Maryland Financial Bank

"Your Partner in Correspondent Banking"

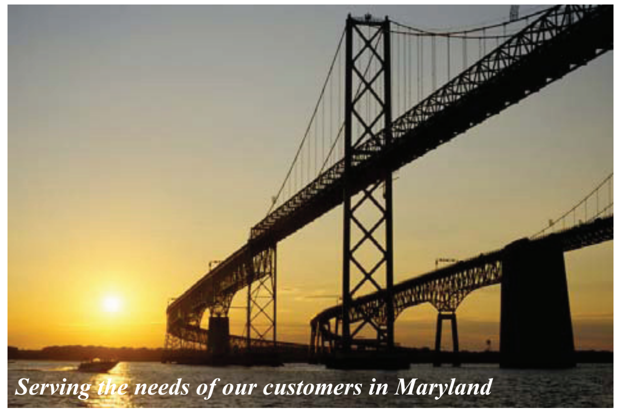
2009 Annual Report

MARYLAND FINANCIAL BANK

April 2, 2010

Dear Fellow Shareholders:

Are you tired of reading and hearing about how bad things are: the worst economic conditions since the Great Depression, 140 bank failures last year and who knows how many this year, massive federal deficits, regulatory reform, Wall Street vs. Main Street and, finally, the demise of commercial real estate?



Serving the needs of our customers in Maryland

We can't do anything about the above issues, but I can tell you that your management team is working hard to make sure your Bank not only survives but prospers in the next several years. We are clearly focused on the following:

- Asset quality
- Strong liquidity
- Profitability
- Capital levels that exceed those required to be well capitalized
- Measured loan growth to support our community bank customers

So how did your Bank do last year in the face of so many economic challenges and uncertainties? We posted a loss of $245,000, but this was due to $903,000 being added to our allowance for loan losses. We did not have any actual loan losses. We built our liquidity, maintained our well capitalized status, enhanced our credit practices, and continued to support our community bank customers by purchasing loans and growing the portfolio by 16%.

We participated in the Treasury Capital Purchase program for two reasons: first, we were approved to participate, and, second, we needed capital to continue to execute our business plan. Notwithstanding what you read in the paper about banks not making loans with the CPP capital, we used the capital to grow our loan portfolio in support of local community banks.

Our vision for the future is very clear and has remained the same since we opened our doors in October 2004: "Enhance stockholder and client value by being the premier facilitator of correspondent banking and credit services in the mid-Atlantic region."

Thank you for your continued support, and please feel free to contact me at any time as your comments are always appreciated.

Sincerely,

Richard E. Hook, IV
Chairman of the Board

MARYLAND FINANCIAL BANK

April 2, 2010

Dear Fellow Shareholders:

Let me please take this opportunity to outline for you my thoughts, concerns, and hopes for Maryland Financial Bank.

Serving the needs of our customers in Washington

Our operating results for the year ended December 31, 2009 produced a net loss of $245 thousand as compared to a net loss of $243 thousand for the year ended December 31, 2008. While we are disappointed that we could not produce a profit for the year, we felt the need to take a very aggressive stance towards bolstering the allowance for loan losses, with provisions of $903 thousand, versus $372 thousand in 2008.

Total assets grew by 22% to $83 million at December 31, 2009, as compared to $68 million at December 31, 2008. The bank produced solid loan growth of 16% to $62 million at December 31, 2009 compared to $54 million at December 31, 2008. This growth was primarily funded with stable term certificates of deposits. Certificate of deposits increased by 32%, during 2009, to $48 million at year end. Our net interest spread improved to approximately 3% at year end from 2% in 2008. This was mostly due to the repricing of CDs at lower interest rates. The one area of concern was the decline in credit quality. Non-performing assets increased to $3 million at December 31, 2009, from $900 thousand at December 31, 2008. Our focus in 2010 is to reduce the level of non-performing assets.

Capital remains precious, which is why we have limited our growth. We intend to maintain our capital ratios in excess of the regulatory requirements to be considered well capitalized. At December 31, 2009 our tier one leverage capital ratio was 7.5%, our tier one risk-based capital ratio was 10.3%, and our total risk-based capital ratio was 11.6%.

As noted in most financial institution annual reports, 2009 was a challenging year, and this was true for MFB. However, 2010 and beyond looks promising. We've grown the bank to the size where the efficiencies of a banker's bank are being realized. Our efficiency ratios have improved, our margins have improved, and our asset liability mix has improved.

It should also be noted, that the success we have enjoyed is a direct result of the assistance and support of our customers, Board of Directors, Board of Advisors, employees, strategic partners, and our networking partners. And finally, I want to thank you, our shareholder, for your support!

Sincerely,

R. Chafey

Robert R. Chafey
President & Chief Executive Officer

Maryland Financial Bank and Subsidiary

Consolidated Financial Statements

December 31, 2009

Maryland Financial Bank and Subsidiary

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ROWLES
& Company, LLP
Certified Public Accountants

Report of Independent Auditors

The Board of Directors and Stockholders
Maryland Financial Bank
Towson, Maryland

We have audited the accompanying consolidated balance sheet of Maryland Financial Bank and Subsidiary as of December 31, 2009, and the related consolidated statements of income, changes in stockholders' equity, and cash flows for the year then ended. These financial statements are the responsibility of the Bank's management. Our responsibility is to express an opinion on these financial statements based on our audit. The consolidated financial statements of Maryland Financial Bank and Subsidiary as of and for the year ended December 31, 2008, were audited by other auditors whose report dated April 9, 2009, expressed an unqualified opinion on those statements.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Bank's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Maryland Financial Bank and Subsidiary as of December 31, 2009, and the consolidated results of its operations and its cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

Rowles & Company, LLP

Baltimore, Maryland
March 30, 2010

101 E. Chesapeake Avenue, Suite 300, Baltimore, Maryland 21286
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Maryland Financial Bank and Subsidiary

Consolidated Balance Sheets

December 31,	2009	2008
	(Dollars in thousands)	
Assets		
Cash and due from banks	**$ 106**	$ 81
Interest-bearing deposits in other banks	**16,633**	10,352
Federal funds sold	**-**	133
Cash and cash equivalents	**16,739**	10,566
Time deposits in other banks	**198**	198
Securities available for sale	**4,983**	3,863
Federal Home Loan Bank stock, at cost	**123**	98
Loans, net of allowance for loan losses of **$1,693** and $790	**60,231**	52,722
Bank premises and equipment, net	**73**	101
Accrued interest receivable	**252**	264
Deferred income taxes	**118**	118
Other assets	**439**	119
	$ 83,156	$ 68,049
Liabilities and Stockholders' Equity		
Deposits		
Noninterest-bearing	**$ 2,347**	$ 2,505
Interest-bearing time deposits	**47,539**	36,043
Total deposits	**49,886**	38,548
Federal funds purchased	**26,077**	23,606
Other liabilities	**352**	520
	76,315	62,674
Stockholders' equity		
Preferred stock and additional paid-in capital; authorized 5,000,000 shares, issued and outstanding 1,785 shares in 2009	**1,705**	-
Common stock, $10 par value; authorized 5,000,000 shares; issued and outstanding 373,688 shares	**3,737**	3,737
Additional paid-in capital	**3,674**	3,668
Accumulated deficit	**(2,300)**	(2,055)
Accumulated other comprehensive income	**25**	25
	6,841	5,375
	$ 83,156	$ 68,049

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

Maryland Financial Bank and Subsidiary

Consolidated Statements of Income

Years Ended December 31,	**2009**	2008
	(Dollars in thousands)	
Interest and dividend revenue		
Loans, including fees	**$ 3,270**	$ 3,221
Securities available for sale	**87**	159
Federal funds sold	**-**	193
Other	**44**	46
Total interest income	**3,401**	3,619
Interest expense		
Deposits	**1,160**	1,615
Federal funds purchased	**74**	459
Other borrowings	**-**	2
Total interest expense	**1,234**	2,076
Net interest income	**2,167**	1,543
Provision for loan losses	**903**	372
Net interest income after provision for loan losses	**1,264**	1,171
Noninterest revenue		
Consulting fees	**280**	203
Other	**135**	102
Total noninterest revenue	**415**	305
Noninterest expenses		
Salaries and employee benefits	**1,183**	1,115
Occupancy and equipment	**164**	177
Data processing	**128**	99
Marketing and promotion	**14**	58
Professional fees	**124**	114
Other	**262**	156
Total noninterest expenses	**1,875**	1,719
Loss before income taxes	**(196)**	(243)
Income taxes	**-**	-
Net loss	**(196)**	(243)
Preferred stock dividends and discount accretion	**49**	-
Net loss to common shareholders	**$ (245)**	$ (243)
Loss per common share	**$ (0.66)**	$ (0.65)

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

Maryland Financial Bank and Subsidiary

Consolidated Statements of Changes in Stockholders' Equity

	Preferred stock	Common stock	Additional paid-in capital	Accumulated deficit	Accumulated other comprehensive income (loss)	Comprehensive loss
Balance, December 31, 2007	**$ -**	$ 3,737	$ 3,662	$ (1,812)	$ (34)	
Net loss	-	-	-	(243)	-	$ (243)
Unrealized gain on securities available for sale net of income taxes of $16	-	-	-	-	59	59
Total comprehensive loss						$ (184)
Stock-based compensation	-	-	6	-	-	
Balance, December 31, 2008	**-**	3,737	3,668	(2,055)	25	
Net loss	-	-	-	(196)	-	$ (196)
Unrealized gain on securities available for sale net of income taxes of $-	-	-	-	-	-	-
Total comprehensive loss						$ (196)
Preferred shares issued to U.S. Department of the Treasury	1,691	-	-	-	-	
Preferred stock dividend and discount accretion	14	-	-	(49)	-	
Stock-based compensation	-	-	6	-	-	
Balance, December 31, 2009	**$ 1,705**	**$ 3,737**	**$ 3,674**	**$ (2,300)**	**$ 25**	

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

Maryland Financial Bank and Subsidiary

Consolidated Statements of Cash Flows

Years Ended December 31,	**2009**	2008
	(Dollars in thousands)	
Cash flows from operating activities		
Net loss	**$ (196)**	$ (243)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Provision for loan losses	**903**	372
Depreciation and amortization	**50**	51
Decrease in deferred loan fees, net	**(21)**	(36)
Net amortization of investment securities premiums	**53**	24
Stock-based compensation	**6**	6
Loss on disposition of premises and equipment	**1**	-
Decrease in accrued interest receivable	**12**	69
(Increase) decrease in other assets	**(324)**	16
Decrease in other liabilities	**(168)**	(11)
Net cash provided by operating activities	**316**	248
Cash flows from investing activities		
Proceeds from maturities and call of securities available for sale	**825**	4,343
Purchases of securities available for sale	**(1,998)**	(2,724)
Net change in Federal Home Loan Bank stock	**(25)**	86
Net increase in loans	**(8,391)**	(9,418)
Purchases of premises and equipment	**(19)**	(46)
Net cash used in investing activities	**(9,608)**	(7,759)
Cash flows from financing activities		
Net increase in federal funds purchased	**2,471**	11,142
Net increase in deposits	**11,338**	4,657
Repayment of advances from Federal Home Loan Bank	**-**	(1,750)
Proceeds from issuance of preferred stock	**1,691**	-
Preferred stock dividend paid	**(35)**	-
Net cash provided by financing activities	**15,465**	14,049
Net increase in cash and cash equivalents	**6,173**	6,538
Cash and cash equivalents at beginning of year	**10,566**	4,028
Cash and cash equivalents at end of year	**$ 16,739**	$10,566
Supplementary cash flows information		
Interest paid	**$ 1,251**	$ 2,218

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

Maryland Financial Bank and Subsidiary

Notes to Consolidated Financial Statements
(Dollars in thousands)

1. Summary of Significant Accounting Policies

Organization and nature of operations

Maryland Financial Bank (the Bank) was incorporated on July 7, 2004, under the laws of the State of Maryland and commenced operations on October 25, 2004. On March 1, 2005, MFB Advisory Services LLC was formed as a wholly-owned subsidiary of the Bank to provide consulting and advisory services, primarily credit reviews for other financial institutions.

As a state chartered bank, the Bank is subject to regulation by the FDIC and the Maryland Commissioner of Financial Regulation.

The Bank participates, through purchases, in commercial and commercial real estate loans with other financial institutions throughout Maryland and contiguous states and makes direct loans to officers and directors of financial institutions. The loan portfolio is generally collateralized by assets of the borrowers. A substantial portion of the Bank's loan portfolio is concentrated in the real estate industry. Therefore, its debtors' ability to repay their loans is dependent upon the real estate sector of the economy. The Bank accepts deposits and purchases federal funds from financial institutions.

Principles of consolidation

The consolidated financial statements include the accounts of Maryland Financial Bank and its wholly-owned subsidiary, MFB Advisory Services LLC. All intercompany accounts and transactions are eliminated in the consolidation.

Use of estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America 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 revenue and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses, the evaluation of other than temporary impairment of securities, and the valuation of deferred tax assets.

Cash and cash equivalents

For purposes of reporting cash flows, cash and cash equivalents include cash on hand, amounts due from banks, interest-bearing deposits in other banks and federal funds sold, all of which have initial maturities of 90 days or less. Generally, federal funds are purchased or sold for one-day periods.

Time deposits in other banks

Time deposits in other banks mature within one year and are carried at cost.

Concentration of credit risk

Most of the Bank's activities are with customers located within Maryland and contiguous states.

1. **Summary of Significant Accounting Policies** (Continued)

Securities available for sale

Securities classified as available for sale are those securities that the Bank intends to hold for an indefinite period of time but not necessarily to maturity. Securities available for sale are carried at fair value. Any decision to sell a security classified as available for sale would be based on various factors, including significant movement in interest rates, changes in maturity mix of the Bank's assets and liabilities, liquidity needs, regulatory capital considerations, and other similar factors. Unrealized gains and losses are reported as increases or decreases in other comprehensive income (loss). Realized gains or losses, determined on the basis of the cost of the specific securities sold, are included in earnings. Premiums and discounts are recognized in interest income using the interest method over the terms of the securities.

Declines in the fair value of securities below their cost that are deemed to be other than temporary are reflected in earnings as realized losses. In estimating other-than-temporary impairment losses, management considers (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, and (3) the intent and ability of the Bank to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value.

Loans

Loans are stated at their outstanding unpaid principal balances and any deferred fees or costs, net of the allowance for loan losses. Interest income is accrued on the unpaid principal balance. Loan origination fees, net of certain direct origination costs, are deferred and recognized as an adjustment of the yield of the related loans. The Bank generally amortizes these amounts over the contractual life of the loan.

The accrual of interest is discontinued when the contractual payment of principal or interest has become 90 days past due and collateral is insufficient to discharge the debt in full. Past due status is based on the contractual terms of the loan. A loan may remain on accrual status if it is in the process of collection and is either guaranteed or well secured. Interest received on nonaccrual loans generally is either applied against principal or reported as interest income, according to management's judgment as to the collectability of principal. Generally, loans are restored to accrual status when the obligation is brought current, has performed in accordance with the contractual terms for a reasonable period of time and the ultimate collectability of the total contractual principal and interest is no longer in doubt.

1. **Summary of Significant Accounting Policies** (Continued)

Allowance for loan losses

The allowance for loan losses is established through provisions for loan losses charged against income. Loans deemed to be uncollectable are charged against the allowance for loan losses, and subsequent recoveries, if any, are credited to the allowance.

The allowance for loan losses is maintained at a level considered adequate to provide for losses that can be reasonably anticipated. Management's periodic evaluation of the adequacy of the allowance is based on known and inherent risks 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.

The allowance consists of specific, general, and unallocated components. The specific component relates to loans that are classified as either doubtful or substandard. For such loans that are also classified as impaired, an allowance is established when the discounted cash flows or collateral value of the impaired loan is lower than the carrying value of that loan. The general component covers loans that are not adversely classified, and is based on historical loss experience adjusted for qualitative factors. An unallocated component is maintained to cover uncertainties that could affect management's estimate of probable losses. The unallocated component of the allowance reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating specific and general losses in the portfolio.

A loan is considered impaired when, based on current information and events, it is probable that the 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. Impairment is measured on a loan-by-loan basis for commercial and construction loans by either the present value of expected future cash flows discounted at the loan's effective interest rate or the fair value of the collateral if the loan is collateral dependent.

Large groups of smaller balance homogeneous loans are collectively evaluated for impairment.

Transfers of financial assets

Transfers of financial assets, including loan and loan participation sales, are accounted for as sales, when control of the assets has been surrendered. Control over transferred assets is deemed to be surrendered when (1) the assets have been isolated from the Bank, (2) the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets, and (3) the Bank does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

1. **Summary of Significant Accounting Policies** (Continued)

Bank premises and equipment

Bank premises and equipment are stated at cost less accumulated depreciation. Depreciation is computed on the straight-line method over the estimated useful lives of the related assets.

Investment in Federal Home Loan Bank of Atlanta stock

Investment in Federal Home Loan Bank of Atlanta (FHLB) stock is carried at cost. The Bank is required to maintain an investment in the stock of the FHLB based on its total assets and any outstanding advances from the FHLB.

Marketing and promotion expense

The Bank expenses marketing and promotion costs as they are incurred.

Income taxes

Deferred income taxes are provided on the asset/liability method whereby deferred tax assets are recognized for deductible temporary differences and deferred tax liabilities are recognized for taxable temporary differences. Temporary differences are the differences between the reported amounts of assets and liabilities and net operating loss carryforwards and their tax basis. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion of the deferred tax asset will not be realized. Deferred tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment.

Stock-based compensation

Stock-based compensation includes the cost of all stock-based payments granted subsequent to December 31, 2005, based on the grant date estimated fair value. Compensation cost is recognized ratably using the straight-line attribution method over the expected vesting period or to the retirement eligibility date, if less than the vesting period when vesting is not contingent upon any future performance.

Comprehensive income

Accounting principles generally require that recognized revenue, expenses, gains, and losses be included in net income (loss). Changes in the unrealized gains and losses on securities available for sale are reported as a separate component of the equity section of the balance sheet and included in comprehensive income (loss).

Off-balance-sheet financial instruments

In the ordinary course of business, the Bank has entered into off-balance-sheet financial instruments consisting of commitments to extend credit. Such financial instruments are recorded in the balance sheet when they are funded.

Reclassifications

Certain amounts in the 2008 consolidated financial statements have been reclassified to conform to the 2009 presentation. The reclassifications had no impact on net income.

(Dollars in thousands)

2. Securities Available for Sale

The amortized cost and fair value of securities available for sale, with gross unrealized gains and losses were as follows:

December 31, 2009	Amortized cost	Gross unrealized gains	Gross unrealized losses	Fair value
U.S. Treasury	**$ 2,004**	**$ 1**	**$ -**	**$ 2,005**
U.S. government agency	**2,146**	**29**	**-**	**2,175**
Mortgage-backed	**791**	**12**	**-**	**803**
	$ 4,941	**$ 42**	**$ -**	**$ 4,983**
December 31, 2008				
U.S. Treasury	$ 494	$ 5	$ -	$ 499
U.S. government agency	2,207	29	-	2,236
Mortgage-backed	1,121	7	-	1,128
	$ 3,822	$ 41	$ -	$ 3,863

Amortized cost and fair value at December 31, 2009 by contractual maturity are shown below. Expected maturities will differ from contractual maturities because issuers may have the right to call or prepay with or without penalties.

	Available for sale	
	Amortized cost	Fair value
Less than one year	**$ 3,535**	**$ 3,552**
After one year through five years	**615**	**628**
Mortgage-backed securities	**791**	**803**
	$ 4,941	**$ 4,983**

The Bank had no sales of securities available for sale during 2009 or 2008.

At December 31, 2009, all of the Bank's securities available for sale were pledged to secure Federal Home Loan Bank advances. At December 31, 2008, securities with carrying values of **$3,863** were pledged to secure Federal Home Loan Bank advances and Federal Reserve Bank daylight overdrafts.

(Dollars in thousands)

3. Loans

The composition of loans receivable at December 31, 2009 and 2008, is as follows:

	2009	2008
Commercial real estate	**$ 38,178**	$ 25,669
Construction and land development	**16,932**	18,752
Commercial	**2,986**	4,046
Consumer	**3,880**	5,118
Total loans	**61,976**	53,585
Less:		
Deferred loan fees and costs, net	**52**	73
Allowance for loan losses	**1,693**	790
	$ 60,231	$ 52,722

The changes in the allowance for loan losses for the years ended December 31, 2009 and 2008, are as follows:

	2009	2008
Balance, beginning	**$ 790**	$ 418
Provision for loan losses	**903**	372
Charge offs	**-**	-
Balance, ending	**$ 1,693**	$ 790

The following is a summary of information pertaining to impaired and nonaccrual loans as of and for the years ended December 31:

	2009	2008
Impaired loans without a valuation allowance	**$ -**	$ -
Impaired loans with a valuation allowance	**4,165**	2,903
Total impaired loans	**$ 4,165**	$ 2,903
Valuation allowance related to impaired loans	**$ 1,072**	$ 299
Total nonaccrual loans	**3,051**	935
Interest not accrued on nonaccrual loans	**194**	-
Total loans past due 90 days or more and still accruing	**-**	-
Average investment in impaired loans	**4,551**	3,416
Interest income recognized on impaired loans	**141**	170
Interest income recognized on a cash basis on impaired loans	**-**	-

The Bank was committed to advance **$128** and $151 in connection with impaired loans at December 31, 2009 and 2008, respectively.

4. Bank Premises and Equipment

The components of premises and equipment at December 31, 2009 and 2008, are as follows:

	Useful lives	**2009**	2008
Furniture, fixtures and equipment	5 to 7 years	**$ 151**	$ 152
Computer equipment	3 years	**136**	123
		287	275
Accumulated depreciation		**214**	174
		$ 73	$ 101
Depreciation expense		**$ 50**	$ 51

5. Interest-Bearing Time Deposits

The aggregate amount of interest-bearing time deposits in denominations of $100,000 or more was **$34,141** and $14,653 as of December 31, 2009 and 2008, respectively.

At December 31, 2009, the scheduled maturities of certificates of deposit are as follows (in thousands):

Year	Amount
2010	$ 26,317
2011	21,222
	$ 47,539

Included in certificates of deposit are brokered certificates of deposit of $793 and wholesale certificates of deposit of $3,964.

6. Federal Funds

Federal funds are reported on a gross basis. Federal funds sold are stated as assets and federal funds purchased are stated as liabilities. The average interest rate paid on federal funds purchased was 0.25% during the year ended December 31, 2008. Federal funds purchased mature daily. The weighted average interest rate on federal funds purchased was 0.25% at December 31, 2009.

7. Borrowings

As of December 31, 2009, the Bank has pledged real estate loans totaling **$26,960** to the Federal Reserve Bank of Richmond to provide a borrowing capacity of $12,821 under its discount window program.

The Bank has a $5 million line of credit available through the FHLB secured by a blanket floating lien on all assets. There were no advances outstanding on these lines at December 31, 2009 or 2008.

8. TARP Capital Purchase Program

On March 27, 2009, as part of the Troubled Asset Relief Program ("TARP") Capital Purchase Program ("CPP"), the Bank entered into a Letter Agreement and the related Securities Purchase Agreement – Standard Terms (collectively, the "Purchase Agreement") with the United States Department of the Treasury ("Treasury"), pursuant to which the Bank issued (1) 1,700 shares of Fixed Rate Non-Cumulative Perpetual Preferred Stock, Series A with liquidation preference of $1,000 per share ("Series A Preferred Stock"), and (2) a warrant to purchase an additional 85 shares of Fixed Rate Non-Cumulative Perpetual Preferred Stock, Series B ("Series B Preferred Stock"), for an aggregate purchase price of $1,700. The Series A Preferred Stock qualifies as Tier 1 capital and pays dividends at a rate of 5% per annum until May 15, 2014. Beginning May 15, 2014, the dividend rate will increase to 9% per annum. On and after May 15, 2012, the Bank may, at its option, redeem shares of Series A Preferred Stock, in whole or in part, at any time and from time to time, for cash at a per share amount equal to the sum of the liquidation preference per share plus any accrued and unpaid dividends to but excluding the redemption date. Prior to May 15, 2012, the Bank may redeem shares of Series A Preferred Stock only if it has received aggregate gross proceeds of not less than $425 from one or more qualified equity offerings, and the aggregate redemption price may not exceed the net proceeds received by the Bank from such offerings. The redemption of the Series A Preferred Stock requires prior regulatory approval. On March 27, 2009, the Treasury exercised all of the warrants on the Series B Preferred Stock at the liquidation price of $1,000 per share. The Series B Preferred Stock qualifies as Tier 1 capital and pays cumulative dividends at a rate of 9% per annum. The Series B Preferred Stock may not be redeemed until all the Series A Preferred Stock has been redeemed. The Series A Preferred Stock and Series B Preferred Stock were issued in a transaction exempt from registration pursuant to the Securities Act of 1933, as amended.

The Bank has not declared or paid dividends on the Series A or Series B preferred stock since August 15, 2009. In accordance with the Purchase Agreement, whenever the dividends payable on the shares have not been paid for an aggregate of six quarterly dividend periods or more, whether or not consecutive, the authorized number of directors of the Bank shall automatically be increased by two and the holders of the shares may elect two directors to fill the newly created directorships at the Bank's next annual meeting and at each subsequent annual meeting until full dividends have been paid on the shares for four consecutive quarters.

(Dollars in thousands)

9. Lease Commitments

In August 2004, the Bank entered into a five-year operating lease agreement for its banking office that commenced in October 2004. The Bank exercised its first renewal option effective November 1, 2010. The Bank has the option to extend the lease agreement for one additional five-year period. The Bank is also required to pay a monthly fee for its portion of certain operating expenses, including real estate taxes, insurance, utilities, maintenance and repairs above a base year amount in addition to the base rent.

The lease requires the following minimum payments:

Year	Payments
2010	$ 92
2011	94
2012	97
2013	100
2014	102
2015	9
	$ 494

Rent expense for the office and equipment leases for the years ended December 31, 2009 and 2008, totaled **$99** and $109, respectively.

10. Income Taxes

The Bank did not incur income tax expense during the years ended December 31, 2009 and 2008.

A reconciliation of the statutory income tax rate of 34% to the income tax expense (benefit) included in the statements of income is as follows for the years ended December 31, 2009 and 2008.

	2009	2008
Federal income tax at statutory rate	**34.0 %**	34.0 %
Nondeductible expenses	**4.9**	2.8
Change in valuation allowance	**(38.9)**	(36.8)
Effective income tax rate	**- %**	- %

(Dollars in thousands)

10. **Income Taxes** (Continued)

The components of the net deferred tax asset at December 31 are as follows:

	2009	2008
Deferred tax assets		
Net operating loss and charitable contribution carryforwards	**$ 516**	$ 663
Allowance for loan losses	**585**	229
Organization and start-up costs	**-**	33
Depreciation	**1**	-
	1,102	925
Valuation allowance	**(739)**	(689)
Total deferred tax assets, net of valuation allowance	**363**	236
Deferred tax liabilities		
Unrealized gain on securities available for sale	**16**	16
Cash basis accounting	**214**	76
Deferred loan costs	**15**	25
Depreciation	**-**	1
Total deferred tax liability	**245**	118
Net deferred tax asset	**$ 118**	$ 118

The Bank has net operating loss carryforwards available for federal and state income tax purposes of approximately $1,302, which begin to expire in 2024.

(Dollars in thousands)

11. Stock Options and Equity Incentive Plan

Under the 2005 Equity Incentive Plan (the Plan), the Bank is permitted to grant stock options (including incentive stock options within the meaning of Internal Revenue Code Section 422 and nonstatutory stock options), stock appreciation rights, restricted or unrestricted stock awards, phantom stock, performance awards, other stock-based awards, or any combination of the foregoing. The shares of common stock that may be issued with respect to awards granted under the Plan shall not exceed an aggregate of 75,000 shares of common stock over the life of the Plan. To date, only options have been granted under this plan. The exercise price of each option equals the fair value of the stock on the date of grant and an option's maximum term is ten years. Vesting periods range from five to seven years from date of grant.

Information regarding the stock options is presented below:

	Options	Weighted average exercise price	Weighted average remaining contractual life
Outstanding at January 1, 2008	49,358	$ 20	8.2
Granted in 2008	-	-	-
Exercised in 2008	-	-	-
Forfeited in 2008	-	-	-
Outstanding at December 31, 2008	49,358	20	7.2
Granted in 2009	-	-	-
Exercised in 2009	-	-	-
Forfeited in 2009	-	-	-
Outstanding at December 31, 2009	49,358	$ 20	6.2
Options exercisable at December 31, 2009	46,775	$ 20	5.7

The intrinsic value of options outstanding at December 31, 2009 and 2008 is $0. As of December 31, 2009, unrecognized compensation cost related to nonvested share-based compensation arrangements granted under the Plan is $16 and will be recognized over 2.6 years.

	Number of options	Weighted average grant date fair value
Nonvested options at January 1, 2009	9,439	$ 6.03
Vested	6,856	6.03
Nonvested options at December 31, 2009	2,583	$ 6.03

(Dollars in thousands)

11. **Stock Options and Equity Incentive Plan** (Continued)

There were no stock options granted in 2009 or 2008.

In connection with the initial private placement offering of the Bank, warrants were issued to purchase 1.5 shares of common stock at $20 per share for every share that the stockholder purchased in the offering. As a result, the Bank issued 110,250 warrants. The warrants were issued in recognition of the financial and organizational risk undertaken by the purchasers in the offering. The warrants are exercisable within ten years from the date of issuance.

12. **Transactions with Executive Officers, Directors, and Principal Stockholders**

The Bank has transactions in the ordinary course of business with its executive officers, directors, principal stockholders, and affiliated companies, on the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with others. Affiliated companies include financial institutions with which a director of the Bank is affiliated, generally as an executive officer. At December 31, 2009 and 2008, the total amount of loans outstanding to related parties were **$198** and $150, respectively.

Activity in these loans during the year ended December 31, 2009 was as follows:

	2009
Beginning balance	**$ 150**
Advances	**48**
Payments	**-**
Ending balance	**$ 198**

Deposits and federal funds purchased from related parties held by the Bank at December 31, 2009 and 2008 amounted to **$10,922** and $7,273, respectively.

13. **Financial Instruments with Off-Balance-Sheet Risk**

The Bank is a party to financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit. Such commitments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the balance sheet.

The Bank's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit is represented by the contractual amount of those instruments. The Bank uses the same credit policies in making commitments and conditional obligations as it does for on-balance-sheet instruments.

(Dollars in thousands)

13. **Financial Instruments with Off-Balance-Sheet Risk** (Continued)

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. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. The Bank evaluates each customer's credit worthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Bank upon extension of credit, is based on management's credit evaluation. Collateral held varies but may include residential or commercial real estate, accounts receivable, inventory, and equipment.

The following financial instruments were outstanding whose contract amounts represent credit risk at December 31:

	Contract amount	
	2009	2008
Commitments to grant loans:		
Fixed rate	**$ -**	$ -
Variable rate	**-**	1,600
Unfunded commitments under lines of credit:		
Fixed rate	**1,639**	2,858
Variable rate	**3,232**	5,300

14. **Regulatory Matters**

The Bank is subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet the minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Bank's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of the Bank's assets, liabilities and certain off-balance-sheet items as calculated under regulatory accounting practices. The Bank's capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk-weightings and other factors.

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios (set forth below) of total and Tier 1 capital (as defined in the regulations) to risk-weighted assets, and of Tier 1 capital to average assets. Management believes, as of December 31, 2009 and 2008, that the Bank meets all capital adequacy requirements to which it is subject.

As of December 31, 2009, the most recent notification from the Federal Deposit Insurance Corporation (FDIC) categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, an institution must maintain minimum total risk-based, Tier 1 risk-based and Tier 1 leverage ratios as set forth in the following tables. There are no conditions or events since the notification that management believes to have changed the Bank's category.

14. **Regulatory Matters** (Continued)

The Bank's actual capital amounts and ratios at December 31, 2009 and 2008, are presented below:

	Actual		For capital adequacy purposes		To be well capitalized under prompt corrective action provisions	
(dollar amounts in thousands)	Amount	Ratio	Amount	Ratio	Amount	Ratio
December 31, 2009						
Total capital (to risk-weighted assets)	**$ 7,560**	**11.61%**	**$ 5,209**	**8.00%**	**$ 6,511**	**10.00%**
Tier 1 capital (to risk-weighted assets)	**6,735**	**10.34%**	**2,604**	**4.00%**	**3,906**	**6.00%**
Tier 1 capital (to average assets)	**6,735**	**7.50%**	**3,593**	**4.00%**	**4,492**	**5.00%**
December 31, 2008						
Total capital (to risk-weighted assets)	$ 6,007	10.18%	$ 4,720	8.00%	$ 5,899	10.00%
Tier 1 capital (to risk-weighted assets)	5,270	8.93%	2,360	4.00%	3,540	6.00%
Tier 1 capital (to average assets)	5,270	7.91%	2,664	4.00%	3,330	5.00%

The Bank is subject to certain restrictions on the amount of dividends that it may declare due to regulatory considerations. The Maryland Banking Code provides that cash dividends may be declared and paid out of accumulated net earnings.

15. **Fair Value of Financial Instruments**

The fair value of a financial instrument is the current amount that would be exchanged between willing parties, other than in a forced liquidation. Generally accepted accounting principles define fair value, establish a framework for measuring fair value, require certain disclosures about fair values, and establish a hierarchy for determining fair value measurements. The hierarchy includes three levels and is based upon the valuation techniques used to measure assets and liabilities.

Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities that the Bank has the ability to access at the measurement date.

Level 2: Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly.

Level 3: Unobservable inputs that reflect the Bank's own assumptions about the asset or liability, in situations in which there is little, if any, market activity for the asset or liability at the measurement date.

15. **Fair Value of Financial Instruments** (Continued)

Fair value measurements on a recurring basis

Investment securities - The fair values of investment securities are determined by obtaining quoted prices on nationally recognized securities exchanges. If quoted prices are not available, fair value is determined using quoted prices for similar securities.

The Bank has categorized its investment securities available for sale as follows:

As of December 31, 2009	Total	Quoted prices in active markets identical assets (Level 1)	Other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Investment securities available for sale	$ 4,983	$ -	$ 4,983	$ -

Fair value measurements on a nonrecurring basis

Impaired loans – The Bank has measured impairment generally based on the fair value of the loan's collateral. Fair value is generally determined based upon independent third-party appraisals of the properties, or discounted cash flows based upon the expected proceeds. These assets are included as Level 3 fair values. The fair value consists of the loan balances of **$4,165**, net of a valuation allowance of **$1,072**.

Description	Total	Level 1 inputs	Level 2 inputs	Level 3 inputs
Impaired loans	$ 3,093	$ -	$ -	$ 3,093

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