2.14 |
| Installment | 223 | 7.28 | 228 | 7.59 |
| Credit Card | - | 0.06 | - | 0.07 |
| Indirect automobile | 835 | 18.68 | 661 | 13.42 |
| Commercial | 542 | 1.93 | 557 | 3.03 |
| Unallocated | 133 | - | (124) | - |
| Total | $3,308 | 100.00% | $3,931 | 100.00% |

| Portfolio | At December 31, 2010 Allowance For Each Category | Percentage Of Loans In Each Category To Total Loans | 2009 Allowance For Each Category | Percentage Of Loans In Each Category To Total Loans | 2008 Allowance For Each Category | Percentage Of Loans In Each Category To Total Loans |
|---|---|---|---|---|---|---|
| | (Dollars In Thousands) | | | | | |
| Real Estate – mortgage: | | | | | | |
| Residential | $196 | 43.62% | $162 | 39.81% | $123 | 36.85% |
| Commercial | 2,096 | 31.02 | 2,377 | 33.23 | 460 | 31.99 |
| Real Estate – construction | 12 | 2.29 | 4 | 0.73 | 63 | 2.77 |
| Installment | 196 | 7.00 | 146 | 6.64 | 161 | 6.91 |
| Credit Card | - | 0.07 | - | 0.07 | - | 0.07 |
| Indirect automobile | 634 | 12.93 | 697 | 15.44 | 942 | 18.47 |
| Commercial | 263 | 3.07 | 237 | 4.08 | 240 | 2.94 |
| Unallocated | 3 | - | (50) | - | 33 | - |
| Total | $3,400 | 100.00% | $3,573 | 100.00% | $2,022 | 100.00% |

**<u>Investment Securities</u>**

The Bank maintains a substantial portfolio of investment securities to provide liquidity as well as a source of earnings. The Bank's investment securities portfolio consists primarily of securities issued by U.S. Government agencies including mortgage-backed securities, securities issued by certain states and their political subdivisions, and corporate trust preferred securities. The tax treatment of the Bank's portfolio of securities issued by certain states and their political subdivisions allows the Company to use the full tax advantage of this portfolio.

The following table presents at amortized cost the composition of the investment portfolio by major category at the dates indicated.

| | At December 31, | | |
|---|---|---|---|
| | 2012 | 2011 | 2010 |
| | (In Thousands) | | |
| U.S. Treasury securities | $- | $- | $- |
| U.S. Government agencies and mortgage backed securities | 57,523 | 62,001 | 52,365 |
| Obligations of states and political subdivisions | 38,528 | 37,165 | 34,776 |
| Corporate trust preferred | 350 | 635 | 1,793 |
| Total investment securities | $96,401 | $99,801 | $88,935 |

The following table sets forth the scheduled maturities, amortized costs and weighted average yields for the Company's investment securities portfolio at December 31, 2012:

| | One Year Or Less | | One To Five Years | | Five to Ten Years | | More Than Ten Years | | Total | |
|---|---|---|---|---|---|---|---|---|---|---|
| | **Amort. Cost** | **Weighted Average Yield** | **Amort. Cost** | **Weighted Average Yield** | **Amort. Cost** | **Weighted Average Yield** | **Amort. Cost** | **Weighted Average Yield** | **Amort. Cost** | **Weighted Average Yield** |
| U.S. Treasury securities | $ - | - % | $ - | - % | $ - | - % | $ - | - % | $ - | - % |
| U.S. Government agencies and mortgage backed securities | - | - | - | - | 3,685 | 4.19 | 53,838 | 3.34 | 57,523 | 3.39 |
| Obligations of states and political subdivisions | 125 | 3.70 | - | - | 400 | 4.00 | 38,003 | 4.26 | 38,528 | 4.31 |
| Corporate trust preferred | - | - | - | - | - | - | 350 | 9.25 | 350 | 9.25 |
| Total investment securities | $ 125 | 3.70 % | $ - | - % | $ 4,085 | 4.17 % | $ 92,191 | 3.74 % | $ 96,401 | 3.76 % |

At December 31, 2012, the Bank had no investments in securities of a single issuer (other than the U.S. Government securities and securities of federal agencies and government-sponsored enterprises), which aggregated more than 10% of stockholders' equity.

Deposits And Other Sources of Funds

The funds needed by the Bank to make loans are primarily generated by deposit accounts solicited from the communities surrounding its branches in Anne Arundel County. Consolidated total deposits were $332,288,886 as of December 31, 2012. The Bank uses borrowings from the Federal Home Loan Bank ("FHLB") of Atlanta to supplement funding from deposits. The Bank was permitted to borrow up to $54.69 million under a line of credit from the FHLB of Atlanta as of December 31, 2012.

**Deposits.** The Bank's deposit products include regular savings accounts (statements), money market deposit accounts, demand deposit accounts, NOW checking accounts, IRA and SEP accounts, Christmas Club accounts and certificates of deposit. Variations in service charges, terms and interest rates are used to target specific markets. Ancillary products and services for deposit customers include safe deposit boxes, money orders, night depositories, automated clearinghouse transactions, wire transfers, ATMs, telephone banking, and internet banking. The Bank is a member of the Cirrus(R), Star(R), Pulse(R) and MoneyPass(R) ATM networks.

As stated above, the Bank obtains deposits principally through its network of branch offices. The Bank does not solicit brokered deposits. At December 31, 2012, the Bank had approximately $46.55 million in certificates of deposit and other time deposits of $100,000 or more, including IRA accounts. The following table provides information as to the maturity of all time deposits of $100,000 or more at December 31, 2012:

| | Amount<br>**(In Thousands)** |
|---|---|
| Three months or less | $ 6,573 |
| Over three through six months | 3,372 |
| Over six through 12 months | 14,637 |
| Over 12 months | 21,967 |
| Total | $ 46,549 |

**Borrowings.** In addition to deposits, the Bank from time to time obtains advances from the FHLB of Atlanta of which it is a member. FHLB of Atlanta advances may be used to provide funds for residential housing finance, for small business lending, and to meet specific and anticipated needs. The Bank may draw on a $54.69 million line of credit from the FHLB of Atlanta, which is secured by a floating lien on the Bank’s residential first mortgage loans and various federal and agency securities. There was $10 million in a convertible advance under this credit arrangement at December 31, 2012. The advance matures in November 1, 2017, is callable monthly, and bears a 3.28% rate of interest. There was a $5 million convertible advance settled July 21, 2008 with a final maturity of July 23, 2018. This advance has a 2.73% rate of interest and was callable quarterly, starting July 23, 2009. There was a $5 million convertible advance taken out August 22, 2008 which has a final maturity of August 22, 2018. This advance has a 3.34% rate of interest and is callable quarterly, starting August 22, 2011. The Bank also has an unsecured line of credit in the amount of $3 million from another commercial bank but currently has no balance outstanding. The Bank also has an additional unsecured line of credit in the amount of $5 million from a financial bank, of which nothing was outstanding at December 31, 2012.

Competition

The Bank faces competition for deposits and loans from other community banks, branches or affiliates of larger banks, savings and loan associations, savings banks and credit unions, which compete vigorously (currently, sixteen FDIC-insured depository institutions operate within two miles of the Bank's headquarters). With respect to indirect lending, the Bank faces competition from other banks and the financing arms of automobile manufacturers. The Bank competes in this area by offering competitive rates and responsive service to dealers.

The Bank's interest rates, loan and deposit terms, and offered products and services are impacted, to a large extent, by such competition. The Bank attempts to provide superior service within its community and to know, and facilitate services, to, its customers. It seeks commercial relationships with small to medium size businesses, which the Bank believes would welcome personal service and flexibility. The bank believes its greatest competition comes from larger intra- and inter-state financial institutions.

Other Activities

The Company also owns all outstanding shares of capital stock of GBB Properties, Inc. ("GBB"), another Maryland corporation which was organized in 1994 and which is engaged in the business of acquiring, holding and disposing of real property, typically acquired in connection with foreclosure proceedings (or deeds in lieu of foreclosure) instituted by the Bank or acquired in connection with branch expansions by the Bank.

Employees

At December 31, 2012, the Bank had 103 full-time equivalent employees. Neither the Company nor GBB currently has any employees.