

Howard Bancorp Inc
Form 10-Q
November 14, 2016

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2016

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

(State or other jurisdiction of incorporation or organization)

20-3735949

(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 No

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

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

The number of outstanding shares of common stock outstanding as of October 31, 2016.

Common Stock, \$0.01 par value – 6,991,072 shares

HOWARD BANCORP, INC.

TABLE OF CONTENTS

	Page
PART I <u>Financial Information</u>	4
Item 1. <u>Financial Statements</u>	4
<u>Consolidated Balance Sheets (Unaudited)</u>	4
<u>Consolidated Statements of Operations (Unaudited)</u>	5
<u>Consolidated Statements of Comprehensive Income (Unaudited)</u>	6
<u>Consolidated Statements of Changes in Shareholders' Equity (Unaudited)</u>	6
<u>Consolidated Statements of Cash Flows (Unaudited)</u>	7
<u>Notes to Consolidated Financial Statements (Unaudited)</u>	8
Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	31
Item 3. <u>Quantitative and Qualitative Disclosure about Market Risk</u>	46
Item 4. <u>Controls and Procedures</u>	46
PART II <u>Other Information</u>	47
Item 1. <u>Legal Proceedings</u>	47
Item 1A. <u>Risk Factors</u>	47
Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	47
Item 3. <u>Defaults Upon Senior Securities</u>	47
Item 4. <u>Mine Safety Disclosures</u>	47
Item 5. <u>Other Information</u>	47
Item 6. <u>Exhibits</u>	47
<u>Signatures</u>	48

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

This report contains forward-looking statements, which can be identified by the use of words such as “estimate,” “project,” “believe,” “intend,” “anticipate,” “plan,” “seek,” “expect,” “will,” “may,” “should” and words of similar meaning. You can 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 with respect to our business plan and strategies, including continuing to focus on commercial customers, continuing to increase our originations of one-to four-family residential mortgage loans, increasing our mortgage lending portfolio and selling loans into the secondary markets;
- statements regarding the asset quality of our investment portfolios and anticipated recovery and collection of unrealized losses on securities available for sale;
- statements with respect to our allowance for credit losses, and the adequacy thereof;
- statement with respect to having adequate liquidity levels;
- our belief that we will retain a large portion of maturing certificates of deposit;
- the expected impact of recent accounting pronouncements; and
- future cash requirements and lack of expected losses relating to commitments to extend credit.

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

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

- deterioration in general economic conditions, either nationally or in our market area, or a return to recessionary conditions, including as a result of the impact of the impending exit of the United Kingdom from the European Union;
- 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;

Edgar Filing: Howard Bancorp Inc - Form 10-Q

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;
loss of key personnel; and
other risks discussed in this report, in our annual report on Form 10-K for the year ended December 31, 2015, as filed with the SEC, and in other reports we may file.

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

PART I**Item 1. Financial Statements****Howard Bancorp, Inc. and Subsidiary****Consolidated Balance Sheets**

(in thousands, except share data)	Unaudited September 30, 2016	December 31, 2015
ASSETS		
Cash and due from banks	\$ 33,553	\$ 31,818
Federal funds sold	10,325	6,522
Total cash and cash equivalents	43,878	38,340
Interst bearing deposits with banks	19,513	-
Securities available-for-sale, at fair value	37,718	49,573
Nonmarketable equity securities	4,741	4,163
Loans held for sale, at fair value	46,342	49,677
Loans and leases, net of unearned income	816,590	760,002
Allowance for credit losses	(5,634)	(4,869)
Net loans and leases	810,956	755,133
Bank premises and equipment, net	20,287	20,765
Goodwill	603	603
Core deposit intangible	2,384	2,903
Bank owned life insurance	21,208	18,548
Other real estate owned	2,543	2,369
Interest receivable and other assets	4,614	4,685
Total assets	\$ 1,014,787	\$ 946,759
LIABILITIES		
Noninterest-bearing deposits	\$ 183,118	\$ 173,689
Interest-bearing deposits	620,655	573,719
Total deposits	803,773	747,408
Short-term borrowings	93,263	69,121
Long-term borrowings	26,643	29,707
Deferred tax liability	881	1,667
Accrued expenses and other liabilities	5,336	5,957
Total liabilities	929,896	853,860

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 December 31, 2015	-	12,562
Common stock - par value of \$0.01 authorized 10,000,000 shares; issued and outstanding 6,988,180 shares at September 30, 2016 and 6,962,139 at December 31, 2015	70	70
Capital surplus	70,897	70,587
Retained earnings	13,895	9,712
Accumulated other comprehensive income (loss)	29	(32)
Total shareholders' equity	84,891	92,899
Total liabilities and shareholders' equity	\$ 1,014,787	\$ 946,759

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

Consolidated Statements of Operations (unaudited)

(in thousands, except share data)	For the nine months ended September 30,		For the three months ended September 30,	
	2016	2015	2016	2015
INTEREST INCOME				
Interest and fees on loans and leases	\$ 28,592	\$ 23,177	\$ 9,684	\$ 8,405
Interest and dividends on securities	299	179	106	68
Other interest income	98	43	34	16
Total interest income	28,989	23,399	9,824	8,489
INTEREST EXPENSE				
Deposits	2,558	1,866	891	693
Short-term borrowings	380	98	169	43
Long-term borrowings	385	188	116	72
Total interest expense	3,323	2,152	1,176	808
NET INTEREST INCOME	25,666	21,247	8,648	7,681
Provision for credit losses	1,302	1,015	402	230
Net interest income after provision for credit losses	24,364	20,232	8,246	7,451
NONINTEREST INCOME				
Service charges on deposit accounts	501	592	178	189
Realized and unrealized gains on mortgage banking activity	6,984	5,415	2,847	1,910
Gain (loss) on the sale of loans	612	-	(40)	-
Loss on the disposal of furniture, fixtures & equipment	(70)	-	(1)	-
Income from bank owned life insurance	461	278	156	103
Loan fee income	2,631	2,140	997	848
Other operating income	687	619	247	207
Total noninterest income	11,806	9,044	4,384	3,257
NONINTEREST EXPENSE				
Compensation and benefits	14,381	12,441	4,927	4,652
Occupancy and equipment	3,625	2,810	1,062	931
Amortization of core deposit intangible	519	248	166	82
Marketing and business development	2,475	2,093	864	786
Professional fees	1,692	1,080	669	386
Data processing fees	1,273	902	524	348
Merger and restructuring	-	3,303	-	2,166
FDIC Assessment	604	315	199	106
Provision for other real estate owned	83	736	-	736
Loan production expense	2,295	1,534	717	600
Other operating expense	2,470	2,412	752	807
Total noninterest expense	29,417	27,874	9,880	11,600
INCOME (LOSS) BEFORE INCOME TAXES	6,753	1,402	2,750	(892)
Income tax expense (benefit)	2,404	747	1,002	(106)
NET INCOME (LOSS)	\$ 4,349	\$ 655	\$ 1,748	\$ (786)

Edgar Filing: Howard Bancorp Inc - Form 10-Q

Preferred stock dividends	166	94	-	31	
Net income (loss) available to common shareholders	\$ 4,183	\$ 561	\$ 1,748	\$ (817)
NET INCOME (LOSS) PER COMMON SHARE					
Basic	\$ 0.60	\$ 0.09	\$ 0.25	\$ (0.13)
Diluted	\$ 0.59	\$ 0.09	\$ 0.25	\$ (0.13)

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

Consolidated Statements of Comprehensive Income (unaudited)

(in thousands)	For the nine months ended September 30,	
	2016	2015
Net Income	\$ 4,349	\$ 655
Other comprehensive income		
Investments available-for-sale:		
Net unrealized holding gains	94	54
Related income tax expense	(33)	(19)
Comprehensive income	\$ 4,410	\$ 690

(in thousands)	For the three months ended September 30,	
	2016	2015
Net Income (Loss)	\$ 1,748	\$ (786)
Other comprehensive income		
Investments available-for-sale:		
Net unrealized holding gains	6	14
Related income tax expense	(4)	(4)
Comprehensive income (loss)	\$ 1,750	\$ (776)

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

Consolidated Statements of Changes in Shareholders' Equity (unaudited)

(dollars in thousands, except share data)	Preferred stock	Number of shares	Common stock	Capital surplus	Retained earnings	Accumulated other comprehensive income/(loss)	Total
Balances at January 1, 2015	\$12,562	4,145,547	\$ 41	\$38,360	\$8,696	\$ (16)	\$59,643
Net income	-	-	-	-	655	-	655
Net unrealized gain on securities	-	-	-	-	-	35	35
Dividends paid on preferred stock	-	-	-	-	(94)	-	(94)

Edgar Filing: Howard Bancorp Inc - Form 10-Q

Issuance of common stock:							
Stock offering	-	2,173,913	22	23,096	-	-	23,118
Director stock awards	-	5,560	-	72	-	-	72
Business combination	-	560,891	6	8,043	-	-	8,049
Exercise of options	-	21,465	-	217	-	-	217
Stock-based compensation	-	14,002	-	385	-	-	385
Balances at September 30, 2015	\$ 12,562	6,921,378	\$ 69	\$ 70,173	\$ 9,257	\$ 19	\$ 92,080
Balances at January 1, 2016	\$ 12,562	6,962,139	\$ 70	\$ 70,587	\$ 9,712	\$ (32)	\$ 92,899
Net income	-	-	-	-	4,349	-	4,349
Net unrealized gain on securities	-	-	-	-	-	61	61
Dividends paid on preferred stock	-	-	-	-	(166)	-	(166)
Redemption of preferred stock	(12,562)	-	-	-	-	-	(12,562)
Issuance of common stock:							
Director stock awards	-	5,629	-	72	-	-	72
Exercise of options	-	1,740	-	19	-	-	19
Stock-based compensation	-	18,672	-	219	-	-	219
Balances at September 30, 2016	\$-	6,988,180	\$ 70	\$ 70,897	\$ 13,895	\$ 29	\$ 84,891

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

Consolidated Statements of Cash Flows (unaudited)

(in thousands)	Nine months ended	
	2016	2015
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	\$4,349	\$655
Adjustments to reconcile net income to net cash from operating activities:		
Provision for credit losses	1,302	1,015
Deferred income tax benefit	(241)	(2,153)
Provision for other real estate owned	83	736
Depreciation	927	712
Stock-based compensation	291	457
Net amortization of investment securities	(8)	(4)
Net amortization of discount on purchased loans	(592)	(798)
Loss on disposal of furniture, fixtures & equipment	70	-
Net amortization of intangible asset	519	248
Loans originated for sale	(418,828)	(464,584)
Proceeds from sale of loans originated for sale	429,148	448,453
Realized and unrealized gains on mortgage banking activity	(6,984)	(5,415)
Cash surrender value of BOLI	(461)	(278)
Increase in interest receivable	(253)	(433)
Increase in interest payable	19	116
(Increase) decrease in other assets	(270)	235
Decrease in other liabilities	(1,202)	(1,626)
Net cash provided by (used in) operating activities	7,869	(22,664)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Interst bearing deposits with banks	(19,513)	-
Purchases of investment securities available-for-sale	(65,569)	(13,916)
Proceeds from maturities of investment securities available-for-sale	77,526	42,541
Net increase in loans and leases outstanding	(56,789)	(47,547)
Purchase of bank owned life insurance	(2,200)	-
Purchase of premises and equipment	(520)	(4,633)
Acquisition activity, net of cash received	-	8,348
Net cash used in investing activities	(67,065)	(15,207)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net increase in deposits	56,365	13,322
Net increase (decrease) in short-term borrowings	11,580	(1,313)
Proceeds from issuance of long-term debt	21,498	5,451
Repayment of long-term debt	(12,000)	(9,000)
Net proceeds from issuance of common stock, net of cost	19	23,335
Redemption of preferred stock	(12,562)	-
Cash dividends on preferred stock	(166)	(94)

Edgar Filing: Howard Bancorp Inc - Form 10-Q

Net cash provided by financing activities	64,734	31,701
Net increase (decrease) in cash and cash equivalents	5,538	(6,170)
Cash and cash equivalents at beginning of period	38,340	24,517
Cash and cash equivalents at end of period	\$43,878	\$18,347
SUPPLEMENTAL INFORMATION		
Cash payments for interest	\$3,304	\$2,035
Cash payments for income taxes	925	2,690
Transferred from loans to other real estate owned	256	-
Assets acquired in business combination (net of cash received)	-	195,237
Liabilities assumed in business combination	-	204,943

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

Notes to Consolidated Financial Statements (unaudited)

Note 1: Summary of Significant Accounting Policies

Nature of Operations

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

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

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

On May 6, 2016, Bancorp redeemed all of the 12,562 shares of the Series AA Preferred Stock that it had previously issued to the U.S. Department of the Treasury (the “Treasury”) under its Small Business Lending Fund (“SBLF”) program.

The aggregate redemption price of the Series AA Preferred Stock was approximately \$12.7 million, including dividends accrued but unpaid through the redemption date. The redemptions of the Series AA Preferred Stock was funded with variable rate debt with Raymond James Bank, N.A. This debt matures one year from commencement, with interest only payments based upon 30 day LIBOR plus 300 basis points.

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

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

Principles of Consolidation

The consolidated financial statements include the accounts of Bancorp, its subsidiary bank and the bank's subsidiaries. All significant intercompany accounts and transactions have been eliminated. Certain reclassifications have been made to the prior year's consolidated financial statements to conform to current period presentation, but any such reclassifications had no impact on net income or shareholders' equity as previously reported.

Use of Estimates

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

Loans Held-For-Sale

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

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

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

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

New Accounting Pronouncements

The Financial Accounting Standards Board (the "FASB") has issued ASU 2016-15, *Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments*. The amendments in this update provide guidance on eight specific cash flow issues with the objective of reducing the existing diversity in practice. The amendments in this update are effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. The Company is currently evaluating this guidance to determine the impact on its consolidated financial

statements.

The FASB has issued ASU 2016-13, *Financial Instruments—Credit Losses (Topic 326)*. The main objective of this update is to provide financial statement users with more decision-useful information about the expected credit losses on financial instruments and other commitments to extend credit held by a reporting entity at each reporting date. To achieve this objective, the guidance in this update replaces the incurred loss impairment methodology in current GAAP with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to inform credit loss estimates. The measurement of expected credit losses is based on relevant information about past events, including historical experience, current conditions, and reasonable and supportable forecasts that affect the collectability of the reported amount. An entity must use judgment in determining the relevant information and estimation methods that are appropriate in its circumstances. The guidance in this update is effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. The Company is currently evaluating this guidance to determine the impact on its consolidated financial statements.

The FASB has issued ASU 2016-09, *Compensation—Stock Compensation (Topic 718)*. The purpose of this guidance is to simplify the accounting for share-based payment transactions, including the income tax consequences of these transactions. Under the provisions of the update, the income tax consequences of excess tax benefits and deficiencies should be recognized in income tax expense in the reporting period in which the awards vest. Currently, excess tax benefits and deficiencies impact shareholders' equity directly to the extent there is a cumulative excess tax benefit. In the event that a tax deficiency has occurred during the reporting period and a cumulative tax benefit does not exist, the tax deficiency is recognized in income tax expense under current GAAP. The update also provides that entities may continue to estimate forfeitures in accounting for stock based compensation or recognize them as they occur. The provision of this update becomes effective for interim and annual periods beginning after December 15, 2016. The Company is currently evaluating this guidance to determine the impact on its consolidated financial statements.

The FASB has issued ASU 2016-02, *Leases (Topic 842)*. The new guidance requires lessees to recognize lease assets and lease liabilities related to certain operating leases on their balance sheet and disclose key information about leasing arrangements. This guidance is effective for fiscal years beginning after December 15, 2018 and interim periods within those fiscal years. The Company is currently evaluating this guidance to determine the impact on its consolidated financial statements.

The FASB has issued ASU No. 2016-01, *Financial Instruments – Recognition and Measurement of Financial Assets and Liabilities*. ASU No. 2016-01 requires equity investments to be measured at fair value with changes in fair value recognized in net income, excluding equity investments that are consolidated or accounted for under the equity method of accounting. The guidance allows equity investments without readily determinable fair values to be measured at cost minus impairment, with a qualitative assessment required to identify impairment. The guidance also: requires public companies to use exit prices to measure the fair value of financial instruments for disclosure purposes; requires separate presentation of financial assets and financial liabilities by measurement category and form of financial asset on the balance sheet or the accompanying notes to the financial statements; and eliminates the disclosure requirements related to measurement assumptions for the fair value of instruments measured at amortized cost. In addition, the guidance requires that for liabilities measured at fair value under the fair value option, changes in fair value due to changes in instrument-specific credit risk be presented in other comprehensive income. ASU No. 2016-01 is effective for fiscal years beginning after December 15, 2017 and interim periods within those fiscal years. The Company is currently evaluating the impact of adopting the new guidance on its consolidated financial statements.

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

Note 2: Business Combinations

Patapsco Bancorp Acquisition

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

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

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

The following table provides the purchase price as of the acquisition date, the identifiable assets acquired and liabilities assumed at their estimated fair values, and the resulting goodwill of \$603 thousand recorded from the acquisition:

(in thousands)

Purchase Price Consideration	
Cash consideration	\$2,015
Purchase price assigned to shares exchanged for stock	8,049
Total purchase price for Patapsco Bancorp acquisition	\$10,064

Assets acquired at fair value:

Cash and cash equivalents	\$19,047
Investment securities available for sale	26,255
Loans	156,907
Accrued interest receivable	602
Other assets	9,090
Core deposit intangible	1,974
Total fair value of assets acquired	\$213,875

Liabilities assumed at fair value:

Deposits	175,083
Borrowings	17,737
Accrued expenses and other liabilities	11,594
Total fair value of liabilities assumed	\$204,414

Net assets acquired at fair value: \$9,461

Transaction consideration paid to Patapsco Bancorp 10,064

Amount of goodwill recorded from Patapsco Bancorp acquisition \$603

Acquired loans

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

(in thousands)

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

Upon the acquisition of Patapsco Bancorp, the Company recorded all loans acquired at the estimated fair value on the purchase date with no carryover of the related allowance for loan losses. On the acquisition date, the Company

segregated the loan portfolio into two loan pools, performing and non-performing loans to be retained in the Bank's portfolio.

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

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

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

Note 3: Investment Securities

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

(in thousands)	September 30, 2016				December 31, 2015			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
U.S. Government Agencies	\$34,531	\$ 21	\$ 12	\$ 34,540	\$48,467	\$ -	\$ 45	\$ 48,422
Treasuries	1,513	-	-	1,513	-	-	-	-
Mortgage-backed	28	1	-	29	54	3	-	57
Other investments	1,600	36	-	1,636	1,100	-	6	1,094
	\$37,672	\$ 58	\$ 12	\$ 37,718	\$49,621	\$ 3	\$ 51	\$ 49,573

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, 2016 and December 31, 2015 are presented below:

September 30, 2016 (in thousands)	Less than 12 months		12 months or more		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
U.S. Government Agencies	\$ 3,523	\$ 12	\$ -	\$ -	\$3,523	\$ 12
	\$ 3,523	\$ 12	\$ -	\$ -	\$3,523	\$ 12

The portfolio contained three agency securities with unrealized losses of \$12 thousand at September 30, 2016.

December 31, 2015 (in thousands)	Less than 12 months		12 months or more		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
U.S. Government Agencies	\$ 39,431	\$ 45	\$ -	\$ -	\$39,431	\$ 45
Other investments	1,000	6	-	-	1,000	6
	\$ 40,431	\$ 51	\$ -	\$ -	\$40,431	\$ 51

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) the duration and magnitude of the decline in value, (2) the financial condition of the issuer or issuers and (3) the structure of the security.

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

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

(in thousands)	September 30, 2016		December 31, 2015	
	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
Amounts maturing:				
One year or less	\$ 29,499	\$ 29,515	\$ 43,465	\$ 43,425
After one through five years	6,560	6,553	5,002	4,997
After five through ten years	13	14	54	57
After ten years	1,600	1,636	1,100	1,094
	\$ 37,672	\$ 37,718	\$ 49,621	\$ 49,573

There were no sales of investment securities during the nine months ended September 30, 2016. At September 30, 2016 and December 31, 2015, \$18.4 million and \$22.8 million, respectively, in fair value of securities were pledged as collateral for repurchase agreements and public fund deposits. No single issuer of securities, except for U.S. Government agency securities, had outstanding balances that exceeded ten percent of shareholders' equity at September 30, 2016.

Note 4: Loans and Leases

The Bank makes loans to customers primarily in the Greater Baltimore Maryland metropolitan area and surrounding communities. A substantial portion of the Bank'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, 2016 and December 31, 2015 are presented in the following table:

(in thousands)	September 30, 2016			December 31, 2015		
	Legacy	Acquired	Total	Legacy	Acquired	Total
Real estate						
Construction and land	\$ 68,635	\$ 5,490	\$ 74,125	\$ 63,085	\$ 6,300	\$ 69,385
Residential - first lien	114,061	85,058	199,119	89,649	93,339	182,988
Residential - junior lien	22,959	11,369	34,328	15,098	12,379	27,477
Total residential real estate	137,020	96,427	233,447	104,747	105,718	210,465
Commercial - owner occupied	103,553	31,513	135,066	94,392	36,722	131,114

Edgar Filing: Howard Bancorp Inc - Form 10-Q

Commercial - non-owner occupied	150,131	52,944	203,075	122,304	59,057	181,361
Total commercial real estate	253,684	84,457	338,141	216,696	95,779	312,475
Total real estate loans	459,340	186,374	645,713	384,528	207,797	592,325
Commercial loans and leases	135,920	29,901	165,821	124,981	38,443	163,424
Consumer	2,916	2,140	5,056	1,302	2,951	4,253
Total loans	\$598,175	\$218,415	\$816,590	\$510,811	\$249,191	\$760,002

Acquired Impaired Loans

The following table documents changes in the accretable discount on acquired impaired loans during the nine months ended September 30, 2016 and 2015, along with the outstanding balances and related carrying amounts for the beginning and end of those respective periods.

(in thousands)	September 30, 2016	September 30, 2015
Balance at beginning of period	\$ 335	\$ 264
Impaired loans acquired	-	372
Accretion of fair value discounts	(239)	(191)
Balance at end of period	\$ 96	\$ 445

(in thousands)	Contractually Required Payments Receivable	Carrying Amount
At September 30, 2016	\$ 1,741	\$ 1,023
At December 31, 2015	3,105	1,708
At September 30, 2015	4,510	2,097
At December 31, 2014	2,466	1,077

There was not an allowance for credit losses required on acquired impaired loans at either September 30, 2016 or September 30, 2015.

Note 5: Credit Quality Assessment

Allowance for Credit Losses

The following table provides information by the respective loan portfolio segment on the activity in the allowance for credit losses for the three and nine month periods ended September 30, 2016 and 2015:

(in thousands)	September 30, 2016							Total
	Construction and land	Residential first lien	Residential junior lien	Commercial owner occupied	Commercial non-owner occupied	Commercial loans and leases	Consumer loans	
Allowance for credit losses:								
Nine months ended:								
Beginning balance	\$265	\$ 300	\$ 47	\$ 309	\$ 728	\$ 3,094	\$ 126	\$4,869
Charge-offs	(216)	-	-	(191)	) -	(233)	) (15)	(655)
Recoveries	-	-	-	40	4	45	29	118
Provision for credit losses	531	150	40	175	373	18	15	1,302
Ending balance	\$580	\$ 450	\$ 87	\$ 333	\$ 1,105	\$ 2,924	\$ 155	\$5,634
Three months ended:								
Beginning balance	\$448	\$ 365	\$ 70	\$ 578	\$ 841	\$ 3,283	\$ 159	\$5,744
Charge-offs	(216)	-	-	(191)	) -	(167)	) (4)	(578)
Recoveries	-	-	-	40	1	19	6	66
Provision for credit losses	348	85	17	(94)	) 263	(211)	) (6)	402
Ending balance	\$580	\$ 450	\$ 87	\$ 333	\$ 1,105	\$ 2,924	\$ 155	\$5,634

Edgar Filing: Howard Bancorp Inc - Form 10-Q

September 30, 2015

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

The following table provides additional information on the allowance for credit losses at September 30, 2016 and December 31, 2015:

(in thousands)	September 30, 2016							Total
	Construction and land	Residential first lien	Residential junior lien	Commercial owner occupied	Commercial non-owner occupied	Commercial loans and leases	Commercial Consumer loans	
Allowance allocated to:								
Legacy Loans:								
individually evaluated for impairment	\$-	\$-	\$-	\$-	\$-	\$ 1,166	\$-	\$1,166
collectively evaluated for impairment	547	327	62	257	885	1,434	38	3,550
Acquired Loans:								
individually evaluated for impairment	-	-	-	-	-	113	72	185
collectively evaluated for impairment	33	123	25	76	220	211	45	733
Loans:								
Legacy Loans:								
Ending balance	\$68,635	\$ 114,061	\$ 22,959	\$ 103,553	\$ 150,131	\$ 135,920	\$ 2,916	\$598,175
individually evaluated for impairment	-	509	-	474	2,667	10,539	-	14,189
collectively evaluated for impairment	68,635	113,552	22,959	103,079	147,464	125,381	2,916	583,986
Acquired Loans:								
Ending balance	5,490	85,058	11,369	31,513	52,944	29,901	2,140	218,415
individually evaluated for impairment	413	248	28	486	481	2,250	140	4,046
collectively evaluated for impairment	5,077	84,810	11,341	31,027	52,463	27,651	2,000	214,369

(in thousands)	December 31, 2015							Total
	Construction and land	Residential first lien	Residential junior lien	Commercial owner occupied	Commercial non-owner occupied	Commercial loans and leases	Commercial Consumer loans	

Edgar Filing: Howard Bancorp Inc - Form 10-Q

Allowance for credit losses:								
Legacy Loans:								
individually evaluated for impairment	\$-	\$-	\$-	\$-	\$-	\$ 1,160	\$-	\$ 1,160
collectively evaluated for impairment	257	289	40	262	621	1,799	30	3,298
Acquired Loans:								
individually evaluated for impairment	-	-	-	-	-	48	75	123
collectively evaluated for impairment	8	11	7	47	107	87	21	288
Loans:								
Legacy Loans:								
Ending balance	\$ 63,085	\$ 89,649	\$ 15,098	\$ 94,393	\$ 122,304	\$ 124,981	\$ 1,302	\$ 510,811
individually evaluated for impairment	-	631	63	-	2,838	5,086	-	8,618
collectively evaluated for impairment	63,085	89,018	15,035	94,393	119,466	119,895	1,302	502,193
Acquired Loans:								
Ending balance	6,300	93,339	12,379	36,722	59,057	38,443	2,951	249,191
individually evaluated for impairment	-	363	-	232	151	1,728	150	2,624
collectively evaluated for impairment	6,300	92,976	12,379	36,490	58,906	36,715	2,801	246,567

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 Bank'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.

Edgar Filing: Howard Bancorp Inc - Form 10-Q

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

		September 30, 2016							
		Construction	Residential	Residential	Commercial	Commercial	Commercial	Consumer	
(in thousands)		and land	first lien	junior lien	owner	non-owner	loans	loans	Total
Credit quality indicators:					occupied	occupied	and leases		
Legacy Loans:									
Not classified	\$68,635	\$113,552	\$22,959	\$103,079	\$146,597	\$133,549	\$2,916	\$591,287	
Special mention	-	-	-	-	539	-	-	539	
Substandard	-	295	-	-	2,401	197	-	2,893	
Doubtful	-	214	-	474	594	2,174	-	3,456	
Total	\$68,635	\$114,061	\$22,959	\$103,553	\$150,131	\$135,920	\$2,916	\$598,175	
Acquired Loans:									
Not classified	\$5,077	\$84,016	\$11,341	\$31,027	\$51,352	\$28,336	\$2,000	\$213,149	
Special mention	-	-	-	-	-	-	-	-	
Substandard	413	794	-	441	1,111	1	-	2,760	
Doubtful	-	248	28	45	481	1,564	140	2,506	
Total	\$5,490	\$85,058	\$11,369	\$31,513	\$52,944	\$29,901	\$2,140	\$218,415	
		December 31, 2015							
		Construction	Residential	Residential	Commercial	Commercial	Commercial	Consumer	
(in thousands)		and land	first lien	junior lien	owner	non-owner	loans	loans	Total
Credit quality indicators:					occupied	occupied	and leases		
Legacy Loans:									
Not classified	\$63,085	\$89,081	\$15,035	\$94,392	\$119,637	\$121,288	\$1,302	\$503,820	
Special mention	-	-	-	-	-	614	-	614	
Substandard	-	410	-	-	2,073	7	-	2,490	
Doubtful	-	158	63	-	594	3,072	-	3,887	
Total	\$63,085	\$89,649	\$15,098	\$94,392	\$122,304	\$124,981	\$1,302	\$510,811	
Acquired Loans:									
Not classified	\$6,300	\$92,975	\$12,379	\$36,484	\$58,393	\$36,731	\$2,801	\$246,063	
Special mention	-	-	-	-	-	-	-	-	
Substandard	-	-	-	-	519	-	-	519	
Doubtful	-	364	-	238	145	1,712	150	2,609	
Total	\$6,300	\$93,339	\$12,379	\$36,722	\$59,057	\$38,443	\$2,951	\$249,191	

Special Mention - A Special Mention asset has potential weaknesses that deserve management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the asset or in the institution's credit position at some future date. Special Mention assets are not adversely classified and do not expose an institution to sufficient risk to warrant adverse classification.

Substandard - Substandard loans are inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any. Loans so classified must have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the Bank will sustain some loss if the deficiencies are not corrected.

Doubtful - Loans classified Doubtful have all the weaknesses inherent in those classified Substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently known facts, conditions and values, highly questionable and improbable.

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

Edgar Filing: Howard Bancorp Inc - Form 10-Q

An aged analysis of past due loans are as follows:

(in thousands)	September 30, 2016							Total
	Construction and land	Residential first lien	Residential junior lien	Commercial owner occupied	Commercial non-owner occupied	Commercial loans and leases	Consumer loans	
Analysis of past due loans:								
Legacy Loans:								
Accruing loans current	\$68,633	\$113,620	\$22,959	\$103,079	\$147,464	\$132,750	\$2,916	\$591,421
Accruing loans past due:								
31-59 days past due	-	-	-	-	2,073	996	-	3,069
60-89 days past due	-	227	-	-	-	-	-	227
Greater than 90 days past due	2	-	-	-	-	-	-	2
Total past due	2	227	-	-	2,073	996	-	3,298
Non-accrual loans	-	214	-	474	594	2,174	-	3,456
Total loans	\$68,635	\$114,061	\$22,959	\$103,553	\$150,131	\$135,920	\$2,916	\$598,175
Acquired Loans:								
Accruing loans current	\$5,490	\$84,241	\$11,283	\$31,468	\$51,799	\$27,751	\$1,959	\$213,991
Accruing loans past due:								
31-59 days past due	-	277	49	-	-	586	13	925
60-89 days past due	-	292	-	-	664	-	-	956
Greater than 90 days past due	-	-	9	-	-	-	28	37
Total past due	-	569	58	-	664	586	41	1,918
Non-accrual loans	-	248	28	45	481	1,564	140	2,506
Total loans	\$5,490	\$85,058	\$11,369	\$31,513	\$52,944	\$29,901	\$2,140	\$218,415

(in thousands)	December 31, 2015							Total
	Construction and land	Residential first lien	Residential junior lien	Commercial owner occupied	Commercial non-owner occupied	Commercial loans and leases	Consumer loans	
Analysis of past due loans:								
Legacy Loans:								
Accruing loans current	\$63,070	\$89,319	\$15,034	\$94,141	\$121,094	\$120,025	\$1,301	\$503,983

Edgar Filing: Howard Bancorp Inc - Form 10-Q

Accruing loans past due:								
31-59 days past due	-	-	1	251	-	24	1	277
60-89 days past due	-	-	-	-	-	725	-	725
Greater than 90 days past due	15	-	-	-	445	-	-	460
Total past due	15	-	1	251	445	749	1	1,462
Non-accrual loans	-	330	63	-	765	4,207	-	5,365
Total loans	\$63,085	\$ 89,649	\$ 15,098	\$ 94,392	\$ 122,304	\$ 124,981	\$ 1,302	\$510,811
Acquired Loans:								
Accruing loans current	\$5,924	\$ 91,936	\$ 12,290	\$ 35,574	\$ 58,369	\$ 36,568	\$ 2,765	\$243,426
Accruing loans past due:								
31-59 days past due	67	89	59	73	337	-	11	636
60-89 days past due	309	10	-	607	200	-	23	1,149
Greater than 90 days past due	-	941	30	236	-	147	2	1,356
Total past due	376	1,040	89	916	537	147	36	3,141
Non-accrual loans	-	363	-	232	151	1,728	150	2,624
Total loans	\$6,300	\$ 93,339	\$ 12,379	\$ 36,722	\$ 59,057	\$ 38,443	\$ 2,951	\$249,191

Total loans either in non-accrual status or in excess of ninety days delinquent totaled \$6.0 million or 0.74% of total loans outstanding at September 30, 2016, which represents a decrease from \$9.8 million or 1.3% at December 31, 2015.

Impaired loans at September 30, 2016 and December 31, 2015 are as follows:

(in thousands)	September 30, 2016							Total
	Construction & land	Residential first lien	Residential junior lien	Commercial owner occupied	Commercial non-owner occupied	Commercial loans and leases	Consumer loans	
Impaired loans:								
Legacy Loans:								
Recorded investment	\$-	\$ 509	\$ -	\$ 474	\$ 2,667	\$ 2,717	\$ -	\$6,367
With an allowance recorded	-	-	-	-	-	1,640	-	1,640
With no related allowance recorded	-	509	-	474	2,667	1,077	-	4,727
Related allowance	-	-	-	-	-	1,166	-	1,166
Unpaid principal	-	509	-	474	2,667	2,717	-	6,367
Nine months ended September 30, 2016								
Average balance of impaired loans	-	542	-	496	2,667	3,242	-	6,947
Interest income recognized	-	21	-	13	20	88	-	142
Three months ended September 30, 2016								
Average balance of impaired loans	-	537	-	474	2,667	3,083	-	6,761
Interest income recognized	-	9	-	4	20	14	-	47
Acquired Loans:								
Recorded investment	\$413	\$ 248	\$ 28	\$ 486	\$ 481	\$ 2,250	\$ 140	\$4,046
With an allowance recorded	-	-	-	-	-	850	140	990
With no related allowance recorded	413	248	28	486	481	1,400	-	3,056
Related allowance	-	-	-	-	-	113	72	185
Unpaid principal	419	265	28	491	629	2,860	146	4,838
Nine months ended September 30, 2016								
Average balance of impaired loans	762	259	28	496	474	2,277	140	4,436

Edgar Filing: Howard Bancorp Inc - Form 10-Q

Interest income recognized Three months ended September 30, 2016	9	2	-	11	9	119	-	150
Average balance of impaired loans	635	256	28	491	477	2,263	140	4,290
Interest income recognized	7	-	-	11	1	31	-	50

18

Edgar Filing: Howard Bancorp Inc - Form 10-Q

(in thousands)	December 31, 2015							
	Commercial & land	Residential first lien	Residential junior lien	Commercial owner occupied	Commercial non-owner occupied	Commercial loans and leases	Consumer loans	Total
Impaired loans:								
Legacy Loans:								
Recorded investment	\$-	\$ 631	\$ 63	\$ -	\$ 2,838	\$ 5,086	\$ -	\$8,618
With an allowance recorded	-	-	-	-	-	1,160	-	1,160
With no related allowance recorded	-	631	63	-	2,838	3,926	-	7,458
Related allowance	-	-	-	-	-	1,160	-	1,160
Unpaid principal	-	631	63	-	2,838	5,086	-	8,618
Average balance of impaired loans	-	622	74	-	3,417	7,198	-	11,311
Interest income recognized	-	29	-	-	119	284	-	432
Acquired Loans:								
Recorded investment	\$-	\$ 363	\$ -	\$ 232	\$ 151	\$ 1,728	\$ 150	\$2,624
With an allowance recorded	-	-	-	-	-	48	75	123
With no related allowance recorded	-	363	-	232	151	1,680	75	2,501
Related allowance	-	-	-	-	-	48	75	123
Unpaid principal	-	426	-	402	302	2,742	150	4,022
Average balance of impaired loans	-	444	-	197	63	901	106	1,711
Interest income recognized	-	8	-	8	-	3	6	25

Included in the total impaired loans above were non-accrual loans of \$6.0 million and \$8.0 million at September 30, 2016 and December 31, 2015, respectively. Interest income that would have been recorded if non-accrual loans had been current and in accordance with their original terms was \$221 thousand for the first nine months of 2016.

Management routinely evaluates other real estate owned (“OREO”) based upon periodic appraisals. There was an additional valuation allowance of \$83 thousand relating to one property recorded for the nine months ended September 30, 2016, and for the same period in 2015 there was a valuation adjustment of \$736 thousand on four properties, as the current appraised value, less estimated cost to sell, was less than the carrying amount. During the nine months ended September 30, 2016 there was one loan transferred from the loan portfolio to OREO. In the same period of 2015 the Company did no transfer any loans into OREO, but acquired one property in the Patapsco Bancorp acquisition. The Company did not sell any properties held as OREO in either nine month period.

Loans may have their terms restructured (e.g., interest rates, loan maturity date, payment and amortization period) in circumstances that provide payment relief to a borrower experiencing financial difficulty. Such restructured loans are

Edgar Filing: Howard Bancorp Inc - Form 10-Q

considered troubled debt restructured loans (“TDRs”) that may either be impaired loans that may either be in accruing status or non-accruing status. Non-accruing restructured loans may return to accruing status provided there is a sufficient period of payment performance in accordance with the restructure terms. Loans may be removed from the restructured category in the year subsequent to the restructuring if: a) the restructuring agreement specifies an interest rate equal to or greater than the rate that the creditor was willing to accept at the time of restructuring for a new loan with comparable risk; and b) the loan is not impaired based on the terms specified by the restructuring agreement.

TDRs at September 30, 2016 and December 31, 2015 are as follows:

(dollars in thousands)	September 30, 2016		Number of Loans	Accrual Status	Total TDRs
	Number of Loans	Non-Accrual Status			
Construction and land	-	\$ -	2	\$413	\$413
Residential real estate - first lien	-	-	1	296	296
Commercial - owner occupied	-	-	1	441	441
Commercial - non-owner occupied	1	594	1	2,073	2,667
Commercial loans and leases	1	76	2	198	274
Consumer	1	140	-	-	140
	3	\$ 810	7	\$3,421	\$4,231

Edgar Filing: Howard Bancorp Inc - Form 10-Q

(dollars in thousands)	December 31, 2015				
	Number of Loans	Non-Accrual Status	Number of Loans	Accrual Status	Total TDRs
Residential real estate - first lien	-	\$ -	1	\$ 301	\$ 301
Commercial - non-owner occupied	1	594	1	2,073	2,667
Commercial loans and leases	-	-	1	7	7
Consumer	1	150	-	-	150
	2	\$ 744	3	\$ 2,381	\$ 3,125

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

(in thousands)	September 30, 2016		
	Not Performing to Modified Terms	Performing to Modified Terms	Total TDRs
Construction and land			
Rate modification	\$-	\$ 288	\$ 288
Extension or other modification	-	125	125
Residential real estate - first lien			
Forbearance	-	296	296
Commercial RE - owner occupied			
Rate modification	-	441	441
Commercial RE - non-owner occupied			
Rate modification	594	2,073	2,667
Commercial loans			
Forbearance	76	197	273
Extension or other modification	-	1	1
Consumer			
Extension or other modification	140	-	140
Total trouble debt restructure loans	\$ 810	\$ 3,421	\$ 4,231

(in thousands)	December 31, 2015		
	Not Performing to Modified Terms	Performing to Modified Terms	Total TDRs
Residential real estate - first lien			
Forbearance	\$-	\$ 301	\$ 301
Commercial RE - non-owner occupied			

Edgar Filing: Howard Bancorp Inc - Form 10-Q

Rate modification	594	2,073	2,667
Commercial loans			
Extension or other modification	-	7	7
Consumer			
Extension or other modification	150	-	150
Total trouble debt restructure loans	\$744	\$ 2,381	\$3,125

There were five loans totaling \$854 thousand restructured in the first nine months of 2016. Two commercial loans totaling \$273 thousand were modified from principal and interest payments to interest only payments for a six to nine month period. One construction and land loan for \$413 thousand and one commercial real estate owner occupied loan for \$441 thousand were restructured to interest only payments with a reduction in the interest rate. Finally, there was a restructuring of a \$466 thousand land development loan that included a paydown from the guarantor, partial debt forgiveness by the Bank and a reduction of the interest rate on the remaining balance of the loan, which the Bank anticipates will be fully repaid. Performing TDRs were in compliance with their modified terms and there are no further commitments associated with these loans.

Note 6: Goodwill and Other Intangible Assets

The Bank has one unit, which is the core banking operation. The table below shows goodwill balances at September 30, 2016 and December 31, 2015.

(in thousands)
Goodwill
Banking \$603

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

(in thousands)	September 30, 2016		Net Carrying Amount	Weighted Average Remaining Life (Years)
	Gross Carrying Amount	Accumulated Amortization		
Amortizing intangible assets:				
Core deposit intangible	\$3,540	\$ 1,156	\$ 2,384	6.86

(in thousands)	December 31, 2015		Net Carrying Amount	Weighted Average Remaining Life (Years)
	Gross Carrying Amount	Accumulated Amortization		
Amortizing intangible assets:				
Core deposit intangible	\$3,540	\$ 637	\$ 2,903	7.61

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

(in thousands)	
2016	\$ 136
2017	506
2018	396
2019	314
2020	269
Thereafter	763
Total amortizing intangible assets	\$2,384

Note 7: Deposits

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

(dollars in thousands)	September 30, 2016		December 31, 2015	
	Amount	% of Total	Amount	% of Total
Noninterest-bearing demand	\$ 183,118	23 %	\$ 173,689	23 %
Interest-bearing checking	58,197	7	54,014	7
Money market accounts	254,880	32	230,661	31
Savings	50,502	6	51,989	7
Certificates of deposit \$250,000 and over	12,687	2	15,749	2
Certificates of deposit under \$250,000	244,389	30	221,306	30
Total deposits	\$ 803,773	100 %	\$ 747,408	100 %

Note 8: Stock Options and Stock Awards

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

Stock awards may also be granted to non-employee members of the Board of Directors as compensation for attendance and participation at meetings of the Board of Directors and meetings of the various committees of the Board. For the nine months ended September 30, 2016 the Company's directors earned 5,362 shares of stock as compensation for their service.

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

	September 30, 2016		December 31, 2015	
	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price
Balance at January 1,	137,463	\$ 12.30	264,652	\$ 11.75
Granted	-	-	-	-
Exercised	(1,740)	11.00	(62,287)	10.48
Forfeited	(10,850)	11.77	(64,902)	11.83
Balance at period end	124,873	\$ 12.36	137,463	\$ 12.30
Exercisable at period end	124,873	\$ 12.36	137,463	\$ 12.30
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 \$13.21 at September 30, 2016 the options outstanding had an aggregate intrinsic value of \$160 thousand. At December 31, 2015, based upon fair market value of \$13.24, the options outstanding had an aggregate intrinsic value of \$185 thousand.

Restricted Stock

Edgar Filing: Howard Bancorp Inc - Form 10-Q

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 were subject to a three year vesting schedule however, they only vested if certain annual performance measures were satisfactorily achieved.

The following table presents a summary of the activity in the Company's restricted stock for the periods ended:

	September 30, 2016		December 31, 2015	
	Shares	Weighted Average Grant Date Fair Value	Shares	Weighted Average Grant Date Fair Value
Balance at January 1,	8,330	\$ 6.92	33,330	\$ 6.89
Granted	-	-	-	-
Vested	(8,330)	6.92	(18,336)	6.89
Forfeited	-	-	(6,664)	6.85
Balance at period end	-	\$ -	8,330	\$ 6.92

At September 30, 2016, there were no restricted stock awards outstanding, and all of the pre-tax compensation expense related to restricted stock awards has been recognized.

Restricted Stock Units

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

The Company granted 27,000 RSUs in the first nine months of 2016, all of which are subject to a three year vesting schedule. During 2015, 73,500 RSUs were granted, with 43,500 of the RSUs subject to a three year vesting schedule with one-third of the RSUs vesting each year on the grant date anniversary. The remaining 30,000 awarded RSUs also are subject to a three year vesting schedule; they only vest, however, if certain annual performance measures are satisfactorily achieved.

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

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

	September 30, 2016		December 31, 2015	
	Shares	Weighted Average Grant Date Fair Value	Shares	Weighted Average Grant Date Fair Value
Balance at January 1,	74,828	\$ 13.23	44,500	\$ 11.21
Granted	27,000	12.91	73,500	14.00
Vested	(17,838)	12.95	(19,836)	11.64
Forfeited	(18,499)	12.96	(23,336)	12.84
Balance at period ended	65,491	\$ 13.16	74,828	\$ 13.23

At September 30, 2016, based on RSU awards outstanding at that time, the total unrecognized pre-tax compensation expense related to unvested RSU awards was \$736 thousand. This expense is expected to be recognized through 2019.

Stock-Based Compensation Expense: Stock-based compensation is recognized as compensation cost in the Statement of Operations based on the fair values on the measurement date, which, for the Company, is the date of the grant. The Company recognized stock-based compensation expense related to the issuance of restricted stock and restricted stock units of \$219 thousand as well as \$68 thousand for director compensation paid in stock for the nine month period ended September 30, 2016. For the three months ended September 30, 2016 stock-based compensation expense related to the issuance of restricted stock and restricted stock units of \$51 thousand as well as \$21 thousand for director compensation paid in stock. The Company recognized stock-based compensation expense related to the issuance of restricted stock and RSUs of \$375 thousand as well as \$95 thousand for director compensation paid in stock for the year ended December 31, 2015.

Valuation of Stock-Based Compensation: The fair value of the Company's stock options granted as compensation is estimated on the measurement date, which, for the Company, is the date of grant. The fair value of stock options was calculated using the Black-Scholes option-pricing model. There were not any stock options granted during the nine months ended September 30, 2016 or in 2015.

Note 9: Benefit Plans

Profit Sharing Plan

The Company sponsors a defined contribution retirement plan through a Section 401(k) profit sharing plan. Employees may contribute up to 15% of their pretax compensation. Participants are eligible for matching Company contributions up to 4% of eligible compensation dependent on the level of voluntary contributions. Company matching contributions totaled \$469 thousand and \$391 thousand, respectively, for the nine months ended September 30, 2016 and 2015. The Company's matching contributions vest immediately.

Supplemental Executive Retirement Plan (SERP)

In 2014, the Bank created a SERP for the Chief Executive Officer. This plan was amended in 2015. Under the defined benefit SERP, Ms. Scully will receive \$150,000 each year for 15 years after attainment of the Normal Retirement Age (as defined in the SERP). Ms. Scully will earn vesting on a graduated schedule in which she will become fully vested on August 25, 2019, which has been established for purposes of the SERP as her retirement date. Expense related to this plan totaled \$182 thousand and \$68 thousand, respectively, for the nine month periods, and \$61 thousand and \$23 thousand, respectively, for the three month periods, ending September 30, 2016 and 2015.

Note 10: Income per Common Share

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

(dollars in thousands, except per share data)	Nine months ended September 30		Three months ended September 30	
	2016	2015	2016	2015
Net income (loss)	\$4,349	\$655	\$1,748	\$(786)
Preferred stock dividends	(166)	(94)	-	(31)
Net income (loss) available to common shareholders (numerator)	\$4,183	\$561	\$1,748	\$(817)
BASIC				
Basic average common shares outstanding (denominator)	6,970,714	5,897,325	6,985,559	6,493,987
Basic income (loss) per common share	\$0.60	\$0.09	\$0.25	\$(0.13)
DILUTED				
Average common shares outstanding	6,970,714	5,897,325	6,985,559	6,493,987
Dilutive effect of common stock equivalents	101,475	127,648	91,861	-
Diluted average common shares outstanding (denominator)	7,072,189	6,024,973	7,077,420	6,493,987
Diluted income (loss) per common share	\$0.59	\$0.09	\$0.25	\$(0.13)
Common stock equivalents outstanding that are anti-dilutive and thus excluded from calculation of diluted number of shares presented above	74,911	2,150	74,911	156,270

Note 11: Risk-Based Capital

In July 2013, the Federal Deposit Insurance Corporation (the “FDIC”) and the other federal bank regulatory agencies issued a final rule that revised their leverage and risk-based capital requirements and the method for calculating risk-weighted assets to make them consistent with agreements that were reached by the Basel Committee on Banking Supervision (“Basel III”) and certain provisions of the Dodd-Frank Act. The final rule, which became effective on January 1, 2015, applies to all depository institutions, top-tier bank holding companies with total consolidated assets of \$1 billion or more and top-tier savings and loan holding companies. The Company will become subject to the final rule as administered by the Board of Governors of the Federal Reserve if and when the Company reaches \$1 billion in total consolidated assets. The final rule creates a new common equity Tier 1 (“CET1”) minimum capital requirement (4.5% of risk-weighted assets), increases the minimum Tier 1 capital ratio (from 4% to 6% of risk-weighted assets), imposes a minimum leverage ratio of 4.0%, and changes the risk-weight of certain assets to better reflect credit risk and other risk exposures. These include, among other things, a 150% risk weight for certain high volatility commercial real estate acquisition, development and construction loans and for non-residential mortgage loans that are 90 days past due or otherwise in non-accrual status, and a 20% credit conversion factor for the unused portion of a commitment with an original maturity of one year or less that is not unconditionally cancellable. The final rule also

requires unrealized gains and losses on certain “available-for-sale” securities holdings to be included for purposes of calculating regulatory capital unless the Company elects to opt-out from this treatment. The Company has elected to permanently opt out of this treatment in the Company’s capital calculations, as permitted by the final rule.

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

In addition, under revised prompt corrective action requirements, in order to be considered “well-capitalized,” the Bank must have a CET1 risk-based capital ratio of 6.5% or greater, a Tier 1 risk-based capital ratio of 8.0% or greater, a total risk-based capital ratio of 10.0% or greater and a leverage ratio of 5.0% or greater.

There are two main categories of capital under the regulatory capital guidelines. Tier 1 capital includes common shareholders' equity, qualifying preferred stock and trust preferred securities, less goodwill and certain other deductions (including the unrealized net gains and losses, after applicable income taxes, on securities available for sale carried at fair value). Tier 2 capital includes preferred stock not qualifying as Tier 1 capital, subordinated debt, the allowance for credit losses and net unrealized gains on marketable equity securities, subject to limitations by the guidelines. Tier 2 capital is limited to the amount of Tier 1 capital (i.e., at least half of total capital must be in the form of Tier 1 capital). Under the guidelines, capital is compared to the relative risk related to the balance sheet. To derive the risk included in the balance sheet, one of several risk weights is applied to the different balance sheet and off-balance sheet assets, primarily based on the relative credit risk of the counterparty. For example, claims guaranteed by the U.S. government or one of its agencies are risk-weighted at 0%. Off-balance sheet items, such as loan commitments, are also applied a risk weight after calculating balance sheet equivalent amounts. One of four credit conversion factors (0%, 20%, 50% and 100%) is assigned to loan commitments based on the likelihood of the off-balance sheet item becoming an asset. For example, certain loan commitments are converted at 50% and then risk-weighted at 100%. The capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

Management believes that, as of September 30, 2016 and December 31, 2015, Bancorp and the Bank met all capital adequacy requirements to which they are subject.

(dollars in thousands)	Actual		For capital adequacy purposes		To be well capitalized under the FDICIA prompt corrective action provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of September 30, 2016:						
Total capital (to risk-weighted assets)						
Howard Bank	\$93,108	11.01 %	\$ 67,662	8.00 %	\$ 84,578	10.00 %
Howard Bancorp	\$91,557	10.71 %	\$ 68,391	8.00 %	N/A	
Common equity tier 1 capital (to risk-weighted assets)						
Howard Bank	\$87,474	10.34 %	\$ 38,060	4.50 %	\$ 54,976	6.50 %
Howard Bancorp	\$82,504	9.65 %	\$ 38,470	4.50 %	N/A	
Tier 1 capital (to risk-weighted assets)						
Howard Bank	\$87,474	10.34 %	\$ 50,747	6.00 %	\$ 67,662	8.00 %
Howard Bancorp	\$82,504	9.65 %	\$ 51,293	6.00 %	N/A	
Tier 1 capital (to average assets) (Leverage ratio)						
Howard Bank	\$87,474	9.07 %	\$ 38,591	4.00 %	\$ 48,239	5.00 %
Howard Bancorp	\$82,504	8.55 %	\$ 38,577	4.00 %	N/A	
As of December 31, 2015:						
Total capital						

Edgar Filing: Howard Bancorp Inc - Form 10-Q

(to risk-weighted assets)						
Howard Bank	\$87,860	11.07 %	\$ 63,482	8.00 %	\$ 79,353	10.00 %
Howard Bancorp	\$95,737	12.09 %	\$ 63,370	8.00 %	N/A	
Common equity tier 1 capital						
(to risk-weighted assets)						
Howard Bank	\$82,991	10.46 %	\$ 35,709	4.50 %	\$ 51,579	6.50 %
Howard Bancorp	\$90,868	11.47 %	\$ 35,646	4.50 %	N/A	
Tier 1 capital (to risk-weighted assets)						
Howard Bank	\$82,991	10.46 %	\$ 47,612	6.00 %	\$ 63,482	8.00 %
Howard Bancorp	\$90,868	11.47 %	\$ 47,528	6.00 %	N/A	
Tier 1 capital (to average assets)						
(Leverage ratio)						
Howard Bank	\$82,991	9.04 %	\$ 36,703	4.00 %	\$ 45,879	5.00 %
Howard Bancorp	\$90,868	9.90 %	\$ 36,710	4.00 %	N/A	

The decrease in Bancorp's risk-based capital ratios for September 30, 2016 was directly impacted by the redemption of the preferred stock issued under the SBLF program. This redemption occurred on May 6, 2016. Further information on this redemption can be found in Note 12 below.

Note 12: Preferred Stock

On September 22, 2011, Bancorp 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 Bancorp's 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 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 were 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 for future dividend periods was 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 could vary from 1% per annum to 5% per annum for the second through tenth dividend periods and from 1% per annum to 7% per annum for the eleventh through the eighteenth dividend periods and through March 22, 2016 with respect to the nineteenth dividend period. If the Series AA Preferred Stock remained outstanding for more than four-and-one-half years, the dividend rate was fixed at 9%. As of March 22, 2016, the dividend rate was fixed at 9%. Such dividends were not cumulative, but Bancorp could only declare and pay dividends on the Common Stock (or any other equity securities junior to the Series AA Preferred Stock) if it had declared and paid dividends for the current dividend period on the Series AA Preferred Stock, and was subject to other restrictions on its ability to repurchase or redeem other securities. In addition, if Bancorp had 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) could have designated a representative to attend all meetings of Bancorp's Board of Directors in a nonvoting observer capacity and Bancorp would have been required to give such representative copies of all notices, minutes, consents and other materials that Bancorp provided to its directors in connection with such meetings.

On May 6, 2016, after receiving all required regulatory approvals, Bancorp redeemed the 12,562 shares of Series AA Preferred Stock that it had previously issued to the Treasury under the SBLF program for \$12,562,000 in accordance with its terms. Bancorp used the proceeds of a \$12,562,000 term loan with Raymond James Bank, N.A. to fund the redemption of the Series AA Preferred Stock. This debt matures one year from commencement, with interest only payments based upon 30 day LIBOR plus 300 basis points.

Note 13: Fair Value

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

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

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

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

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

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

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

Recurring Fair Value Measurements

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

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

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

For loans held for investment that were originally intended to be sold and previously included as loans held for sale, the fair value of these loans is determined 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.

Non-recurring Fair Value Measurements

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

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

and adjusted accordingly, based on the same factors identified above.

Other real estate owned acquired through, or in lieu of, foreclosure are held for sale and are initially recorded at fair value, less selling costs. Any write-downs to fair value at the time of transfer to OREO are charged to the allowance for credit losses subsequent to foreclosure. Values are derived from appraisals of underlying collateral and discounted cash flow analysis. There was an \$83 thousand valuation loss recognized during the nine months ended September 30, 2016 and valuation losses of \$736 thousand recognized for the year ended December 31, 2015. OREO is classified within Level 3 of the hierarchy.

The following table sets forth the Company's financial assets and liabilities that were accounted for at fair value on a recurring basis at September 30, 2016 and December 31, 2015:

Edgar Filing: Howard Bancorp Inc - Form 10-Q

September 30, 2016	Carrying Value	Quoted Price in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
(in thousands)	(Fair Value)	(Level 1)	(Level 2)	(Level 3)
Investment securities:				
U.S. Government agencies	\$ 34,540	\$ -	\$ 34,540	\$ -
U.S. Government treasuries	1,513	-	1,513	-
Mortgage-backed securities	29	-	29	-
Other investments	1,636	-	1,636	-
Loans held for sale	46,342	-	46,342	-
Loans held for investment	9,368	-	9,368	-
Rate lock commitments	679	-	679	-

December 31, 2015	Carrying Value	Quoted Price in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
(in thousands)	(Fair Value)	(Level 1)	(Level 2)	(Level 3)
Investment securities:				
U.S. Government agencies	\$ 48,422	\$ -	\$ 48,422	\$ -
Mortgage-backed securities	57	-	57	-
Other investments	1,094	-	1,094	-
Loans held for sale	49,677	-	49,677	-
Rate lock commitments	508	-	508	-

Assets under fair value option:

September 30, 2016	Carrying Fair Value	Aggregate Unpaid Principal	Difference
(in thousands)	Amount	Principal	Difference
Loans held for sale	\$ 46,342	\$ 45,028	\$ 1,314
Loans held for investment	9,368	8,881	487

December 31, 2015	Carrying Fair Value	Aggregate Unpaid Principal	Difference
(in thousands)	Amount	Principal	Difference
Loans held for sale	\$ 49,677	\$ 48,395	\$ 1,282

There was one loan for \$214 thousand that was originally classified as held for sale that was downgraded to non-accrual status in the third quarter of 2016. There were no loans held for sale and held for investment 90 days or

more past due and still accruing interest at either September 30, 2016 or December 31, 2015. Net gain from the changes included in earnings in fair value of loans held for sale and held for investment was \$519 thousand and \$69 thousand during the nine months ended September 30, 2016 and the year ended December 31, 2015, respectively.

The following table sets forth the Company's financial assets and liabilities that were accounted for at fair value on a nonrecurring basis at September 30, 2016 and December 31, 2015. OREO is initially recorded at fair value less anticipated costs to sell. Impaired loans are measured using the fair value of collateral, if applicable.

Edgar Filing: Howard Bancorp Inc - Form 10-Q

September 30, 2016	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)
(in thousands)				
Other real estate owned	\$ 2,543	\$ -	\$ -	\$ 2,543
Impaired loans:				
Construction and land	413	-	-	413
Residential - first lien	757	-	-	757
Residential - junior lien	28	-	-	28
Commercial - owner occupied	960	-	-	960
Commercial - non-owner occupied	3,149	-	-	3,149
Commercial loans and leases	3,688	-	-	3,688
Consumer	68	-	-	68

December 31, 2015	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)
(in thousands)				
Other real estate owned	\$ 2,369	\$ -	\$ -	\$ 2,369
Impaired loans:				
Construction and land	-	-	-	-
Residential - first lien	994	-	-	994
Residential - junior lien	63	-	-	63
Commercial - owner occupied	232	-	-	232
Commercial - non-owner occupied	2,989	-	-	2,989
Commercial loans and leases	5,606	-	-	5,606
Consumer	75	-	-	75

At September 30, 2016 OREO consisted of initially recorded value of \$5.4 million, less a valuation allowance of \$2.9 million. At December 31, 2016 OREO initially recorded value was \$5.2 million, less a valuation allowance of \$2.9 million. The allowance for credit losses on impaired loans was \$1.4 million and \$1.3 million at September 30, 2016 and December 31, 2015 respectively.

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

The following table presents required information in accordance with ASC Topic 825 “Financial Instruments” at September 30, 2016 and December 31, 2015. 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 the Bank’s financial instruments, estimates may be based on the present value of estimated future cash flows and estimated discount rates. These financial assets and liabilities have not been recorded at fair value.

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

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

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

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

Loans held for investment: Determined 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

Rate lock commitments: Based on estimate loan closing and investor delivery rate based on historical experience.

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

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

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

Long-term borrowing: Based on quoted market prices. If quoted market price is not available, discounted cash flow analyses, based on current incremental borrowing rates for similar types of instruments.

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

	September 30, 2016				
	Carrying	Fair	Quoted Price in	Significant	Significant
(in thousands)	Amount	Value	Active Markets	Other	Unobservable
Financial Assets			for Identical	Observable	Inputs
Investment securities			Assets	Inputs	Inputs
			(Level 1)	(Level 2)	(Level 3)
	\$37,718	\$37,718	\$ -	\$ 37,718	\$ -

Edgar Filing: Howard Bancorp Inc - Form 10-Q

Nonmarketable equity securities	4,741	4,741	-	4,741	-
Loans held for sale	46,342	46,342	-	46,342	-
Loans held for investment	9,368	9,368	-	9,368	-
Rate lock commitments	679	679	-	679	-
Loans and leases	801,588	807,168	-	-	807,168
Financial Liabilities					
Deposits	803,773	802,797	-	802,797	-
Short-term borrowings	93,263	93,263	-	93,263	-
Long-term borrowings	26,643	26,791	-	26,791	-

December 31, 2015

(in thousands)	Carrying Amount	Fair Value	Quoted Price in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Financial Assets					
Investment securities	\$49,573	\$49,573	\$ -	\$ 49,573	\$ -
Nonmarketable equity securities	4,163	4,163	-	4,163	-
Loans held for sale	49,677	49,677	-	49,677	-
Rate lock commitments	508	508	-	508	-
Loans and leases	755,133	760,562	-	-	760,562
Financial Liabilities					
Deposits	747,408	747,938	-	747,938	-
Short-term borrowings	69,121	69,121	-	69,121	-
Long-term borrowings	29,707	29,911	-	29,911	-

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

This section is intended to help our stockholders and potential investors understand our financial performance through a discussion of the factors affecting our consolidated financial condition at September 30, 2016 and December 31, 2015 and our consolidated results of operations for the periods ended September 30, 2016 and September 30, 2015. This section should be read in conjunction with the consolidated financial statements and notes to the consolidated financial statements.

Overview

Howard Bancorp, Inc. is the holding company for Howard Bank. Howard Bank is a trust company chartered under Subtitle 2 of Title 3 of the Financial Institutions Article of the Annotated Code of Maryland. The Bank was formed in March 2004 and commenced banking operations on August 9, 2004. Howard Bank does not exercise trust powers, and our regulatory structure is the same as a Maryland-chartered commercial bank. As such, our business has consisted primarily of originating both commercial and real estate loans secured by property in our market area. Typically, commercial real estate and business loans involve a higher degree of risk and carry a higher yield than one-to-four-family residential loans. Although we plan to continue to focus on commercial customers, we 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 The Greater Baltimore Metropolitan Area. We engage in a general commercial banking business, making various types of loans and accepting deposits. We market our financial services to small to medium sized businesses and their owners, professionals and executives, and high-net-worth individuals. Our loans are primarily funded by core deposits of customers in our market.

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

Our results of operations depend mainly on our net interest income, which is the difference between the interest income we earn on our loan and investment portfolios and the interest expense we pay on deposits and borrowings. Results of operations are also affected by provisions for credit losses, noninterest income and noninterest expense.

Our noninterest expense consists primarily of compensation and employee benefits, as well as office occupancy, loan production expense, deposit insurance and general administrative and data processing expenses. Our operations are significantly affected by general economic and competitive conditions, particularly with respect to changes in interest rates, government policies and actions of regulatory authorities. Future changes in applicable laws, regulations or government policies may materially affect our financial condition and results of operations.

On August 28, 2015, Bancorp completed its acquisition of Patapsco Bancorp, Inc., the parent company of The Patapsco Bank, through the merger of Patapsco Bancorp with and into Bancorp.

Total assets increased by \$68.0 million or 7.2% when comparing September 30, 2016 assets of \$1.0 billion to the \$946.8 million at December 31, 2015. Total loans and leases outstanding of \$816.6 million at the end of September 2016 showed an increase of \$56.6 million or 7.5% compared to total loans and leases of \$760.0 million on December 31, 2015. Total deposits grew \$56.4 million or 7.5% when comparing September 30, 2016 to December 31, 2015.

Net income for the first nine months of 2016 was \$4.3 million, which represents an increase of \$3.7 million or 563.8% over net income of \$655 thousand for the first nine months of 2015. Net interest income for the nine months ended September 30, 2016 was \$25.7 million versus \$21.2 million for the first nine months of 2015, an increase of approximately \$4.4 million or 20.8%. Total noninterest income was \$11.8 million for the first nine months of 2016, compared to a total of \$9.0 million for the same period in 2015. Total noninterest expenses increased to \$29.4 million from \$27.9 million for the nine months ended September 30, 2016 and 2015, respectively.

Critical Accounting Policies

Our accounting and financial reporting policies conform to GAAP and general practice within the banking industry. Accordingly, preparation of the financial statements require management to exercise significant judgment or discretion or make significant assumptions and estimates based on the information available that have, or could have, a material impact on the carrying value of certain assets or on income. These estimates and assumptions affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of income and expenses during the periods presented. In reviewing and understanding financial information for us, you are encouraged to read and understand the significant accounting policies used in preparing our financial statements. The accounting policies we view as critical are those relating to the allowance for credit losses, goodwill and other intangible assets, business combinations, income taxes and share based compensation. Significant accounting policies are discussed in detail in “Notes to Consolidated Financial Statements - Note 1: Summary of Significant Account Policies” in our Annual Report on Form 10-K for the year ended December 31, 2015. There have been no changes to the significant accounting policies as described in the Annual Report. Disclosures regarding the effects of new accounting pronouncements are included in Note 1 of this report.

Balance Sheet Analysis and Comparison of Financial Condition

A comparison between September 30, 2016 and December 31, 2015 balance sheets is presented below.

Balance Sheet

Total assets increased \$68.0 million, or 7.2%, to \$1.0 billion at September 30, 2016 compared to \$946.8 million at December 31, 2015. This asset growth was primarily a result of an increase in loans and leases of \$56.6 million. In addition, the Bank invested approximately \$20.0 million in interest bearing certificates of deposit at other financial institutions. Partially offsetting the growth in these categories was a decline in investment securities of \$11.9 million. Organic loan growth was funded from increases in customer deposits, which increased by \$56.4 million or 7.5% during the first nine months of 2016. Supplementing the deposit growth was an increase in borrowings of \$21.1 million as we increased the level of short-term Federal Home Loan Bank of Atlanta (“FHLB”) borrowings. As a result of the redemption of our Series AA Preferred Stock in May 2016, as discussed in Notes 1 and 12 to our consolidated financial statements, preferred shareholders’ equity decreased from \$12.6 million on December 31, 2015 to \$0 at September 30, 2016. As a result, total shareholders’ equity declined \$8.0 million despite the increase in retained earnings.

Securities Available for Sale

We currently hold U.S. agency and treasury securities, mortgage-backed securities, stock in another small financial institution and mutual fund investments in our securities portfolio, all of which are categorized as available for sale. The investment in a mutual fund is a supplement to our community reinvestment program activities. We use our securities portfolio to provide the required collateral for funding via commercial customer repurchase agreements as well as to provide sufficient liquidity to fund our loans and provide funds for withdrawals of deposited funds. At September 30, 2016 and December 31, 2015 we held an investment in stock of the FHLB. of \$4.7 million and \$4.2 million, respectively. This investment, which is required for continued FHLB membership, is based partially upon the dollar amount of borrowings outstanding from the FHLB. These investments are carried at cost.

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

(in thousands)	September 30, 2016	December 31, 2015
	Amortized Estimated	Amortized Estimated

Edgar Filing: Howard Bancorp Inc - Form 10-Q

	Cost	Fair Value	Cost	Fair Value
U.S. Government Agencies	\$ 34,531	\$ 34,540	\$48,467	\$ 48,422
Treasuries	1,513	1,513	-	-
Mortgage-backed	28	29	54	57
Other investments	1,600	1,636	1,100	1,094
	\$ 37,672	\$ 37,718	\$49,621	\$ 49,573

We had securities available for sale of \$37.7 million and \$49.6 million at September 30, 2016 and December 31, 2015, respectively, which were recorded at fair value. This represents a decrease of \$11.9 million, or 23.9%, from year end 2015, all of which was a result of scheduled maturities as well as calls of the securities. Nearly \$30.0 million of our securities portfolio matures in one year or less, giving us the capacity to fund future loan growth while maintaining an appropriate amount of securities available for use as collateral. We did not record any gains or losses on the sales or calls of securities for the first nine months of 2016.

With respect to our portfolio of securities available for sale, the portfolio contained three securities with unrealized losses of \$12 thousand and 19 securities with unrealized losses of \$51 thousand at September 30, 2016 and December 31, 2015, respectively. Changes in the fair value of these securities resulted primarily from interest rate fluctuations. We do not intend to sell these securities nor is it more likely than not that we would be required to sell these securities before their anticipated recovery, and we believe the collection of the investment and related interest is probable. Based on this analysis, we do not consider any of the unrealized losses to be other than temporary impairment losses.

Loan and Lease Portfolio

Total loans and leases (which excludes loans held for sale) increased \$56.6 million or 7.5%, to \$816.6 million at September 30, 2016 from \$760.0 million at December 31, 2015. At September 30, 2016, total loans and leases represented 80.5% of total assets, compared to 80.3% of total assets at December 31, 2015. This organic growth resulted from growth in total real estate loans during the first nine months of 2016, which increased \$38.6 million or 6.5% from December 31, 2015 levels. Residential real estate loans grew \$23.0 million and commercial real estate loans (including construction and land development) grew \$30.4 million comparing September 30, 2016 levels to those at December 31, 2015. Commercial loans and leases remained relatively level increasing just \$2.4 million during the first nine months of 2016.

The following table sets forth the composition of our loan portfolio at the dates indicated. In addition to the amounts below, we had loans held for sale of \$46.3 million at September 30, 2016 and \$49.7 million at December 31, 2015.

(dollars in thousands)	September 30, 2016		December 31, 2015	
	Amount	Percent	Amount	Percent
Real Estate				
Construction and land	\$ 74,125	9.1 %	\$ 69,385	9.1 %
Residential - first lien	199,119	24.4	182,988	24.1
Residential - junior lien	34,328	4.2	27,477	3.6
Total residential real estate	233,447	28.6	210,465	27.7
Commercial - owner occupied	135,066	16.5	131,114	17.3
Commercial - non-owner occupied	203,075	24.9	181,361	23.9
Total commercial real estate	338,141	41.5	312,475	41.1
Total real estate loans	645,713	79.2	592,325	77.9
Commercial loans and leases	165,821	20.3	163,424	21.4
Consumer loans	5,056	0.6	4,253	0.6
Total loans and leases	\$ 816,590	100.0 %	\$ 760,002	100.0 %

Deposits

Our deposits increased from \$747.4 million at December 31, 2015 to \$803.8 million at September 30, 2016, an increase of \$56.4 million or 7.5%. Money market accounts had the largest increase - \$24.2 million or 10.5%, followed by: certificates of deposit with growth of \$20.0 million or 8.5%; noninterest-bearing demand deposits with growth of \$9.4 million or 5.4%; and interest-bearing demand deposits, which increased by \$4.2 million or 7.7%. The only deposit category that declined was our savings accounts, which decreased \$1.5 million or 2.9% during the nine months ended September 30, 2016.

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

(dollars in thousands)	September 30, 2016		December 31, 2015	
	Amount	% of Total	Amount	% of Total
Noninterest-bearing demand	\$ 183,118	23 %	\$ 173,689	23 %
Interest-bearing checking	58,197	7	54,014	7
Money market accounts	254,880	32	230,661	31
Savings	50,502	6	51,989	7
Certificates of deposit \$250,000 and over	12,687	2	15,749	2
Certificates of deposit under \$250,000	244,389	30	221,306	30
Total deposits	\$ 803,773	100 %	\$ 747,408	100 %

Borrowings

Customer deposits remain the primary source we utilize to meet funding needs, but we supplement this with short-term and long-term borrowings. Borrowings have historically consisted of overnight unsecured master notes, overnight securities sold under agreement to repurchase (“repurchase agreements”), FHLB advances, and a junior subordinated debenture assumed in the Patapsco Bancorp acquisition. In the second quarter of 2016 a variable rate short-term debt with Raymond James Bank, N.A. was added to our borrowings to help fund the redemption of \$12.6 million in preferred stock issued under the SBLF program.

Our borrowings totaled \$119.9 million at September 30, 2016 and \$98.8 million at December 31, 2015. Short-term borrowings totaled \$93.3 million at September 30, 2016 and \$69.1 million at December 31, 2015. At September 30, 2016, we had six long-term FHLB advances outstanding totaling \$23.0 million and junior subordinated debt totaling \$3.6 million.

Shareholders' Equity

Total shareholders' equity decreased \$8.0 million, or approximately 8.6%, from \$92.9 million at December 31, 2015 to \$84.9 million at September 30, 2016. Changes in shareholders' equity were primarily the result of Howard Bancorp redeeming all \$12.6 million of our Series AA Preferred Stock, partially offset by the retention of the earnings for the first nine months of 2016. Absent the redemption of the preferred stock, shareholders' equity would have increased \$4.6 million or 5.7% at September 30, 2016 compared to December 31, 2015.

Total shareholders' equity at September 30, 2016 represents a capital to asset ratio of 8.4%, while total shareholders' equity at December 31, 2015 represented a capital to asset ratio of 9.8%. The decrease in the capital asset ratio is similarly the result of the redemption of our Series AA Preferred Stock in May 2016, partially offset by the retention of the earnings for the first nine months of 2016.

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.

Edgar Filing: Howard Bancorp Inc - Form 10-Q

	Nine months ended September 30,					
	2016			2015		
(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	\$ 162,957	\$ 6,115	5.01 %	\$ 140,432	\$ 5,158	4.91 %
Commercial real estate	317,631	11,608	4.88	257,428	10,068	5.23
Construction and land	71,909	2,508	4.66	64,216	2,274	4.73
Residential real estate	221,839	7,050	4.25	123,080	4,188	4.55
Consumer	4,421	181	5.46	4,192	181	5.76
Total loans and leases	778,757	27,462	4.71	589,348	21,869	4.96
Loans held for sale	44,109	1,130	3.42	48,690	1,308	3.59
Other earning assets ²	31,268	98	0.42	23,122	43	0.25
Securities: ³						
U.S. Treasury	630	4	0.83	2,769	12	0.58
U.S Gov agencies	46,835	145	0.41	31,630	77	0.33
Mortgage-backed	41	1	4.42	1,686	3	0.21
Other investments	5,012	149	3.96	3,314	87	3.50
Total securities	52,518	299	0.76	39,399	179	0.61
Total earning assets	906,652	28,989	4.27	700,559	23,399	4.47
Cash and due from banks	7,230			6,984		
Bank premises and equipment, net	20,677			14,645		
Other assets	30,704			17,755		
Less: allowance for credit losses	(5,428)			(4,024)		
Total assets	\$959,835			\$735,919		
Interest-bearing liabilities						
Deposits:						
Interest-bearing demand accounts	\$57,032	\$ 97	0.23 %	\$45,007	\$ 71	0.21 %
Money market	249,488	871	0.47	153,695	552	0.48
Savings	52,876	54	0.14	36,295	40	0.15
Time deposits	238,525	1,536	0.86	211,929	1,203	0.76
Total interest-bearing deposits	597,921	2,558	0.57	446,926	1,866	0.56
Short-term borrowings	57,803	380	0.88	47,406	98	0.28
Long-term borrowings	30,889	385	1.66	20,507	188	1.23
Total interest-bearing funds	686,613	3,323	0.65	514,839	2,152	0.56
Noninterest-bearing deposits	180,209			143,239		
Other liabilities and accrued expenses	6,253			7,223		
Total liabilities	873,075			665,301		
Shareholders' equity	86,760			70,618		
Total liabilities & shareholders' equity	\$959,835			\$735,919		
Net interest rate spread ⁴		\$ 25,666	3.62 %		\$ 21,247	3.91 %
Effect of noninterest-bearing funds			0.16			0.14
Net interest margin on earning assets ⁵			3.78 %			4.05 %

(1)

Edgar Filing: Howard Bancorp Inc - Form 10-Q

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

(2) *Includes Federal funds sold and interest-bearing deposits with banks*

(3) *Available for sale securities are presented at amortized cost.*

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

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

Edgar Filing: Howard Bancorp Inc - Form 10-Q

(dollars in thousands)	Three months ended September 30,					
	2016			2015		
	Average Balance	Income / Expense	Yield / Rate	Average Balance	Income / Expense	Yield / Rate
Earning assets						
Loans and leases: ¹						
Commercial loans and leases	\$ 160,170	\$ 1,929	4.79 %	\$ 149,237	\$ 1,798	4.78 %
Commercial real estate	327,110	4,096	4.98	271,633	3,563	5.20
Construction and land	72,654	827	4.53	68,284	816	4.74
Residential real estate	228,963	2,389	4.15	146,785	1,611	4.35
Consumer	5,213	70	5.34	4,111	56	5.42
Total loans and leases	794,110	9,311	4.66	640,050	7,844	4.86
Loans held for sale	44,739	373	3.32	62,555	561	3.56
Other earning assets ²	29,405	34	0.46	25,434	16	0.25
Securities: ³						
U.S. Treasury	1,515	3	0.79	478	10	
U.S. Gov agencies	39,353	52	0.53	37,040	26	0.28
Mortgage-backed	33	-	-	4,832	1	0.06
Other investments	4,835	51	4.20	4,002	31	3.05
Total securities	45,736	106	0.92	46,352	68	0.58
Total earning assets	913,990	9,824	4.28	774,391	8,489	4.35
Cash and due from banks	7,421			7,163		
Bank premises and equipment, net	20,447			17,260		
Other assets	30,821			13,844		
Less: allowance for credit losses	(5,896)			(4,334)		
Total assets	\$966,783			\$808,324		
Interest-bearing liabilities						
Deposits:						
Interest-bearing demand accounts	\$57,396	33	0.23 %	\$47,017	\$ 25	0.21 %
Money market	257,133	300	0.46	176,851	211	0.47
Savings	51,487	17	0.13	41,236	16	0.15
Time deposits	238,791	541	0.90	222,690	441	0.79
Total interest-bearing deposits	604,807	891	0.59	487,794	693	0.56
Short-term borrowings	57,768	169	1.16	53,554	43	0.32
Long-term borrowings	26,656	116	1.73	23,163	72	1.23
Total interest-bearing funds	689,231	1,176	0.68	564,511	808	0.57
Noninterest-bearing deposits	189,194			151,410		
Other liabilities and accrued expenses	6,159			6,792		
Total liabilities	884,584			722,713		
Shareholders' equity	82,199			85,611		
Total liabilities & shareholders' equity	\$966,783			\$808,324		
Net interest rate spread ⁴		\$ 8,648	3.60 %		\$ 7,681	3.78 %
Effect of noninterest-bearing funds			0.17			0.16
Net interest margin on earning assets ⁵			3.76 %			3.94 %

(1)

Edgar Filing: Howard Bancorp Inc - Form 10-Q

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

(2) *Includes Federal funds sold and interest-bearing deposits with banks*

(3) *Available for sale securities are presented at amortized cost.*

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

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

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 of the changes set forth in the rate and volume columns are presented in the total column.

(in thousands)	Nine months ended September 30, 2016 vs. 2015			Three months ended September 30, 2016 vs. 2015		
	Total	Rates	Volumes ¹	Total	Rates	Volumes ¹
Interest earned on:						
Loans and leases:						
Commercial loans and leases	\$ 957	\$ 107	\$ 850	\$ 131	\$ 4	\$ 127
Commercial real estate	1,540	(669)	2,209	533	(152)	685
Construction and land	234	(37)	271	11	(37)	48
Residential real estate	2,862	(280)	3,142	778	(75)	853
Consumer	-	(9)	9	14	(1)	15
Loans held for sale	(178)	(62)	(116)	(188)	(38)	(150)
Taxable securities	120	45	75	38	40	(2)
Other earning assets	55	29	26	18	13	5
Total interest income	5,590	(876)	6,466	1,335	(246)	1,581
Interest paid on:						
Savings deposits	14	(3)	17	1	(2)	3
Interest-bearing demand deposits	26	5	21	8	2	6
Money market accounts	319	(16)	335	89	(4)	93
Time deposits	333	161	172	100	65	35
Short-term borrowings	282	214	68	126	114	12
Long-term borrowings	197	67	130	44	29	15
Total interest expense	1,171	428	743	368	204	164
Net interest earned	\$ 4,419	\$ (1,304)	\$ 5,723	\$ 967	\$ (450)	\$ 1,417

(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, 2016 and September 30, 2015 is presented below.

General

Net income available to common shareholders increased \$3.6 million, or 645.6%, to \$4.2 million for the nine months ended September 30, 2016 compared to \$561 thousand for the same period in 2015. The increase in net income available to common shareholders was primarily driven by a \$6.9 million increase in revenues (net interest income plus noninterest income) partially offset by a \$1.5 million increase in noninterest expense. Much of this revenue growth and the increased operating expenses are attributable the balance sheet growth resulting from our continued strategic and organic growth initiatives.

Interest Income

Interest income increased \$5.6 million, or 23.9%, to \$29.0 million for the nine months ended September 30, 2016 compared to \$23.4 million for the same period in 2015. The increase was almost entirely due to a \$5.4 million, or 23.4%, increase in interest and fees on loans and leases (including loans held for sale). The increase in interest and fees on loans and leases, in turn, was due to a \$184.8 million or 29.9% increase in the average balance of loans and leases, largely as a result of the Patapsco Bancorp acquisition, partially offset by a 23 basis point decrease in the yield on these assets. Increases in interest and dividends on securities and other interest income, as a result of increased average volumes and average yield on these assets, also contributed to the increase in total interest income.

Interest Expense

Interest expense increased \$1.2 million, or 54.4%, to \$3.3 million for the nine months ended September 30, 2016, compared to \$2.2 million for the same period in 2015. Interest expense on deposits increased \$692 thousand or 37.1% period over period as a direct result of the \$151.0 million or 33.8% increase in average interest-bearing deposits we experienced, largely attributable to the deposits we acquired in the Patapsco Bancorp acquisition. Overall, the average rate paid on our interest-bearing deposits remained relatively unchanged when comparing the first nine months of 2016 to the same period in 2015. We were able to keep our cost of funds stable despite the 10 basis point increases in the average rates paid on time deposits by attracting and maintaining lower-cost money market accounts. Average money market balances grew 62.3% when comparing the nine months ended September 30, 2016 to the same period last year, while the average rate on these deposits decreased slightly over the same period in 2015.

Interest expense on borrowings increased \$479 thousand or 167.5% period over period as a result of increases in both the average volume and average rate of our borrowings. There were two main reasons for these increases. The first was an increase in the average balance of and average rate on our long-term borrowings resulting from the \$3.4 million of debt we assumed in the Patapsco Bancorp acquisition. The second was the increase in the average balance of and the average rate paid on our short-term borrowings resulting from the \$12.6 million variable rate debt we incurred to fund the redemption of our outstanding preferred stock as discussed above. It is important to note that while our Series AA Preferred Stock was outstanding we were paying a dividend on the stock, which was not a component of interest expense, while the additional \$12.6 million in borrowings used to redeem the preferred stock has associated interest payments, which is now a component of interest expense.

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 \$4.4 million, or 20.8%, during the nine months ended September 30, 2016 compared to the nine months ended September 30, 2015. As would be expected, the impact of the additional interest expense on increased borrowing used to redeem our outstanding Series AA Preferred Stock as well as reduction in loan yields resulted in a decrease in our net interest margin from 4.05% for the first nine months of 2015 to 3.78% for the first nine months of 2016.

Provision for Credit Losses

We establish a provision for credit losses, which is a charge to earnings, in order to maintain the allowance for credit losses at a level we consider adequate to absorb credit losses incurred in the loan portfolio that are both probable and reasonably estimable at the balance sheet date. In determining the level of the allowance for credit losses, management considers past and current loss experience, evaluations of real estate collateral, current economic conditions, volume and type of lending, adverse situations that may affect a borrower's ability to repay a loan and the levels of

nonperforming loans. The amount of the allowance is based on estimates and actual losses may vary from such estimates as more information becomes available or economic conditions change. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as circumstances change as more information becomes available. The allowance for credit losses is assessed on a quarterly basis and provisions are made for credit losses as required in order to maintain the allowance.

Based on management's evaluation of the above factors, we had a provision for credit losses of \$1.3 million for the nine months ended September 30, 2016 compared to \$1.0 million for the same period in 2015, an increase of \$287 thousand or 28.3%. The provision for 2016 reflects additional general provisions that are required given the continued growth in the size of our loan portfolio, while maintaining specific provisions required on loans that are individually evaluated and deemed to be impaired.

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

Noninterest Income

Noninterest income was \$11.8 million for the nine months ended September 30, 2016 compared to \$9.0 million for the nine months ended September 30, 2015, a \$2.8 million or 30.5% increase. Noninterest income levels during 2016 continue to be driven by growth in our mortgage banking activities. Due to higher levels of mortgage loans sold into the secondary market, realized and unrealized gains on the sale of loans produced approximately \$7.0 million in noninterest revenues for the first nine months of 2016 compared to \$5.4 million for the same period of 2015. Noninterest income also benefited from a \$652 thousand one-time gain on the sale of an acquired impaired loan during the second quarter of 2016 partially offset by a \$40 thousand loss on a similar credit in the third quarter of 2016. In addition, earnings on bank owned life insurance ("BOLI") increased \$183 thousand comparing the first nine months of 2016 to the first nine months of 2015 as a result of the Bank purchasing an additional \$2.2 million in BOLI in January 2016, as well as the addition of the BOLI acquired in the Patapsco Bancorp acquisition. Loan fee income, which is associated with the origination of portfolio and held for sale loans, increased \$491 thousand as a direct result of the increase in the number of loans originated period over period.

Noninterest Expenses

Noninterest expenses increased \$1.5 million, or 5.5%, to \$29.4 million for the nine months ended September 30, 2016 from \$27.8 million for the same period of 2015. The primary driver in noninterest expense variances was the impact of the Patapsco Bancorp acquisition. Incremental infrastructure and increased staffing to support growth continue to contribute to rising noninterest expenses, while the lack of merger and restructuring costs associated with the acquisition, which were \$3.3 million during the nine months ended September 30, 2015, mitigated the impact of many of the increased non-interest expenses during the 2016 period.

Compensation and benefit expenses, which increased \$1.9 million or 15.6% when comparing the nine months ended September 30, 2016 to the nine months ended September 30, 2015, continue to represent the largest percentage of noninterest expense. The increased compensation and benefit costs resulted from the effects of successfully attracting a sizable commercial loan origination team and the larger infrastructure (including acquired branches) resulting from the Patapsco Bancorp acquisition as well as continuing organic growth in both portfolio and mortgage loan originations. In this regard, the number of our full time equivalent (FTE) employees increased from 220 at September 30, 2015 to nearly 270 at September 30, 2016. In addition, occupancy and equipment expense for the 2016 period increased \$815 thousand compared to the nine months ended September 30, 2015 due to the increased number of locations we operated during the 2016 period compared to the nine months ended September 30, 2015. Additionally, we incurred approximately \$500 thousand in occupancy cost to exit lease agreements on three branch locations that we closed in the second quarter of 2016.

Growth initiatives and the implementation of mobile banking and other electronic banking delivery channels continued to result in increases in many of our noninterest expenses during 2016. Cost increases related to this expansion when comparing the nine months ended September 30, 2016 to the same period last year include: marketing and business development - \$382 thousand; professional fees - \$612 thousand; data processing - \$371 thousand; and FDIC assessment - \$289 thousand. In addition, loan production expense, which includes costs related to originating, closing and securitizing loans, including both loans placed in our portfolio and loans held for sale, increased \$761 thousand to \$2.3 million during the nine months ended September 30, 2016 as a result of the increased number of loans originated during the 2016 period compared to the comparable period of 2015.

Net Income Available to Common Shareholders

Net income available to common shareholders for the nine months ended September 30, 2016 increased \$3.6 million to \$4.2 million compared to net income available to common shareholders of \$561 thousand for the nine months ended September 30, 2015. This increase was due to the increases in net interest income and noninterest income partially offset by an increase in noninterest expenses, as discussed above.

Pretax income increased by \$5.4 million from \$1.4 million in the first nine months of 2015 to \$6.8 million in the first nine months of 2016.

Basic earnings per common share (EPS) for the first nine months of 2016 were \$0.60 compared to \$0.09 for the same nine month period in 2015, representing an increase of \$0.51. This significant EPS growth was achieved even with the 18% increase in the average shares outstanding for 2016 resulting from our common stock offering in June 2015 and shares issued in the Patapsco Bancorp acquisition in the third quarter of 2015.

A comparison between the three months ended September 30, 2016 and September 30, 2015 is presented below.

General

Net income available to common shareholders increased \$2.6 million, or over 100%, to \$1.7 million for the three months ended September 30, 2016 compared to a loss of \$817 thousand for the three months ended September 30, 2015. This resulted in basic earnings per common share of \$0.25 for the third quarter 2016 compared to a loss of \$0.13 for the same period of 2015.

Interest Income

Interest income increased \$1.3 million, or 15.7%, to \$9.8 million for the three months ended September 30, 2016 compared to \$8.5 million for the same period of 2015. The increase was almost entirely due to a \$1.3 million, or 15.2%, increase in interest income and fees on loans and leases (including loans held for sale). This increase, in turn, resulted from a \$136.2 million increase in average loan and lease balances, primarily as a result of the Patapsco Bancorp acquisition, partially offset by a 16 basis point decrease in the average yield on these assets when comparing the three months ended September 30, 2016 to the same period of 2015. In addition, the average balance of securities decreased slightly, by \$616 thousand, while their average yield increased 34 basis points during the third quarter of 2016 compared to the same period in the prior year, resulting in increased interest and dividends on securities income of \$38 thousand or 56.0% quarter over quarter.

Interest Expense

Interest expense increased \$368 thousand, or 45.5%, to \$1.2 million for the three months ended September 30, 2016, compared to \$808 thousand for the same period of 2015. Deposit interest expense increased \$198 thousand and interest on borrowings increased \$170 thousand quarter over quarter. These increases were the result of increases in both the average balance of and average rates paid on interest-bearing deposits and borrowings. Average interest bearing deposits grew \$117.0 million or 24.0% quarter over quarter driven primarily by the deposits acquired in the Patapsco Bancorp acquisition, while the primary reason for the \$7.7 million or 10.0% increase in borrowing levels was the \$3.4 million of debt we assumed in the Patapsco Bancorp acquisition and the \$12.6 million variable rate debt we incurred to fund the redemption of our Series AA Preferred Stock, as discussed above. The average rate paid on our interest-bearing liabilities increased to 0.68% during the three months ended September 30, 2016 from 0.57% during the same period of 2015; the rate paid on our deposits increased three basis points, while the average rate paid on our borrowings increased 74 basis points during the three months ended September 30, 2016 compared to the same period of 2015 as a result of the acquired Patapsco Bancorp debt and the debt used to redeem the preferred stock.

Net Interest Income

As a result of the changes in our interest income and interest expense discussed above, our net interest income increased \$967 thousand, or 12.6%, during the three months ended September 30, 2016 compared to the three months ended September 30, 2015. As is to be expected given the 45.5% increase in interest expense, driven largely by the additional borrowings to fund the preferred stock redemption, while interest income grew only 15.7% during the third quarter of 2016 versus the same period in 2015, our net interest margin decreased from 3.94% for the third quarter of 2015 to 3.76% for the third quarter of 2016.

Provision for Credit Losses

Based on management's evaluation of all of the relevant loan loss methodology factors, we had a provision for credit losses of \$402 thousand for the three months ended September 30, 2016 compared to \$230 thousand for the same period in 2015, an increase of \$172 thousand or 74.8%.

Noninterest Income

Noninterest income was \$4.4 million for the three months ended September 30, 2016 compared to \$3.3 million for the three months ended September 30, 2015, a \$1.1 million or 34.6% increase. This increase was primarily due to increases of \$937 thousand in income generated from the mortgage banking activities, \$149 thousand in loan fee income and \$53 thousand in BOLI income, partially offset by a \$40 thousand loss on the sale of an impaired loan during the 2016 period, when comparing the third quarter of 2016 to the third quarter of 2015.

Noninterest Expenses

Noninterest expenses decreased by \$1.7 million, or 14.8%, during the three months ended September 30, 2016 compared to the three months ended September 30, 2015. The largest contributor to this decrease was the \$2.2 million decrease in merger and restructuring costs as a result of incurring no such costs during the 2016 period; such expenses incurred during the 2015 period were related to the NBRFS Financial Bank (which we acquired in 2014) systems conversion and the Patapsco Bancorp acquisition. As discussed above with respect to the nine month period comparison, increased costs to support expanding infrastructure, growth initiatives and delivery strategies are the primary reason for the increases in many noninterest expense categories quarter over quarter. In this regard, increases quarter over quarter were compensation and employee benefits of \$275 thousand, occupancy of \$131 thousand, professional fees of \$283 thousand, data processing cost of \$176 thousand, and loan production cost of \$117 thousand.

Nonperforming and Problem Assets

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

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

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

(in thousands)	September 30, 2016	December 31, 2015		
Non-accrual loans:				
Real estate loans:				
Residential - first lien	\$ 462	\$	693	
Residential - junior lien	28		63	
Commercial	1,594		1,148	
Commercial and leases	3,738		5,935	
Consumer	140		150	
Total non-accrual loans	5,962		7,989	
Accruing troubled debt restructured loans:				
Real estate loans:				
Construction and land	413	-		
Residential - first lien	296		301	
Commercial	2,514		2,073	
Commercial and leases	198		7	
Total accruing troubled debt restructured loans	3,421		2,381	
Total non-performing loans	9,383		10,370	
Other real estate owned:				
Land	1,220		964	
Commercial	1,323		1,405	
Total other real estate owned	2,543		2,369	
Total non-performing assets	\$ 11,926	\$	12,739	
Ratios:				
Non-performing loans to total gross loans	1.15	%	1.36	%
Non-performing assets to total assets	1.18	%	1.35	%

Included in non-accrual loans at September 30, 2016 are three troubled debt restructured loans totaling \$810 thousand that were not performing in accordance with their modified terms, and the accrual of interest has ceased. Further, there were seven troubled debt restructured loans totaling \$3.4 million performing subject to their modified terms at September 30, 2016. At September 30, 2016, loans 90 days or more past due and still accruing interest consisted of the following:

- One construction and land loan in the amount of \$2 thousand.
- Two residential junior liens totaling \$9 thousand.
- Two consumer loans totaling \$28 thousand.

Under GAAP, we are required to account for certain loan modifications or restructurings as “troubled debt restructurings.” In general, the modification or restructuring of a debt constitutes a troubled debt restructuring if the 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. A debt restructuring or loan modification for a borrower, however, does not necessarily constitute a troubled debt restructuring.

Nonperforming assets amounted to \$11.9 million, or 1.18% of total assets, at September 30, 2016 compared to \$12.7 million, or 1.35% of total assets, at December 31, 2015. Total nonperforming assets decreased \$813 thousand or 6.4% during the first nine months of 2016. There was an additional valuation allowance of \$83 thousand recorded on one property during the first nine months of 2016 as the current appraised value, less estimated cost to sell, was not sufficient to cover the recorded OREO amount.

The composition of our nonperforming loans at September 30, 2016 is further described below:

Non-Accrual Loans:

Two residential first lien loans totaling \$462 thousand.

Two residential junior liens totaling \$28 thousand.

Two commercial owner occupied loans totaling \$519 thousand.

- Six commercial non-owner occupied loans totaling \$1.1 million, four of which represent one relationship.
- 28 commercial loans totaling \$3.7 million, seven with a Small Business Administration (“SBA”) guarantee and eight that include a specific reserve totaling \$1.3 million.
 - One consumer loan in the amount of \$140 thousand with a specific reserve of \$72 thousand.

Accruing Troubled Debt Restructured Loans:

- Two construction and land loans totaling \$413 thousand.
- One residential first lien in the amount of \$296 thousand.
- One owner occupied commercial real estate loan in the amount of \$441 thousand
- One non-owner occupied commercial real estate loan in the amount of \$2.1 million.
- Two commercial loans totaling \$198 thousand.

Allowance for Credit Losses

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

Specific allowances are established for loans classified as Substandard or Doubtful. For loans classified as impaired, the allowance is established when the net realizable value (collateral value less costs to sell) of the impaired loan is lower than the carrying amount of the loan. The amount of impairment provided for as a specific allowance is 1) 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 2) classification. We apply an estimated loss rate to each loan group. The loss rates applied are based upon our loss experience adjusted, as appropriate, for the qualitative factors discussed below. This evaluation is inherently subjective, as it requires material estimates that may be susceptible to significant revisions based upon changes in economic and real estate market conditions.

The allowance for credit losses is maintained at a level to provide for losses that are probable and can be reasonably estimated. Management’s periodic evaluation of the adequacy of the allowance is based on Howard Bank’s past credit

loss experience, known and inherent losses in the portfolio, adverse situations that may affect the borrower's ability to repay, the estimated value of any underlying collateral, composition of the loan portfolio, current economic conditions and other relevant factors. This evaluation is inherently subjective as it requires material estimates that may be susceptible to significant change, including the amounts and timing of future cash flows expected to be received on impaired loans.

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

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

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

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

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

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

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

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

At September 30, 2016 and December 31, 2015, nonperforming loans were \$9.4 million and \$10.4 million, respectively. The amount of impaired loans requiring specific reserves totaled \$1.4 million at September 30, 2016 and \$1.3 million at December 31, 2015. The amount of impaired loans not in need of a specific valuation allowance totaled \$7.8 million and \$10.0 million, respectively, at such dates.

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

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

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

(in thousands)	Nine months ended September 30, 2016		Twelve months ended December 31, 2015	
Balance at beginning of year	\$	4,869	\$	3,602
Charge-offs:				
Real estate				
Construction and land loans	(216)	-	
Residential first lien loans	-		(23)
Residential junior lien loans	-		(12)
Commercial owner occupied loans	(191)	-	
Commercial non-owner occupied loans	-		(82)
Commercial loans and leases	(233	)	(825)
Consumer loans	(15	)	(5)
	(655	)	(947)
Recoveries:				
Real estate				
Construction and land loans	-		-	
Residential first lien loans	-		3	
Residential junior lien loans	-		1	
Commercial owner occupied loans	40		-	
Commercial non-owner occupied loans	4		318	
Commercial loans and leases	45		52	
Consumer loans	29		4	
	118		378	
Net charge-offs	(537	)	(569)
Provision for credit losses	1,302		1,836	
Balance at end of year	\$	5,634	\$	4,869
Net charge-offs to average loans and leases	0.069	%	0.090	%

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, 2016		December 31, 2015	
	Amount	Percent ¹	Amount	Percent 1

Edgar Filing: Howard Bancorp Inc - Form 10-Q

Real estate

Construction and land loans	\$ 580	9.1	%	\$ 265	9.1	%
Residential first lien loans	450	24.4		300	24.1	
Residential junior lien loans	87	4.2		47	3.6	
Commercial owner occupied loans	333	16.5		309	17.3	
Commercial non-owner occupied loans	1,105	24.9		728	23.9	
Commercial loans and leases	2,924	20.3		3,094	21.5	
Consumer loans	155	0.6		126	0.6	
Total	\$ 5,634	100.0	%	\$ 4,869	100.0	%

(1) Represents the percent of loans in each category to total loans, not the composition of the allowance for credit losses.

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, 2016 and December 31, 2015. 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, 2016 and December 31, 2015, cash and cash equivalents totaled \$43.9 million and \$38.3 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, 2016 and December 31, 2015, we had \$130.8 million and \$167.7 million, respectively, in loan commitments outstanding, including commitments issued to originate loans of \$55.2 million and \$95.0 million at September 30, 2016 and December 31, 2015, respectively, and \$75.6 million and \$72.7 million in unused lines of credit to borrowers at September 30, 2016 and December 31, 2015, respectively. In addition to commitments to originate loans and unused lines of credit we had \$6.9 million and \$7.8 million in letters of credit at September 30, 2016 and December 31, 2015, respectively. Certificates of deposit due within one year of September 30, 2016 totaled \$164.7 million, or 20.5% of total deposits. If we do not retain these deposits, 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 first nine months of 2016 cash was utilized to increase our portfolio of loans by \$56.8 million. For the same period of 2015, cash used to fund our loan portfolio totaled \$47.5 million. During the first nine months of 2016 we utilized cash to purchase additional securities totaling \$65.6 million while receiving \$77.5 million as a result of securities maturing. For the same period in 2015 we purchased additional securities totaling \$13.9 million and we received \$42.5 million in security maturities. During the first nine months of 2016, we invested \$19.5 million in short term certificates of deposit at other financial institutions.

Financing activities consist primarily of activity in deposit accounts and FHLB advances. We experienced a net increase in deposits of \$56.4 million during the nine months ended September 30, 2016. Deposit flows are affected by the overall level of interest rates, the interest rates and products offered by us and our local competitors, and by other factors.

Liquidity management is both a daily and long-term function of business management. If we require funds beyond our ability to generate them internally, borrowing agreements exist with the FHLB that provide an additional source of funds. FHLB advances were \$91.5 million at September 30, 2016 compared to \$78.5 million at December 31, 2015. At September 30, 2016, we had the ability to borrow up to a total of \$217.0 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, 2016 and December 31, 2015, 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, 2016 and December 31, 2015 are as follows:

(in thousands)	September 30, 2016	December 31, 2015
Unfunded loan commitments	\$ 55,182	\$ 95,009
Unused lines of credit	75,643	72,664
Letters of credit	6,861	7,848

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, 2016 or December 31, 2015 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, 2016. 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, 2016, 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, 2015, as filed with the SEC on March 30, 2016.

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

None

Item 3. Defaults Upon Senior Securities

None

Item 4. Mine Safety Disclosures

Not applicable

Item 5. Other Information

None

Item 6. Exhibits

31(a) Certification of Chief Executive Officer pursuant to Rule 13a-14(a) or 15d-14(a) of the Exchange Act pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 - filed herewith

31(b) Certification of Chief Financial Officer pursuant to Rule 13a-14(a) or 15d-14(a) of the Exchange Act pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 - filed herewith

32 Certifications pursuant to 18 U.S.C. Section 1350, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 – filed herewith

101 Extensible Business Reporting Language (“XBRL”) – filed herewith

101.INS XBRL Instance File

101.SCH XBRL Schema File

101.CAL XBRL Calculation File

101.DEF XBRL Definition File

101.LAB XBRL Label File

101.PRE XBRL Presentation File

47

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 14, 2016 /s/ Mary Ann Scully
Date MARY ANN SCULLY
PRESIDENT AND CEO

November 14, 2016 /s/ George C. Coffman
Date GEORGE C. COFFMAN
EVP AND CFO