Howard Bancorp Inc
Form 10-Q
November 14, 2013

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, 2013

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 to 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 Act). Yes ¨ No x

The number of outstanding shares of common stock outstanding as of October 31, 2013.

Common Stock, $0.01 par value 4,040,471 shares

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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 within the meaning Private Securities Litigation Reform Act of 1995, which can be identified by the use of words such as “estimate,” “project,” “believe,” “intend,” “anticipate,” “plan,” “seek,” “ex “will,” “may,” “should” and words of similar meaning. You can also identify 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 our business plans and strategies, including increasing originations of residential mortgage loans and our mortgage lending portfolio and our selling of loans into the secondary market;
· expansion and the expected timing of the opening of our new office in Towson, Maryland;
· statements regarding our intentions with respect to our investment portfolio and the status of unrealized losses in such portfolio;
· statement regarding anticipated changes in occupancy costs;
· statement regarding our credit quality;
· statements with respect to anticipated losses on nonperforming loans;
· statements with respect to our allowance for credit losses, and the adequacy thereof;
· future cash requirements relating to commitments to extend credit, and that we do not anticipate any material losses in connection therewith;
· our ability to retain maturing certificates of deposits; and
· statement with respect to adequate liquidity.

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 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. These and other risk factors are detailed in the Company's Annual Report on Form 10-K for the year ended December 31, 2012 under "Item 1A Risk Factors". You should not put undue reliance on any forward-looking statements.

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PART I
Item 1. Financial Statements

Howard Bancorp, Inc. and Subsidiary

Consolidated Balance Sheets

(in thousands)	Unaudited September 30, 2013	December 31, 2012
ASSETS		
Cash and due from banks	$ 17,397	$ 25,739
Federal funds sold	2,017	10,622
Total cash and cash equivalents	19,414	36,361
Securities available-for-sale	21,205	26,875
Nonmarketable equity securities	2,282	1,475
Loans held for sale	804	1,639
Loans and leases, net of unearned income	401,508	322,218
Allowance for credit losses	(3,145)	(2,764)
Net loans and leases	398,363	319,454
Bank premises and equipment, net	10,385	9,573
Core deposit intangible	363	-
Bank owned life insurance	8,210	-
Other real estate owned	2,377	2,903
Deferred income taxes	1,458	1,160
Interest receivable and other assets	2,057	2,235
Total assets	$ 466,918	$ 401,675
LIABILITIES		
Noninterest-bearing deposits	$ 91,189	$ 95,875
Interest-bearing deposits	268,699	218,983
Total deposits	359,888	314,858
Short-term borrowings	39,934	26,987
Long-term borrowings	18,000	12,000
Accrued expenses and other liabilities	1,060	1,109
Total liabilities	418,882	354,954
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, 2013 and December 31, 2012, net of issuance cost	12,562	12,562
Common stock - par value of $0.01 authorized 10,000,000 shares; issued and outstanding 4,040,471 shares at September 30, 2013 and December 31, 2012	40	40
Capital surplus	37,541	37,484
Accumulated deficit	(2,116)	(3,386)

Accumulated other comprehensive income		9		21
Total shareholders' equity		48,036		46,721
Total liabilities and shareholders'equity	$	466,918	$	401,675

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

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Consolidated Statements of Operations

	Unaudited Nine months ended September 30,		Three months ended September 30,	
(in thousands)	2013	2012	2013	2012
INTEREST INCOME				
Interest and fees on loans	$ 12,713	$ 11,386	$ 4,627	$ 3,854
Interest and dividends on securities	57	74	16	29
Other interest income	35	46	12	15
Total interest income	12,805	11,506	4,655	3,898
INTEREST EXPENSE				
Deposits	1,208	1,371	422	432
Short-term borrowings	83	125	26	40
Long-term borrowings	90	53	49	14
Total interest expense	1,381	1,549	497	486
NET INTEREST INCOME	11,424	9,957	4,158	3,412
Provision for credit losses	666	650	140	308
Net interest income after provision for credit losses	10,758	9,307	4,018	3,104
NONINTEREST INCOME				
Service charges on deposit accounts	275	235	106	87
Gains on the sale of loans	195	111	35	31
Loss on the sale of other real estate owned	(37)	(131)	-	-
Income from bank owned life insurance	210	-	72	-
Other operating income	319	334	106	98
Total noninterest income	962	549	319	216
NONINTEREST EXPENSE				
Compensation and benefits	5,260	4,291	1,905	1,491
Occupancy and equipment	1,154	1,124	406	381
Amortization of core deposit intangible	14	-	14	-
Marketing and business development	464	435	153	145
Professional fees	634	445	246	134
Data processing fees	387	331	148	116
FDIC Assessment	242	228	87	83
Provision for other real estate owned	347	48	347	-
Other operating expense	1,006	941	401	309
Total noninterest expense	9,508	7,843	3,707	2,659
INCOME BEFORE INCOME TAXES	2,212	2,013	630	661
Income tax expense	808	831	223	273
NET INCOME	$ 1,404	$ 1,182	$ 407	$ 388
Preferred stock dividends	134	471	31	157

Net income available to common shareholders	$	1,270	$	711	$	376	$	231
NET INCOME PER COMMON SHARE AVAILABLE								
Basic	$	0.31	$	0.24	$	0.09	$	0.06
Diluted	$	0.31	$	0.24	$	0.09	$	0.06

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

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Consolidated Statements of Comprehensive Income

(in thousands) (Unaudited)	For the nine months ended September 30, 2013		2012	
Net Income	$	1,404	$	1,182
Other comprehensive income				
Investments available-for-sale:				
Unrealized holding (losses) gains		(21)		3
Related income tax benefit (expense)		9		(1)
Comprehensive income	$	1,392	$	1,184

(in thousands) (Unaudited)	For the three months ended September 30, 2013		2012	
Net Income	$	407	$	388
Other comprehensive income				
Investments available-for-sale:				
Unrealized holding (losses) gains		(1)		15
Related income tax benefit (expense)		-		(5)
Comprehensive income	$	406	$	398

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

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Consolidated Statements of Changes in Shareholders' Equity

(dollars in thousands, except per share data) (Unaudited)	Preferred stock	Number of shares	Common stock	Capital Surplus	Accumulated deficit	Accumulated other comprehensive gain/loss	Total
Balances at January 1, 2012	$ 12,562	2,640,264	$ 26	$ 28,413	$ (4,391)	$ 20	$ 36,630
Net income	-	-	-	-	1,182	-	1,182
Net unrealized gain on securities	-	-	-	-	-	2	2
Dividends paid on preferred stock	-	-	-	-	(471)	-	(471)
Issuance of common stock:							
Stock offering	-	1,396,364	14	8,966	-	-	8,980
Balances at September 30, 2012	$ 12,562	4,036,628	$ 40	$ 37,379	$ (3,680)	$ 22	$ 46,323
Balances at January 1, 2013	$ 12,562	4,040,471	$ 40	$ 37,484	$ (3,386)	$ 21	$ 46,721
Net income	-	-	-	-	1,404	-	1,404
Net unrealized loss on securities	-	-	-	-	-	(12)	(12)
Stock-based compensation	-	-	-	57	-	-	57
Dividends paid on preferred stock	-	-	-	-	(134)	-	(134)
Balances at September 30, 2013	$ 12,562	4,040,471	$ 40	$ 37,541	$ (2,116)	$ 9	$ 48,036

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

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Consolidated Statements of Cash Flows

	Unaudited Nine months ended September 30,	
(in thousands)	2013	2012
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 1,404	$ 1,182
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for credit losses	666	650
Deferred income taxes (benefit) expense	(289)	470
Provision for other real estate owned	347	48
Depreciation	441	381
Stock-based compensation	57	8,980
Net accretion of investment securities	16	32
Net amortization of intangible asset	14	-
Loans originated for sale	(9,827)	(8,658)
Proceeds from loans originated for sale	10,856	8,841
Gains on sales of loans	(195)	(111)
Loss on sales of other real estate owned, net	37	131
Cash surrender value of BOLI	(210)	-
Decrease in interest receivable	(16)	(62)
Increase in interest payable	36	10
(Increase) decrease in other assets	(477)	1,003
(Decrease) increase in other liabilities	(86)	278
Net cash provided by operating activities	2,774	13,175
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of investment securities available-for-sale	(34,997)	(44,018)
Proceeds from maturities of investment securities available-for-sale	40,631	21,413
Net increase in loans and leases outstanding	(42,389)	(25,358)
Purchase of bank owned life insurance	(8,000)	-
Proceeds from the sale of other real estate owned	141	527
Purchase of premises and equipment	(416)	(555)
Branch acquisition (net of cash received)	(3,195)	-
Net cash used in investing activities	(48,225)	(47,991)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net (decrease) increase in noninterest-bearing deposits	(4,685)	17,890
Net increase in interest-bearing deposits	14,376	6,893
Net increase in short-term borrowings	12,947	14,635
Proceeds from issuance of long-term debt	14,000	-
Repayment of long-term debt	(8,000)	(4,000)
Cash dividends on preferred stock	(134)	(471)
Net cash provided by financing activities	28,504	34,947
Net (decrease) increase in cash and cash equivalents	(16,947)	131
Cash and cash equivalents at beginning of period	36,361	18,205

Cash and cash equivalents at end of period	$	19,414	$	18,336
SUPPLEMENTAL INFORMATION				
Cash payments for interest	$	848	$	1,539
Cash payments for income taxes		707		475
Transferred from loans to other real estate owned		-		1,598
BRANCH ACQUSITION				
Tangible assets acquired (net of cash received)		38,159		-
Identifiable intangible assets acquired		376		-
Liabilities assumed		35,340		-

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

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 Bank 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. These consolidated financial statements included herein are unaudited; however in the opinion of management, present a fair representation of the Company's financial condition, results of operations, and cash flows for the periods presented. The Company believes that the disclosures are adequate to make the information presented not misleading. The balances as of December 31, 2012 have been derived from audited financial statements. There have been no significant changes to the Company's accounting policies as disclosed in the 2012 Annual Report. The results of operations for the three and nine months ended September 30, 2013 are not necessarily indicative of the results of operations to be expected for the remainder of the year or any other period.

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").

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 Howard County Maryland, Anne Arundel County Maryland and their contiguous counties.

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 accounting principles generally accepted in the United States of America ("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.

Segment Information

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

New Accounting Pronouncements

ASU No. 2013-02, *Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income*. ASU No. 2013-02 requires an entity to provide information about the amounts reclassified out of accumulated other comprehensive income by component. In addition, an entity is required to present significant amounts reclassified out of accumulated other comprehensive income by the respective line items of net income if the amount is reclassified in its entirety in the same reporting period. For other amounts that are not to be reclassified in their entirety to net income, an entity is required to provide cross references to related footnote disclosures. The amendments do not change the current requirements for reporting net income or other comprehensive income, nor do they require new information to be disclosed. The amendments were effective prospectively for reporting periods beginning after December 15, 2012. The adoption of ASU No. 2013-02 as of January 1, 2013 did not have a material impact on the Company's consolidated financial statements.

Note 2: Investments Securities

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

(in thousands)	September 30, 2013				December 31, 2012			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
U.S. Federal agencies	$ 21,007	$ 2	$ -	$ 21,009	$ 26,526	$ 14	$ -	$ 26,540
Mortgage-backed	184	12	-	196	314	21	-	335
	$ 21,191	$ 14	$ -	$ 21,205	$ 26,840	$ 35	$ -	$ 26,875

There have not been any individual securities with an unrealized loss position for a period greater than one year as of either September 30, 2013 or December 31, 2012. 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, 2013 and December 31, 2012 are presented below:

September 30, 2013 (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. Federal agencies	$ 4,000	$ -	$ -	$ -	$ 4,000	$ -
Mortgage-backed	-	-	-	-	-	-
	$ 4,000	$ -	$ -	$ -	$ 4,000	$ -

December 31, 2012 (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. Federal agencies	$ 3,000	$ -	$ -	$ -	$ 3,000	$ -
Mortgage-backed	-	-	-	-	-	-
	$ 3,000	$ -	$ -	$ -	$ 3,000	$ -

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.

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

(in thousands)	September 30, 2013				December 31, 2012			
	Amortized Cost		Estimated Fair Value		Amortized Cost		Estimated Fair Value	
Amounts maturing:								
One year or less	$	21,006	$	21,008	$	23,536	$	23,544
After one through five years		62		66		3,121		3,136
After five through ten years		123		131		90		96
After ten years		-		-		93		99
	$	21,191	$	21,205	$	26,840	$	26,875

There were no sales of investment securities during the nine months ended September 30, 2013 or in 2012. At September 30, 2013 and December 31, 2012, $16.5 million and $16.6 million fair value of securities was pledged as collateral for repurchase agreements, respectively. The outstanding balance of no single issuer, except for U. S. Government and U. S. Government agency securities, exceeded ten percent of shareholders' equity at either period.

Note 3: 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, 2013 and December 31, 2012 are presented in the following table:

(in thousands)	September 30, 2013		% of Total		December 31, 2012		% of Total	
Real estate								
Construction and land	$	49,390	12.3	%	$	37,963	11.8	%
Residential - first lien		36,149	9.0			29,826	9.3	
Residential - junior lien		8,244	2.1			7,983	2.5	
Total residential real estate		44,393	11.1			37,809	11.7	
Commercial - owner occupied		89,008	22.1			61,119	19.0	
Commercial - non-owner occupied		116,306	29.0			96,223	29.9	
Total commercial real estate		205,314	51.1			157,342	48.8	
Total real estate loans		299,097	74.5			233,114	72.3	
Commercial loans and leases		101,463	25.3			87,844	27.3	
Consumer		948	0.2			1,260	0.4	
Total loans	$	401,508	100.0	%	$	322,218	100.0	%

There were $.8 million and $1.6 million in loans held for sale at September 30, 2013 and at December 31, 2012, respectively.

Note 4: Credit Quality Assessment

Allowance for Credit Losses

The following table provides information on the activity in the allowance for credit losses by the respective loan portfolio segment for the three months and nine months ended September 30, 2013 and September 30, 2012:

	September 30, 2013							
(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	$ 127	$ 204	$ 22	$ 650	$ 505	$ 1,227	$ 29	$ 2,764
Charge-offs	-	(183)	-	-	(2)	(202)	-	(387)
Recoveries	-	-	-	-	30	72	-	102
Provision for credit losses	(20)	138	-	(70)	241	393	(16)	666
Ending balance	$ 107	$ 159	$ 22	$ 580	$ 774	$ 1,490	$ 13	$ 3,145
Three months ended								
Beginning balance	$ 122	$ 133	$ 22	$ 663	$ 502	$ 1,482	$ 27	$ 2,951
Charge-offs	-	-	-	-	(2)	-	-	(2)
Recoveries	-	-	-	-	-	56	-	56
Provision for credit losses	(15)	26	-	(83)	274	(48)	(14)	140
Ending balance	$ 107	$ 159	$ 22	$ 580	$ 774	$ 1,490	$ 13	$ 3,145
Ending balance: individually evaluated for impairment	-	-	-	-	373	715	-	1,088
collectively evaluated for impairment	107	159	22	580	401	775	13	2,057
Loans:								
Ending balance	49,390	36,149	8,244	89,008	116,306	101,463	948	401,508
Ending balance: individually evaluated for impairment	-	-	-	-	3,098	3,403	-	6,501
collectively evaluated for impairment	49,390	36,149	8,244	89,008	113,208	98,060	948	395,007

	September 30, 2012							
(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	$ 111	$ 64	$ 611	$ 197	$ 2,233	$ 43	$ 3,433
Charge-offs	-	(23)	(44)	-	(268)	(1,130)	(15)	(1,480)
Recoveries	-	-	-	-	63	65	2	130
Provision for credit losses	18	17	2	40	357	215	1	650
Ending balance	$ 192	$ 105	$ 22	$ 651	$ 349	$ 1,383	$ 31	$ 2,733
Three months ended								
Beginning balance	$ 99	$ 65	$ 42	$ 553	$ 532	$ 1,744	$ 41	$ 3,076
Charge-offs	-	-	-	-	(268)	(463)	-	(731)
Recoveries	-	-	-	-	63	16	1	80
Provision for credit losses	93	40	(20)	98	22	87	(11)	308
Ending balance	$ 192	$ 105	$ 22	$ 651	$ 349	$ 1,383	$ 31	$ 2,733
Ending balance: individually evaluated for impairment	103	73	-	-	-	257	-	433
collectively evaluated for impairment	89	32	22	651	349	1,126	31	2,300
Loans:								
Ending balance	35,889	23,074	8,162	58,793	86,116	85,409	1,371	298,814
Ending balance: individually evaluated for impairment	432	471	-	-	3,146	1,978	-	6,027
collectively evaluated for impairment	35,457	22,603	8,162	58,793	82,970	83,431	1,371	292,787

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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:

(in thousands)	September 30, 2013 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:								
Not classified	$ 49,390	$ 36,149	$ 8,244	$ 89,008	$ 115,933	$ 98,453	$ 948	$ 398,125
Special mention	-	-	-	-	-	-	-	-
Substandard	-	-	-	-	373	3,010	-	3,383
Doubtful	-	-	-	-	-	-	-	-
Total	$ 49,390	$ 36,149	$ 8,244	$ 89,008	$ 116,306	$ 101,463	$ 948	$ 401,508

(in thousands)	December 31, 2012 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:								
Not classified	$ 37,531	$ 29,384	$ 7,983	$ 61,119	$ 95,839	$ 86,701	$ 1,260	$ 319,817
Special mention	-	-	-	-	-	-	-	-
Substandard	432	442	-	-	384	1,143	-	2,401
Doubtful	-	-	-	-	-	-	-	-
Total	$ 37,963	$ 29,826	$ 7,983	$ 61,119	$ 96,223	$ 87,844	$ 1,260	$ 322,218

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

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

An aged analysis of past due loans are as follows:

	September 30, 2013							
(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:								
Accruing loans current	$ 49,390	$ 35,494	$ 8,244	$ 89,008	$ 115,516	$ 97,951	$ 948	$ 396,551
Accruing loans past due:								
31-59 days past due	-	655	-	-	-	45	-	700
60-89 days past due	-	-	-	-	-	-	-	-
Greater than 90 days past due	-	-	-	-	417	457	-	874
Total past due	$ -	$ 655	$ -	$ -	$ 417	$ 502	$ -	$ 1,574
Non-accrual loans	-	-	-	-	373	3,010	-	3,383
Total loans	$ 49,390	$ 36,149	$ 8,244	$ 89,008	$ 116,306	$ 101,463	$ 948	$ 401,508

	December 31, 2012							
(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:								
Accruing loans current	$ 37,531	$ 29,176	$ 7,942	$ 61,119	$ 95,839	$ 86,393	$ 1,260	$ 319,260
Accruing loans past due:								
31-59 days past due	-	-	-	-	-	-	-	-
60-89 days past due	-	-	-	-	-	308	-	308
Greater than 90 days past due	-	208	41	-	-	-	-	249
Total past due	$ -	$ 208	$ 41	$ -	$ -	$ 308	$ -	$ 557
Non-accrual loans	432	442	-	-	384	1,143	-	2,401
Total loans	$ 37,963	$ 29,826	$ 7,983	$ 61,119	$ 96,223	$ 87,844	$ 1,260	$ 322,218

Total loans either in non-accrual status or in excess of ninety days delinquent totaled $4.3 million or 1.06% of total loans outstanding as of September 30, 2013 which represents an increase from $2.7 million as of December 31, 2012. This increase was primarily from one commercial relationship with three loans totaling nearly $1.9 million that was transferred into non-accrual status during 2013.

The impaired loans at September 30, 2013 and December 31, 2012 are as follows:

September 30, 2013

(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:								
Recorded investment	-	-	-	-	3,098	3,403	-	6,501
With an allowance recorded	-	-	-	-	373	2,549	-	2,922
With no related allowance recorded	-	-	-	-	2,725	854	-	3,579
Related allowance	-	-	-	-	373	715	-	1,088
Unpaid principal	-	-	-	-	3,161	3,418	-	6,579
Nine months ended								
Average balance of impaired loans	-	-	-	-	3,489	3,649	-	7,138
Interest income recognized	-	-	-	-	185	98	-	283
Three months ended								
Average balance of impaired loans	-	-	-	-	3,483	3,536	-	7,019
Interest income recognized	-	-	-	-	73	8	-	81

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	December 31, 2012							
(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:								
Recorded investment	432	442	-	-	3,134	1,568	-	5,576
With an allowance recorded	432	442	-	-	381	540	-	1,795
With no related allowance recorded	-	-	-	-	2,753	1,028	-	3,781
Related allowance	21	138	-	-	148	257	-	564
Unpaid principal	432	442	-	-	3,372	1,580	-	5,826
Average balance of impaired loans	439	444	-	-	4,225	1,809	7	6,924
Interest income recognized	18	15	-	-	211	96	1	341

Nonaccrual loans included in impaired loans totaled $3.4 million and $2.4 million at September 30, 2013 and December 31, 2012, respectively. Interest income that would have been recorded if nonaccrual loans had been current and in accordance with their original terms was $50 thousand for the first nine months of 2013.

Management routinely evaluates other real estate owned (“OREO”) based upon periodic appraisals. For the nine months ended September 30, 2013 and 2012 an additional valuation allowance of $347 thousand and $48 thousand, respectively, were recorded in non-interest expense as the current appraised value was not sufficient to cover the recorded OREO amount. For the nine months ended September 30, 2013 there were no new loans transferred from loans to OREO and one OREO property totaling $141 thousand was sold. In comparison, for the nine months ended September 30, 2012 two loans were transferred from loans to OREO totaling $1.6 million, net of reserves, and the Bank sold one OREO property totaling $527 thousand.

The trouble debt restructured loans (“TDRs”) at September 30, 2013 and December 31, 2012 are as follows:

	September 30, 2013				
(dollars in thousands)	Number of Loans	Non-Accrual Status	Number of Loans	Accrual Status	Total TDRs
Commercial real estate non-owner occupied	1	$ 373	-	$ -	$ 373
Commercial loans	6	875	-	-	875
	7	$ 1,248	-	$ -	$ 1,248

	December 31, 2012				
(dollars in thousands)	Number of Loans	Non-Accrual Status	Number of Loans	Accrual Status	Total TDRs
Commercial real estate non-owner occupied	1	$ 381	-	$ -	$ 381
Commercial loans	6	903	-	-	903
	7	$ 1,284	-	$ -	$ 1,284

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

	September 30, 2013		
(in thousands)	Not Performing to Modified Terms	Performing to Modified Terms	Total TDRs
Commercial loans			
Interest only payments	$ -	$ -	$ -
Rate modification	-	-	-
Forbearance	1,248	-	1,248
Extension or other modification	-	-	-
Total commercial	1,248	-	1,248
Total TDR's	$ 1,248	$ -	$ 1,248

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(in thousands)	December 31, 2012 Not Performing to Modified Terms	Performing to Modified Terms	Total TDRs
Commercial loans			
Interest only payments	$ -	$ -	$ -
Rate modification	-	-	-
Forberance	1,284	-	1,284
Extension or other modification	-	-	-
Total commercial	1,284	-	1,284
Total TDR's	$ 1,284	$ -	$ 1,284

There were no new loans restructured in the first nine months of 2013.

Note 5: Intangibles

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

(in thousands)	September 30, 2013 Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Amortizing intangible assets:			
Core deposit intangible	$ 377	$ 14	$ 363

There were no intangible assets in prior periods

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

(in thousands)	
2013	20
2014	74
2015	57
2016	46
Thereafter	166
Total amortizing intangible assets	$363

Note 6: Deposits

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

(dollars in thousands)	September 30, 2013 Amount	% of Total		December 31, 2012 Amount	% of Total	
Noninterest-bearing demand	$ 91,189	25	%	$ 95,875	30	%
Interest-bearing checking	25,180	7		26,209	8	
Money market accounts	80,657	22		70,856	23	
Savings	12,823	4		11,107	4	

Certificates of deposit $100,000 and over		96,969	27			77,759	25	
Certificates of deposit under $100,000		53,070	15			33,052	10	
Total deposits	$	359,888	100	%	$	314,858	100	%

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Note 7: Stock Options, Awards and Warrants

The Company initially raised $4,775,000 of capital by selling to its founders investment units consisting of one share of common stock and a fully detachable warrant equal to .25 shares of common stock per unit. The warrants were issued in recognition of the financial and organizational risk undertaken by the purchasers in the organizational offering. The warrants are immediately exercisable and will expire ten (10) years from the date of issuance on August 8, 2014. As of September 30, 2013 there have not been any exercises of these warrants and the Company has outstanding warrants to purchase 119,376 shares at the price of $10.00 per share.

The Company's stock incentive plans provide for awards of nonqualified and incentive stock options as well as vested and non-vested common stock awards and other stock-based 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 options and 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. The Company previously maintained an Advisory Board, for which non-employee members were compensated via stock options for meeting attendance. These nonqualified stock options can be granted with terms up to ten years, vest immediately, and are fully exercisable at time of grant. Stock awards granted to directors are based on the fair value of the awards, which is generally the market price of the common stock on the measurement date, and vest immediately.

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

	September 30, 2013		December 31, 2012	
	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price
Balance at January 1, 2013	395,351	$ 11.16	395,351	$ 11.16
Granted	-	-	-	-
Exercised	-	-	-	-
Forfeited	(1,800)	7.50	-	-
Balance at September 30, 2013	393,551	$ 11.18	395,351	$ 11.16
Exercisable at September 30, 2013	393,551	$ 11.18	395,351	$ 11.16
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 $8.66 at September 30, 2013 the options outstanding had an aggregate intrinsic value of $12 thousand. There were no options exercised during the first nine months of 2013.

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

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

(In dollars, except share data):	Number of Shares	Weighted Average Grant-Date Fair Value
Restricted stock at January 1, 2013	0	$ 0
Granted	50,000	$ 6.89
Vested	0	$ 0
Restricted stock at September 30, 2013	50,000	$ 6.89

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At September 30, 2013, based on equity awards outstanding at that time, the total unrecognized pre-tax compensation expense related to unvested equity awards was $287 thousand. This expense is expected to be recognized through 2016.

Note 8: Profit Sharing Plan

The Company sponsors a defined contribution retirement plan through a Section 401(k) profit sharing plan. Employees may contribute up to 15% of their pretax compensation. Participants are eligible for matching Company contributions up to 4% of eligible compensation dependent on the level of voluntary contributions. Company matching contributions totaled $103 thousand for the nine months ended September 30, 2013 and $80 thousand for the nine months ended September 30, 2012. The Company's matching contributions vest immediately.

Note 9: 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)	2013	2012	2013	2012
Net income	$ 1,404	$ 1,182	$ 407	$ 388
Preferred dividends	(134)	(471)	(31)	(157)
Net income available to common shareholders (numerator)	$ 1,270	$ 711	$ 376	$ 231
BASIC				
Average common shares outstanding (denominator)	4,040,471	3,012,288	4,040,471	3,748,248
Basic income per common share	$ 0.31	$ 0.24	$ 0.09	$ 0.06
DILUTED				
Average common shares outstanding	4,040,471	3,012,288	4,040,471	3,748,248
Diluted effect of stock options and warrants	1,371	-	1,371	-
Diluted average common shares outstanding (denominator)	4,041,842	3,012,288	4,041,842	3,748,248
Diluted income per common share	$ 0.31	$ 0.24	$ 0.09	$ 0.06
Stock options and warrants outstanding that are anti-dilutive and thus excluded from calculation of diluted number of shares presented above	486,422	514,127	486,422	514,127

Note 10: Risk-Based Capital

The Federal Deposit Insurance Corporation Improvement Act of 1991 ("FDICIA") required that the federal regulatory agencies adopt regulations defining five capital tiers for banks: well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized and critically undercapitalized. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Company's financial statements. Quantitative measures, established by the regulators to ensure capital adequacy, require that the Bank and Bancorp maintain minimum ratios (set forth below) of capital to risk-weighted assets. Under the guidelines, capital is compared to the relative risk related to the balance sheet. The capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

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Management believes that, as of September 30, 2013 and December 31, 2012 the Bank met all capital adequacy requirements to which it is subject.

(dollars in thousands)	Actual Amount	Ratio	For capital adequacy purposes Amount	Ratio	To be well capitalized under the FDICIA prompt corrective action provisions Amount	Ratio
As of September 30, 2013:						
Total capital (to risk-weighted assets)						
Howard Bank	$ 49,722	12.22 %	$ 32,541	8.00 %	$ 40,676	10.00 %
Howard Bancorp	$ 50,749	12.31 %	$ 32,975	8.00 %	N/A	
Tier 1 capital (to risk-weighted assets)						
Howard Bank	$ 46,580	11.45 %	$ 16,271	4.00 %	$ 24,406	6.00 %
Howard Bancorp	$ 47,604	11.55 %	$ 16,487	4.00 %	N/A	
Tier 1 capital (to average assets) (Leverage ratio)						
Howard Bank	$ 46,580	10.64 %	$ 17,509	4.00 %	$ 21,887	5.00 %
Howard Bancorp	$ 47,604	10.86 %	$ 17,535	4.00 %	N/A	
As of December 31, 2012:						
Total capital (to risk-weighted assets)						
Howard Bank	$ 39,739	12.17 %	$ 26,127	8.00 %	$ 32,659	10.00 %
Howard Bancorp	$ 49,404	15.02 %	$ 26,312	8.00 %	N/A	
Tier 1 capital (to risk-weighted assets)						
Howard Bank	$ 36,978	11.32 %	$ 13,064	4.00 %	$ 19,595	6.00 %
Howard Bancorp	$ 46,640	14.18 %	$ 13,156	4.00 %	N/A	
Tier 1 capital (to average assets) (Leverage ratio)						
Howard Bank	$ 36,978	9.79 %	$ 15,109	4.00 %	$ 18,887	5.00 %
Howard Bancorp	$ 46,640	12.34 %	$ 15,114	4.00 %	N/A	

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

Note 11: Preferred Stock

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

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

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

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

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

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

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

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

The types of instruments valued based on quoted market prices in active markets include most U.S. government and agency securities, liquid mortgage products, active listed equities and most money market securities. Such instruments are generally classified within Level 1 or Level 2 of the fair value hierarchy. As required by FASB ASC Topic 820, the Company does not adjust the quoted price for such instruments.

The types of instruments valued based on quoted prices in markets that are not active, broker or dealer quotations, or alternative pricing sources with reasonable levels of price transparency include most investment-grade and high-yield corporate bonds, less liquid mortgage products, less liquid equities, state, municipal and provincial obligations, and certain physical commodities. Such instruments are generally classified within Level 2 of the fair value hierarchy.

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.

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 as of September 30, 2013 and December 31, 2012.

September 30, 2013 (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. Federal agencies	$ 21,009	$ -	$ 21,009	$ -
Mortgage-backed securities	196	-	196	-
Loans held for sale	804	-	804	-

December 31, 2012 (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. Federal agencies	$ 26,540	$ -	$ 26,540	$ -
Mortgage-backed securities	335	-	335	-
Loans held for sale	1,639	-	1,639	-

The following table sets forth the Company's financial assets and liabilities that were accounted for or disclosed at fair value on a nonrecurring basis as of September 30, 2013 and December 31, 2012.

September 30, 2013 (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	$ 2,377	$ -	$ -	$ 2,377
Impaired loans:				
Construction and land	-	-	-	-
Residential - first lien	-	-	-	-
Residential - junior lien	-	-	-	-
Commercial - owner occupied	-	-	-	-
Commercial - non-owner occupied	2,725	-	-	2,725
Commercial loans and leases	2,688	-	-	2,688
Consumer	-	-	-	-

December 31, 2012 (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	$ 2,903	$ -	$ -	$ 2,903
Impaired loans:				
Construction and land	411	-	-	411
Residential - first lien	304	-	-	304
Residential - junior lien	-	-	-	-
Commercial - owner occupied	-	-	-	-
Commercial - non-owner occupied	2,985	-	-	2,985
Commercial loans and leases	1,311	-	-	1,311
Consumer	-	-	-	-

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:

Cash and cash equivalents: The fair value of cash and cash equivalents is estimated to approximate the carrying amounts.

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. See Note 2 for additional information.

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

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

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

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

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

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

The following table presents required information in accordance with ASC Topic 825 "Financial Instruments" at September 30, 2013 and December 31, 2012.

	September 30, 2013				
(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					
Cash and cash equivalents	$ 19,414	$ 19,414	$ -	$ 19,414	$ -
Nonmarketable equity securities	2,282	2,282	-	2,282	-
Loans and leases	398,363	402,061	-	-	402,061
Financial Liabilities					
Deposits	359,888	360,425	-	-	360,425
Short-term borrowings	39,934	39,934	-	39,934	-
Long-term borrowings	18,000	18,003	-	18,003	-

	December 31, 2012				
(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					
Cash and cash equivalents	$ 36,361	$ 36,361	$ -	$ 36,361	$ -
Nonmarketable equity securities	1,475	1,475	-	1,475	-
Loans and leases	319,454	322,495	-	-	322,495
Financial Liabilities					
Deposits	314,858	314,292	-		314,292
Short-term borrowings	26,987	26,987	-	26,987	-
Long-term borrowings	12,000	12,025	-	12,025	-

Note 13: Acquisition

On August 16, 2013, Howard Bank, the operating subsidiary of Howard Bancorp, Inc., purchased from Cecil Bank its branch located at 3 West Bel Air Avenue, Aberdeen, Maryland. Pursuant to the transaction, Howard Bank acquired $37.1 million in loans and $35.2 million in deposits from Cecil Bank, as well as the branch premises and equipment at their book value. In connection with its purchase of the branch from Cecil Bank, Howard Bank made a net cash payment to Cecil Bank of $3.3 million, including a premium of approximately $240,000.

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

This section is intended to help potential investors understand our financial performance through a discussion of the factors affecting our consolidated financial condition. This section should be read in conjunction with the consolidated financial statements and accompanying notes.

Overview

Bancorp is the holding company for the Bank. The 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. The Bank does not exercise trust powers, and our regulatory structure is the same as a Maryland-chartered commercial bank. As such, our business has consisted primarily of originating both commercial and real estate loans secured by property in our market area. Typically, commercial real estate and business loans involve a higher degree of risk and carry a higher yield than one-to four-family residential loans. Although we plan to continue to focus on commercial customers, we intend to increase our originations of one-to four-family residential mortgage loans going forward, increasing our portfolio of mortgage lending and also selling select loans into the secondary markets.

We are headquartered in Ellicott City, Maryland and we consider our primary market area to be Howard County, Anne Arundel County, Baltimore County and Harford County, all in Maryland. Our secondary market area, primarily for commercial lending, includes the Maryland counties of Carroll, Frederick, Montgomery and Prince George's as well as Baltimore City. 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. We call it Hands-On Service.

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, business development, 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 law, regulations or government policies may materially affect our financial condition and results of operations.

Total assets increased by over $65.2 million or 16.2% when comparing September 30, 2013 assets of $466.9 million to the $401.7 million at December 31, 2012. Total loans and leases outstanding of $401.5 million at the end of September 2013, showed an increase of $79.3 million or 24.6% compared to total loans of $322.2 million on December 31, 2012. Total deposits grew by $45.0 million or 14.3% when comparing September 30, 2013 to December 31, 2012. These increases reflect our acquisition of our new Aberdeen branch from Cecil Bank, which added $37.1 million in loans and $35.2 million in deposits, during the third quarter of 2013. Additionally, in the first quarter of 2013, the Bank initiated an investment of $8.0 million in bank owned life insurance ("BOLI").

For the nine months ended September 30, 2013 net income was $1.4 million, which represents an increase of 18.8% over net income for the same period of 2012. Net interest income for the nine months ended September 30, 2013 was $11.4 million versus $10.0 million for the first nine months of 2012, an increase of approximately $1.4 million or 14.7%. Total noninterest income was $549 thousand for the first nine months of 2012, compared to $962 thousand for the same period in 2013. Noninterest income during the 2012 period was negatively impacted by a $131 thousand loss on sale of OREO, while there was a similar loss of only $37 thousand in 2013. Noninterest income during the nine months ended September 30, 2013 also benefited from $210 thousand in income generated from the 2013 initiation of the BOLI program. Total noninterest expenses increased by $1.7 million from $7.8 million for the nine months ended September 30, 2012 to $9.5 million for the same period in 2013. Nearly $1.0 million if this increase was due to additional compensation costs as we continue to expand our staff to support our continued growth initiatives.

We are proceeding with the design and construction of our first Baltimore County, MD branch along with a regional office to be located in Towson, MD, which we expect will open in the fourth quarter of 2013

Critical Accounting Policies

Our accounting and financial reporting policies conform to GAAP and general practice within the banking industry. Accordingly, the financial statements require management to exercise significant judgment or discretion or make significant assumptions 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. We consider the allowance for credit losses to be our most significant accounting policy, which is further described in the notes to the financial statements.

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 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.

Identifiable intangible assets consist of core deposit intangibles acquired in our branch office acquisition. The core deposit intangible asset represents the excess of the fair value of liabilities assumed over the fair value of tangible assets acquired in the Aberdeen branch acquisition. This intangible asset is amortized on an accelerated basis over an original life of approximately ten years. Bancorp reviews its intangible assets periodically for impairment. If such impairment is indicated, impairment is recognized by accelerating the amortization of the asset to the extent that the carrying value exceeds the estimated fair value.

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Balance Sheet Analysis and Comparison of Financial Condition

A comparison between September 30, 2013 and December 31, 2012 balance sheets is presented below.

Assets

Total assets increased $65.2 million, or 16.2%, to $466.9 million at September 30, 2013 compared to $401.7 million at December 31, 2012. This asset growth was primarily due to a $79.3 million growth in total loans and leases, partially offset by decreases of $16.9 million in cash and cash equivalents and $5.7 million in investment securities. In addition to the organic loan growth, total assets were enhanced from the Bank's purchase of nearly $37.1 million of loans in the Aberdeen branch acquisition. The asset growth was funded primarily from increases in customer deposits, which increased from $314.9 million at December 31, 2012 to $359.9 million at September 30, 2013, an increase of $45.0 million or 14.3%. A large contributor to the deposit growth was the approximately $35 million in additional deposits we acquired in the Aberdeen branch acquisition.

Securities Available for Sale

We currently hold both U.S. agency securities and mortgage backed securities in our securities portfolio, all of which are categorized as available for sale. Our securities portfolio is used 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, 2013 and December 31, 2012 we held an investment in stock of the Federal Home Loan Bank of Atlanta ("FHLB") of $1.9 million and $1.5 million, respectively. This investment is required for continued FHLB membership, and is based partially upon the dollar 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.

	September 30, 2013		December 31, 2012	
(in thousands)	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
U.S. Federal agencies	$ 21,007	$ 21,009	$ 26,526	$ 26,540
Mortgage-backed	184	196	314	335
Total	$ 21,191	$ 21,205	$ 26,840	$ 26,875

We had securities available for sale of $21.2 million and $26.9 million at September 30, 2013 and December 31, 2012, respectively, which were recorded at fair value. This represents a decrease of $5.7 million, or 21.1%, from the prior year end. The decrease in our securities was used to fund the $8.0 million BOLI program, while maintaining an appropriate amount of securities to collateralize our repurchase agreements at September 30, 2013. We did not record any gains or losses on the sales or calls of securities or mortgage backed securities in any of the periods presented.

With respect to our total portfolio of securities available for sale, we held certain securities that had unrealized losses of less than $1 thousand at both September 30, 2013 and December 31, 2012. The minimal 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 $79.3 million or 24.6%, to $401.5 million at September 30, 2013 from $322.2 million at December 31, 2012. At September 30, 2013, total loans were 86.0% of total assets, up from 80.2% of total assets at December 31, 2012. Over the last several years, loan growth throughout the banking industry has been impacted by decreased loan demand resulting from uncertain economic conditions. As the economy in our market area has started to gradually improve so has demand for certain types of credit, especially commercial real estate, commercial and construction loans.

The following table sets forth the composition of our loan portfolio at the dates indicated. We had loans held for sale of $0.8 million at September 30, 2013, and $1.6 million at December 31, 2012.

(in thousands)	September 30, 2013	% of Total	December 31, 2012	% of Total
Real estate				
Construction and land	$ 49,390	12.3 %	$ 37,963	11.8 %
Residential - first lien	36,149	9.0	29,826	9.3
Residential - junior lien	8,244	2.1	7,983	2.5
Total residential real estate	44,393	11.1	37,809	11.7
Commercial - owner occupied	89,008	22.1	61,119	19.0
Commercial - non-owner occupied	116,306	29.0	96,223	29.9
Total commercial real estate	205,314	51.1	157,342	48.8
Total real estate loans	299,097	74.5	233,114	72.3
Commercial loans and leases	101,463	25.3	87,844	27.3
Consumer	948	0.2	1,260	0.4
Total loans	$ 401,508	100.0 %	$ 322,218	100.0 %

Deposits

Our deposits increased from $314.9 million at December 31, 2012 to $359.9 million at September 30, 2013, an increase of $45.0 million or 14.3%. The increase resulted primarily from purchased deposits of $35.2 million in the Aberdeen branch acquisition. The largest increase was in certificates of deposit, which increased from $110.8 million at December 31, 2012 to $150.0 million at September 30, 2013, an increase of $39.2 million or 35.4%. In addition, interest bearing money market accounts increased $9.8 million from December 31, 2012 to September 30, 2013. Partially offsetting this growth was a decrease in transaction deposits, interest and noninterest bearing, from $122.1 million at December 31, 2012 to $116.4 million at September 30, 2013, a decline of $5.7 million or 4.7%. This transaction deposit decline is attributable primarily to one commercial customer that made a large deposit (in excess of $10 million) in December 2012 of cash received from the sale of a business and subsequently transferred these funds out of the Bank in January 2013.

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

	September 30, 2013		December 31, 2012	
(dollars in thousands)	Amount	% of Total	Amount	% of Total
Noninterest-bearing demand	$ 91,189	25 %	$ 95,875	30 %
Interest-bearing checking	25,180	7	26,209	8
Money market accounts	80,657	22	70,856	23
Savings	12,823	4	11,107	4
Certificates of deposit $100,000 and over	96,969	27	77,759	25
Certificates of deposit under $100,000	53,070	15	33,052	10
Total deposits	$ 359,888	100 %	$ 314,858	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”) and FHLB advances. Our borrowings totaled $57.9 million at September 30, 2013 and $39.0 million at December 31, 2012. Short-term borrowings totaled $40.0 million at September 30, 2013 and $27.0 million at December 31, 2012. We had seven long-term FHLB advances outstanding totaling $18.0 million at September 30, 2013 compared to nine FHLB advances outstanding totaling $12.0 million at December 31, 2012.

Shareholders' Equity

Total shareholders' equity increased by $1.3 million, or approximately 2.8%, from $46.7 million at December 31, 2012 to $48.0 million at September 30, 2013. The increase in shareholders' equity is the result of the retention of the earnings for the nine months of 2013.

Total shareholders' equity at September 30, 2013 represents a capital to asset ratio of 10.29%, while the total shareholders' equity at December 31, 2012 represents a capital to asset ratio of 11.63%. Even though capital levels increased, the overall growth in asset levels resulted in a decline in the capital to asset ratio.

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.

	For the nine months ended September 30,		
	2013			2012		
(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	$ 90,880	$ 3,308	4.87 %	$ 79,080	$ 3,226	5.45 %
Commercial real estate	171,569	6,407	4.99	131,227	5,412	5.51
Construction and land	42,044	1,617	5.14	38,107	1,544	5.41
Residential real estate	39,325	1,336	4.54	31,138	1,147	4.92
Consumer	1,133	44	5.23	1,679	57	4.53
Total loans and leases	344,951	12,713	4.93	281,231	11,386	5.41
Federal funds sold	21,648	35	0.22	27,827	46	0.22
Securities: [2]						
U.S Gov agencies	15,365	21	0.18	21,835	39	0.24
Mortgage-backed	266	9	4.57	504	17	4.51
Other investments	1,680	27	2.12	1,190	18	2.02
Total securities	17,311	57	0.44	23,529	74	0.42
Total earning assets	383,910	12,805	4.46	332,587	11,506	4.62
Cash and due from banks	4,812			3,690		
Bank premises and equipment, net	9,589			9,664		
Other assets	14,445			6,445		
Less: allowance for credit losses	(2,943)			(3,269)		
Total assets	$ 409,813			$ 349,117		
Interest-bearing liabilities						
Deposits:						
Interest-bearing demand accounts	$ 24,916	$ 51	0.27 %	$ 17,678	$ 48	0.36 %
Money market	76,148	241	0.42	64,321	280	0.58
Savings	12,131	33	0.37	11,576	47	0.54
Time deposits $100,000 and over	58,491	524	1.20	61,815	554	1.20
Other time deposits	64,575	359	0.74	51,747	442	1.14
Total interest-bearing deposits	236,261	1,208	0.68	207,137	1,371	0.88
Short-term borrowings	23,578	83	0.47	23,303	125	0.72
Long-term borrowings	16,029	90	0.75	7,248	53	0.98
Total interest-bearing funds	275,868	1,381	0.67	237,688	1,549	0.87
Noninterest-bearing deposits	85,517			71,018		
Other liabilities and accrued expenses	928			842		

Total liabilities	362,313					309,548			
Shareholders' equity	47,500					39,569			
Total liabilities & shareholders' equity	$ 409,813					$ 349,117			
Net interest rate spread [3]		$ 11,424	3.79	%			$ 9,957	3.75	%
Effect of noninterest-bearing funds			0.19					0.25	
Net interest margin on earning assets [4]			3.98	%				4.00	%

(1) Loan fee income is included in the interest income calculation, and nonaccrual loans are included in the average loan base upon which the interest rate earned on loans is calculated.
(2) Available for sale securities 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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	For the three months ended September 30,							
	2013				2012			
(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	$ 96,927	$ 1,203	4.92	%	$ 81,412	$ 1,084	5.30	%
Commercial real estate	189,024	2,368	4.97		136,046	1,861	5.44	
Construction and land	43,936	566	5.11		37,577	509	5.39	
Residential real estate	41,875	477	4.52		31,296	381	4.84	
Consumer	951	13	5.60		1,615	19	4.68	
Total loans and leases	372,713	4,627	4.92		287,946	3,854	5.32	
Federal funds sold	22,469	12	0.21		25,944	15	0.23	
Securities: [2]								
U.S. Gov agencies	14,660	4	0.10		29,198	18	0.25	
Mortgage-backed	211	2	4.53		434	5	4.58	
Other investments	1,925	10	2.12		1,051	6	2.27	
Total securities	16,795	16	0.39		30,683	29	0.38	
Total earning assets	411,977	4,655	4.48		344,573	3,898	4.50	
Cash and due from banks	5,018				3,762			
Bank premises and equipment, net	9,842				9,740			
Other assets	15,013				6,244			
Less: allowance for credit losses	(3,056)				(2,831)			
Total assets	$ 438,795				$ 361,488			
Interest-bearing liabilities								
Deposits:								
Interest-bearing demand accounts	$ 24,643	$ 16	0.25	%	$ 17,887	$ 13	0.29	%
Money market	79,169	68	0.34		65,418	77	0.47	
Savings	12,406	9	0.27		12,164	13	0.43	
Time deposits $100,000 and over	64,498	192	1.18		60,557	182	1.20	
Other time deposits	76,414	138	0.72		50,737	147	1.15	
Total interest-bearing deposits	257,130	422	0.65		206,763	432	0.83	
Short-term borrowings	25,695	26	0.40		26,341	40	0.60	
Long-term borrowing	21,957	49	0.88		6,000	14	0.93	
Total interest-bearing funds	304,782	497	0.65		239,104	486	0.81	
Noninterest-bearing deposits	85,073				77,122			
Other liabilities and accrued expenses	939				708			
Total liabilities	390,793				316,934			
Shareholders' equity	48,001				44,554			
Total liabilities & shareholders' equity	$ 438,795				$ 361,488			
Net interest rate spread [3]		$ 4,158	3.84	%		$ 3,412	3.69	%
Effect of noninterest-bearing funds			0.17				0.25	

Net interest margin on earning assets [4]	4.00 %	3.94 %

(1) Loan fee income is included in the interest income calculation, and nonaccrual loans are included in the average loan base upon which the interest rate earned on loans is calculated.
(2) Available for sale securities 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.

	For the nine months ended September 30, 2013 vs. 2012			For the three months ended September 30, 2013 vs. 2012		
	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	$ 82	$ (459)	$ 541	$ 119	$ (304)	$ 423
Commercial real estate	995	(674)	1,669	507	(643)	1,150
Construction and land	73	(103)	176	57	(103)	160
Residential real estate	189	(117)	306	96	(102)	198
Consumer	(12)	12	(24)	(6)	15	(21)
Taxable securities	(17)	5	(22)	(13)	1	(14)
Federal funds sold	(11)	(1)	(10)	(3)	(5)	2
Interest-bearing deposits in other banks	-	-	-	-	-	-
Total interest income	1,299	(1,337)	2,636	757	(1,141)	1,898
Interest paid on:						
Savings deposits	(13)	(20)	7	(5)	(19)	14
Checking plus interest deposits	3	(16)	19	3	(6)	9
Money market accounts	(39)	(101)	62	(9)	(84)	75
Time deposit $100,000 and over	(30)	0	(30)	10	(9)	19
Other time deposits	(83)	(205)	122	(9)	(221)	212
Short-term borrowings	(42)	(57)	15	(14)	(53)	39
Long-term borrowing	37	(16)	53	35	(3)	37
Total interest expense	(168)	(415)	248	11	(395)	404
Net interest earned	$ 1,467	$ (922)	$ 2,388	$ 746	$ (746)	$ 1,492

(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, 2013 and September 30, 2012 is presented below.

General

Net income available to common shareholders increased $559 thousand, or 78.6%, to $1.3 million for the nine months ended September 30, 2013 compared to net income of $.7 million for the nine months ended September 30, 2012. This increase was primarily due to an increase in net income arising from increases of $1.5 million or 14.7% in net interest income and $413 thousand in noninterest income as well as a $337 thousand, or 71.6%, decrease in dividends paid on preferred stock due to a reduction in the dividend rate which is attributable to meeting growth thresholds in certain loan categories defined under the SBLF program. These positive effects were partially offset by a $1.7 million or 21.2% increase in non-interest expenses.

Interest Income

Interest income increased $1.3 million, or 11.3%, to $12.8 million for the nine months ended September 30, 2013 compared to $11.5 million for the same period in 2012. The increase was primarily due to a $1.3 million or 11.7%, increase in interest and fees on loans. The increase in interest income on loans was due to a 22.7% increase in the average balance during the nine months ended September 30, 2013 compared to the nine months ended September 30, 2012, partially offset by a decrease in the average yield on such loans despite an improvement in the mix of loans towards higher-yielding loan products. Interest income from our other sources of interest income, our securities portfolio and our federal funds sold during this same period declined $28 thousand or 23.3% primarily as a result of lower average balances in both these categories.

Interest Expense

Interest expense decreased $168 thousand, or 10.9%, to $1.4 million for the nine months ended September 30, 2013, compared to $1.5 million for the same period in 2012. Even though we were able to grow interest bearing sources of funds on average by $29.1 million or 14.1% for the first nine months of 2013 compared to the first nine months of 2012, total interest expense decreased as the average rates paid on deposits and borrowings decreased from .88% to .68% when comparing the two periods, primarily as a result of a continuing shift in the composition of our deposits towards lower cost deposit products.

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 $1.5 million, or 14.7%, during the nine months ended September 30, 2013 compared to the nine months ended September 30, 2012. As noted above, the increase in net interest income was due to an increase of $1.3 million, or 11.3%, in interest income and a reduction of $0.2 million or 10.9% 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 $666 thousand for the nine months ended September 30, 2013 compared to $650 thousand for the same period in 2012, an increase of $16 thousand. The provision reflects both a general provision that is required given our continued growth in the size of the loan portfolio, as well as a specific provision required on loans individually evaluated and deemed to be impaired. The $666 thousand provision for the first nine months of 2013 represented an increase in specific provisions required on loans individually evaluated for impairment of $524 thousand, an additional $142 thousand for loans collectively evaluated due to growth in the loan portfolio for the first nine month of 2013.

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 Federal Deposit Insurance Corporation (“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 $962 thousand for the nine months ended September 30, 2013 compared to $549 thousand for the nine months ended September 30, 2012, a $413 thousand or 75.2% increase. This increase was primarily a result of the Bank initiating a BOLI program in January 2013, as well as an increase in gain on the sale of loans and a decrease in loss on the sale of other real estate owned. The BOLI program generated $210 thousand of income during the first nine months of 2013; there was no such income in the first nine months of 2012. Our heightened focus on mortgage banking activities and broadening the secondary market investor base led to increased revenue derived from mortgage banking activities of $85 thousand or 76.8% for the first nine months of 2013 compared to the same period in 2012. The Bank sold one property held in the other real estate owned (“OREO”) portfolio in the first nine months of 2013 at a loss of $37 thousand compared to the sale of one property sold in the same period of 2012 at a loss of $131 thousand. Other operating income consists mainly of certain loan fees comprised of letters of credit fees, late fees and other assessed loan fees and non-depository account fees such as electronic banking fees, which consist of merchant card processing fees, foreign ATM fees and check card fees, and various other sources. Other operating income slightly decreased by $15 thousand or 4.5% in the nine month period ended September 30, 2013 compared to the same period in 2012 primarily as a result of a $50 thousand one time pre-payment penalty collected on a single commercial relationship in 2012, partially offset by an increase in revenues from merchant card and ATM activity of $16.0 thousand and $12.9 thousand, respectively.

Noninterest Expenses

Noninterest expenses increased $1.7 million or 21.2%, to $9.5 million for the nine months ended September 30, 2013 from $7.8 million for the nine months ended September 30, 2012. The increase was primarily due to an increase in salaries and employee benefits expenses resulting from the continuing growth of our business development initiatives, branch expansion efforts, and additional support personnel. Salaries and employee benefits increased $969 thousand or 22.6% in the first nine months of 2013 compared to the same period in 2012. Full time equivalent employees increased nearly 20% as the Bank has expanded its mortgage banking team including a highly seasoned executive management member and also additional business development officers focused on our expansion through the greater Baltimore market, in addition to additional back office support and normal merit increases. Occupancy costs remained relatively unchanged period over period, but are expected to increase as the Bank continues with its anticipated Baltimore expansion including the ongoing impact of our recently acquired Aberdeen branch and the anticipated opening of our Towson location. Professional fees increased $189 thousand or 42.6% primarily as a result of additional legal costs related to both our above-mentioned branch expansion and cost associated with SEC compliance matters. Further increasing these expenses was a valuation allowances for an OREO property of $347 thousand required during the 2013 period, compared to a $48 thousand provision during the nine months ended September 30, 2012.

Net Income Available to Common Shareholders

Net income available to common shareholders during the nine months ended September 30, 2013 increased $559 thousand or 78.6% to $1.3 million compared to $0.7 million during the nine months ended September 30, 2012, as a result of the above factors and a $337 thousand, or 71.6%, decrease in preferred stock dividends. Preferred stock dividends were lower during the 2013 period because of a reduction in the dividend rate paid on our SBLF Preferred Stock given the growth in applicable loan categories in accordance with the terms of the program. As of September 30, 2013, given the growth in applicable loan categories the dividend rate now stands at the minimum rate of 1.00%. The average dividend rate we paid on the preferred stock decreased to 1.42% during the nine months ended September 30, 2013 compared to 3.75% during the nine months ended September 30, 2012.

A comparison between the three months ended September 30, 2013 and September 30, 2012 is presented below.

General

Net income available to common shareholders increased $145 thousand, or 62.8%, to $376 thousand for the three months ended September 30, 2013 compared to $231 thousand for the three months ended September 30, 2012. This increase was due to a decrease in preferred stock dividends and an increase in net income during the 2013 period. Net income increased $19 thousand when comparing net income of $407 thousand for the three months ended September 30, 2013 to net income of $388 thousand for the same period of 2012. In addition, the dividends we paid on our outstanding preferred stock decreased $126 thousand during the first nine months of 2013 compared to the same period of 2012 due to the reduction in the dividend rate in accordance with the terms of the SBLF program, as discussed above.

Interest Income

Interest income increased $757 thousand, or 19.4%, to $4.7 million for the three months ended September 30, 2013 compared to $3.9 million for the same period in 2012. The increase was primarily due to a $773 thousand, or 20.1%, increase in interest income on loans. The increase in interest income on loans was due to a 29.4% increase in the average balance of the loan portfolio compared to the three months ended September 30, 2012, partially offset by a decrease in the average yield. Partially offsetting the increase in loan interest was a decline in interest income on investment securities and other interest income, consisting of federal funds sold, which decreased $16 thousand or

23.3% over the same period in 2012, primarily as a result of a $17.4 million or 30.7% decrease in the average balance of these interest earning assets.

Interest Expense

Interest expense slightly increased $11 thousand, or 2.3%, to $497 thousand for the three months ended September 30, 2013, compared to $486 thousand for the same period in 2012, primarily as a result of a $21 thousand increase in borrowing expense partially offset by a $10 thousand decrease in interest paid on deposits during the 2013 period compared to the three months ended September 30, 2012. The average balance of our long-term borrowings during the three months ended September 30, 2013 increased $16 thousand, or 266.0%, to $22 thousand compared to $6 thousand during the same period in 2012. This increase in average balances was partially offset by decreases in the average interest rate we paid on short- and long-term borrowings during the 2013 period compared to the three months ended September 30, 2012. Interest paid on deposits decreased during the three months ending September 30, 2013 versus the same period in 2012 because the average rate paid on interest-bearing deposits decreased to 0.65% during the three months ended September 30, 2013 from 0.83% during the same period of 2012. This decrease was partially offset by increases of 24.4% in the average balance of interest-bearing deposits during the three months ended September 30, 2013 compared to the same period of the prior year. By comparison, noninterest bearing balances grew only $8.0 million on average during the 2013 period compared to the same period in 2012.

Net Interest Income

Net interest income increased $746 thousand, or 21.9%, during the three months ended September 30, 2013 compared to the three months ended September 30, 2012. As noted above, the increase in net interest income was due to an increase of $757 thousand, or 19.4%, in interest income partially offset by an $11 thousand, or 2.3%, increase in interest expense during the three month period.

Provision for Credit Losses

Based on management's evaluation, we had a provision for credit losses of $140 thousand for the three months ended September 30, 2013 compared to $308 thousand for the same period in 2012, a decrease of $168 thousand or 54.5%. The provision for the third quarter of 2013 was primarily due to additional general provisions that were required given the continued growth in the size of our loan portfolio.

Noninterest Income

Noninterest income was $319 thousand for the three months ended September 30, 2013 compared to $216 thousand for the three months ended September 30, 2012, a $103 thousand or 47.7% increase. This increase was primarily due to the $72 thousand of income generated from the BOLI program during the third quarter of 2013; there was no such income in the third quarter of 2012 as we did not make the BOLI investment until January 2013. In addition, service charges on deposit accounts increased $19 thousand quarter over quarter.

Noninterest Expenses

Noninterest expenses increased by $1.0 million or 39.4% to $3.7 million during the three months ended September 30, 2013 compared to $2.7 million the three months ended September 30, 2012. Salaries and employee benefits increased $414 thousand or 27.8% quarter over quarter primarily as a result of the previously mentioned continuing growth of our business development initiatives, branch expansion efforts, and the hiring of additional support personnel. Professional fees increased $112 thousand as a result of legal costs associated with strategic growth initiatives and SEC compliance matters. Additionally, provision for OREO, which results from a lower valuation on one of our properties held, was $347 thousand for the third quarter of 2013, while there was no such provision recorded for the same period of 2012

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.

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The table below sets forth the amounts and categories of our nonperforming assets, which consist of nonaccrual 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, 2013			December 31, 2012		
Non-accrual loans:						
Real estate loans:						
Construction and land	$	-		$	432	
Residential - First Lien		-			442	
Residential - Junior Lien		-			-	
Commercial		373			384	
Commercial and leases		3,010			1,143	
Consumer		-			-	
Total non-accrual loans		3,383			2,401	
Troubled debt restructure loans:						
Real estate loans:						
Commercial		-			-	
Residential - First Lien		-			-	
Commercial		-			-	
Total troubled debt restructure loans		-			-	
Total non-performing loans		3,383			2,401	
Other real estate owned:						
Land		595			595	
Commercial		1,782			2,130	
Residential		-			178	
Total other real estate owned		2,377			2,903	
Total non-performing assets	$	5,760		$	5,304	
Ratios:						
Non-performing loans to total gross loans		0.84	%		0.75	%
Non-performing assets to total assets		1.23	%		1.32	%

Included in total non-accrual loans above are seven trouble debt restructured loans totaling $1.2 million that were not performing in accordance with the modified terms, and the accrual of interest has ceased. There were two commercial real estate credits totaling $417 thousand and three commercial credits totaling $457 thousand that were 90 days or more past due and still accruing interest at September 30, 2013. At December 31, 2012 there were two residential loans totaling $249 thousand 90 days or more past due and still accruing interest.

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 $5.8 million, or 1.23% of total assets, at September 30, 2013 compared to $5.3 million or 1.32% of total assets at December 31, 2012. Total nonperforming assets increased by $457 thousand during 2013, while OREO decreased by $525 thousand with the sale of one commercial property for a loss on sale of $37 thousand and an additional provision of $347 thousand on another commercial property. Non-accrual loans increased $982 thousand or 40.9% primarily as a result of three credits to one customer totaling $1.9 million being placed on non-accrual in the second quarter of 2013. Partially offsetting this increase in non-accrual loans were reductions in non-accrual loans from the sale of two residential first mortgage loans totaling $442 thousand and one land loan totaling $432 thousand being was returned to accrual status.

The composition of our nonperforming loans at September 30, 2013 is further described below:

- Six commercial loans to a local business totaling $0.88 million. Most of these loans have an SBA guarantee, and reserves have been taken to reflect the amount expected to be received once claims are submitted to the SBA.
- Eight small commercial loans totaling approximately $0.23 million to borrowers that are in various stages of collection. Each relationship is independently evaluated, and no losses are anticipated from these eight loans.
- One commercial real estate loan for $0.37 million, which is guaranteed by a local business and is also secured by the assets of the business. A specific reserve has been established and based upon current valuations, no further losses are anticipated.
- Three commercial loans to one customer totaling $1.9 million which were placed in non-accrual during the second quarter of 2013, of which one loan for $1.6 million carries a partial SBA guarantee. A specific reserve has been established on each loan and based upon a settlement offer that is under evaluation, no further losses are anticipated.

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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 impaired. 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 by 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 nonaccrual 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.

As of September 30, 2013 and December 31, 2012, impaired loans amounted to $6.5 million and $5.6 million, respectively. The amount of impaired loans requiring specific reserves totaled $2.9 million and $1.8 million, respectively. The amount of impaired loans with no specific valuation allowance totaled $3.6 million and $3.8 million, respectively.

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, 2013	2012	Three months ended September 30, 2013	2012
Balance at beginning of period	$ 2,764	$ 3,433	$ 2,951	$ 3,076
Charge-offs:				
Real estate				
Construction and land loans	-	-	-	-
Residential first lien loans	(183)	(23)	-	-
Residential junior lien loans	-	(44)	-	-
Commercial owner occupied loans	-	-	-	-
Commercial non-owner occupied loans	(2)	(268)	(2)	(268)
Commercial loans and leases	(202)	(1,130)	-	(463)
Consumer loans	-	(15)	-	-
	(387)	(1,480)	(2)	(731)
Recoveries:				
Real estate				
Construction and land loans	-	-	-	-
Residential first lien loans	-	-	-	-
Residential junior lien loans	-	-	-	-
Commercial owner occupied loans	-	-	-	-
Commercial non-owner occupied loans	30	63	-	63
Commercial loans and leases	72	65	56	16
Consumer loans	-	2	-	1
	102	130	56	80
Net recoveries (charge-offs)	(285)	(1,350)	54	(651)
Provision for credit losses	666	650	140	308
Balance at end of period	$ 3,145	$ 2,733	$ 3,145	$ 2,733

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, 2013 Amount	Percent [1]	December 31, 2012 Amount	Percent [1]
Real estate				
Construction and land loans	$ 107	12.3 %	$ 127	11.8 %
Residential first lien loans	159	9.0	204	9.2
Residential junior lien loans	22	2.1	22	2.5
Commercial owner occupied loans	580	22.2	650	19.0
Commercial non-owner occupied loans	774	29.0	505	29.8
Commercial loans and leases	1,490	25.3	1,227	27.3

Consumer loans		13	0.2		29	0.4
Total	$	3,145	100.0 %	$	2,764	100.0 %

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

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, 2013 and December 31, 2012. 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, 2013 and December 31, 2012, cash and cash equivalents totaled $19.4 million and $36.4 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, 2013 and December 31, 2012, we had $84.2 million and $74.6 million, respectively, in loan commitments outstanding, including commitments issued to originate loans of $50.7 million and $34.1 million at September 30, 2013 and December 31, 2012, respectively, and $33.5 million and $40.5 million in unused lines of credit to borrowers at September 30, 2013 and December 31, 2012, respectively. In addition to commitments to originate loans and unused line of credits we had $8.7 million and $6.2 million in letters of credit at September 30, 2013 and December 31, 2012, respectively. Certificates of deposit due within one year of September 30, 2013 totaled $85.0 million, or 23.6% 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, 2013 cash was utilized by net loan growth of $79.6 million, while for the nine months ended September 30, 2012 cash was used to fund net loan growth totaling $25.4 million. Due to the amount of maturities of our investments exceeding new investments, we had net cash provided by investing activities of $5.6 million in 2013 while in 2012 we used $22.6 million in cash outlays to grow the securities portfolio.

Financing activities consist primarily of activity in deposit accounts and FHLB advances. We experienced a net increase in deposits of $45.0 million during the nine months ended September 30, 2013. 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, including growth via acquisition.

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 $40 million at September 30, 2013 compared to $26 million at December 31, 2012. At September 30, 2013, we had the ability to borrow up to a total of $82.9 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, 2013 and December 31, 2012, 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 which would have a material effect on us.

Outstanding loan commitments and lines of credit at September 30, 2013 and December 31, 2012 are as follows:

(in thousands)	September 30, 2013	December 31, 2012
Unfunded loan commitments	$ 50,687	$ 34,057
Unused lines of credit	33,470	40,493
Letters of credit	8,647	6,178

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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, 2013 or December 31, 2012 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, 2013. 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, 2013, 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, 2012, as filed with the SEC on March 27, 2013.

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

Our registration statement on Form S-1, File Number 333-178204, with respect to our initial public offering of our common stock, was declared effective by the SEC on May 14, 2012. We sold a total of 1,396,364 shares of common stock in our initial public offering for aggregate gross proceeds of $10.2 million.

After expenses, we raised net proceeds of approximately $9.0 million in the public offering. During the third quarter we provided $8.5 million of the proceeds to the Bank to increase its capital levels in order to support the continued growth of the Bank.

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 12, 2013 Date	/s/ Mary Ann Scully MARY ANN SCULLY PRESIDENT AND CEO
November 12, 2013 Date	/s/ George C. Coffman GEORGE C. COFFMAN EVP AND CFO

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