Section 1: 10-K (FORM 10-K)

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-K

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

For the fiscal year ended December 31, 2019

OR

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

COMMISSION FILE NUMBER 000-50400

SELECT BANCORP, INC.

(Exact name of registrant as specified in its charter)

NORTH CAROLINA	**20-0218264**
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)
700 W. Cumberland Street, Dunn, North Carolina	**28334**
(Address of Principal Executive Offices)	(Zip Code)

Registrant's Telephone number, including area code: **(910) 892-7080**

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

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Common Stock, par value $1.00 per share	**SLCT**	**The NASDAQ Stock Market LLC**

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

None.
(Title of Class)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. ☐ Yes ☒ No

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

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 every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). ☒ Yes ☐ No

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

Large accelerated filer ☐	Accelerated filer ☒
Non-accelerated filer ☐	Smaller reporting company ☒

Emerging growth company ☐

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐

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

State the aggregate market value of the voting and non-voting common equity held by non-affiliates computed by reference to the price at which the common equity was last sold, or the average bid and asked price of such common equity, as of the last business day of the registrant's most recently completed second fiscal quarter: $187,956,020.

Indicate the number of shares outstanding of each of the registrant’s classes of common stock as of the latest practicable date: 18,239,614 shares outstanding as of March 6, 2020.

Documents Incorporated by Reference:

Portions of the registrant’s Proxy Statement for its 2020 Annual Meeting of Shareholders are incorporated by reference into Part III hereof.

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PART I

ITEM 1 – BUSINESS

General

Select Bancorp, Inc. (the "Registrant" or the "Company") (formerly New Century Bancorp, Inc.) was incorporated under the laws of the State of North Carolina on May 14, 2003, at the direction of the Board of Directors of Select Bank & Trust Company (formerly New Century Bank), for the purpose of serving as the bank holding company for Select Bank & Trust Company ("Select Bank" or the "Bank") and became the holding company for the Bank on September 19, 2003. On July 25, 2014, New Century Bancorp, Inc. and New Century Bank changed their names to Select Bancorp, Inc. and Select Bank & Trust Company, respectively. This was in conjunction with the merger with "Legacy" Select Bancorp, Inc. and Select Bank & Trust Company of Greenville, NC. On December 15, 2017, the Registrant acquired Premara Financial, Inc. ("Premara") and its banking subsidiary Carolina Premier Bank ("Carolina Premier") of Charlotte, North Carolina. Under the terms of that acquisition, Premara was merged with and into the Registrant, Carolina Premier was merged with and into the Bank, and shareholders of Premara received 1.0463 shares of the Registrant's common stock or $12.65 in cash for each outstanding share of Premara common stock, with approximately 70% of such shares being exchanged for shares of the Registrant's common stock and 30% being exchanged for cash.

The Registrant operates for the primary purpose of serving as the holding company for its subsidiary depository institution, Select Bank & Trust Company. The Registrant's headquarters is located at 700 West Cumberland Street, Dunn, North Carolina 28334.

The Bank was incorporated on May 19, 2000 as a North Carolina-chartered commercial bank, opened for business on May 24, 2000, and has its main office located at 700 West Cumberland Street, Dunn, North Carolina.

The Bank operates for the primary purpose of serving the banking needs of individuals and small to medium-sized businesses in its market area. The Bank offers a range of banking services including checking and savings accounts, commercial, consumer, mortgage and personal loans, and other associated financial services.

Primary Market Area

The Registrant's market area consists of portions of central and eastern North Carolina which includes Alamance, Brunswick, Carteret, Cumberland, Harnett, Mecklenburg, New Hanover, Pasquotank, Pitt, Robeson, Sampson, Wake and Wayne counties, portions of northwestern South Carolina in Cherokee and York counties and the City of Virginia Beach, Virginia. The Bank's main office is in Dunn, North Carolina, and it has branch offices in Burlington, Charlotte, Clinton, Elizabeth City, Fayetteville, Goldsboro, Greenville, Holly Springs, Leland, Lillington, Lumberton, Morehead City, Raleigh, and Wilmington, North Carolina. The Bank's South Carolina branch offices are located in Rock Hill and Blacksburg, South Carolina. The Bank's Virginia branch office is located in Virginia Beach, Virginia. The Registrant's market area has a population of over 4.4 million with an average household income of over $47,000.

Total deposits in the Registrant's market area exceeded $250 billion at June 30, 2019. The leading economic components of Alamance County, North Carolina, are healthcare and education with the largest employers being LabCorp, the public school system, the Alamance Regional Medical Center and Elon University. Brunswick County North Carolina's leading industries are education, public administration and energy, with the County of Brunswick Education Board and Government, and Progress Energy as the top employers. In Carteret County, North Carolina, public services are the leading economic factors such as education, health services and public administration (the leading employers) followed by major retailers including Lowes Home Improvement, Walmart, and Food Lion. Cumberland County, North Carolina's leading sector is the Department of Defense with extensions of the Army, Navy and Air Force located there, followed by Cumberland County School System, Cape Fear Valley Health Systems, and a Wal-Mart distribution Center. The U.S. Department of Veteran's Affairs and Fayetteville Technical Community College also employ over 1,000 each in Cumberland County. In Harnett County, North Carolina, a top economic sector is education including top employers Harnett County Schools, Campbell University then also other large employers like Food Lion distribution center, public administration, Betsy Johnson Memorial Hospital, Walmart and a Carlie C's Operation center. In Mecklenburg County, education, financial activities and health services are leading industries. The Atrium Healthcare (FKA Carolinas Health Care), Novant Medical Group and the school system are top employers along with Wells Fargo and Bank of America. Transportation is also a leading industry in Mecklenburg County with American Airlines as a top employer. In New Hanover County, North Carolina, education, health services and government offices are leaders in the economy. New Hanover Regional Medical Center, the school system and the University of North Carolina at Wilmington are the largest employers along with PPD Development, a pharmaceutical company. In Pasquotank County, North Carolina, education (including the local school system and Elizabeth City State University), health services (specifically top employer Sentara Internal Medicine) and the U.S. Department of Homeland Security through the U.S. Coast Guard base in Elizabeth City are top employers. Pitt County, North Carolina, has a mix of education and health services employers, including top employers East Carolina University, Pitt County Board of Education and Vidant Medical Center. The county still relies heavily on manufacturing with over 2,000 jobs attributable to NACCO Materials Handling Group and Patheon Manufacturing Services. In Robeson County, North Carolina, leading sectors include education, health services, and manufacturing with Mountaire Farms of N.C. employing over 1,000 citizens. Robeson County is also home to UNC Pembroke and the Campbell Soup Supply Company. In Sampson County, North Carolina, leading sectors include education, manufacturing, agriculture and natural resources with top employers including Smithfield Foods, Prestage Farms and Hog Slat. In Wake County, North Carolina, leading sectors include government, education, healthcare, and technology with education leading the pack with the top employers being Wake County Public Schools, NC State University, and several teaching hospitals in the area, including Wake Med, Rex Hospital. Technology is also an emerging leader with SAS Institute, Inc. being one of the top 5 employers. Wayne County North Carolina's leading areas are education, healthcare and retail trade including top employers Wayne County Public Schools and Wayne Memorial Hospital, additionally manufacturing does hold several of the top 10 employers, including Mount Olive Pickle Company. In South Carolina's Cherokee County healthcare, education, and manufacturing are leading industries. Murphy Medical Center, the local school system, and Moog Components are among the largest employers. In York County, South Carolina, the financial industry, retail and healthcare are leading economic components including Lash Group, LPL Financial, Ross Stores distribution and Wells Fargo Mortgage. Virginia Beach, Virginia contains large employers from Healthcare, Government/Military, and travel/leisure. These include Naval Air Station Oceana, Joint Expeditionary Base Little Creek, Sentara Healthcare, Lynnhaven Mall and Gold Key/PHR Hotel & Resorts.

Competition

Commercial banking in the North Carolina, South Carolina and Virginia markets in which the Bank operates is extremely competitive. The Registrant competes in its market areas with some of the largest banking organizations in the state and country as well as other financial institutions, such as federally and state-chartered savings and loan institutions and credit unions. It also competes against consumer finance companies, mortgage companies and other lenders engaged in the business of extending credit. Many of the Registrant's competitors have broader geographic markets and higher lending limits than the Registrant and are also able to provide more services and make greater use of advertising. As of June 30, 2019, data provided by the FDIC Deposit Market Share Report indicated that, within the Registrant's market area, there were 957 offices of insured depository institutions (38 in Alamance County, 37 in Brunswick County, 22 in Carteret County, 56 in Cumberland County, 23 in Harnett County, 223 in Mecklenburg County, 64 in New Hanover, 13 in Pasquotank County, 40 in Pitt County, 27 in Robeson County, 14 in Sampson County, 249 in Wake County and 25 in Wayne County, all in North Carolina, 10 in Cherokee County, and 43 in York County, South Carolina, and 73 in Virginia Beach, Virginia, including offices of the Bank).

Many out-of-state commercial banks have recently acquired a number of North Carolina, South Carolina and Virginia banks and further heightened the competition among banks in the markets served.

Despite the competition in its market areas, the Registrant believes that it has certain competitive advantages that distinguish it from its competition. The Registrant believes that its primary competitive advantages are its strong local identity and affiliation within the community and its emphasis on providing specialized services to small and medium-sized business enterprises as well as professional and upper-income individuals. The Registrant offers customers modern, high-tech banking without forsaking community values such as prompt, personal service and friendliness. The Registrant offers many personalized services and intends to attract customers by being responsive and sensitive to their individualized needs. The Registrant also relies on goodwill and referrals from shareholders and satisfied customers as well as traditional marketing media to attract new customers. To enhance a positive image in the community the Registrant supports and participates in local events and its officers and directors serve on boards of local civic and charitable organizations.

Employees

As of December 31, 2019, the Registrant employed 213 full time equivalent employees. None of the Registrant's employees are covered by a collective bargaining agreement. The Registrant believes relations with its employees to be good.

Where to Find Additional Information About the Company

We are subject to the reporting requirements of the Securities Exchange Act of 1934, as amended, and file annual, quarterly and current reports, proxy statements and other information with the SEC. Our SEC filings are also available at the SEC's website at http://www.sec.gov and through the "Investor Relations" section of our website (www.selectbank.com).

REGULATION

Regulation of the Bank

General. The Bank is a North Carolina-chartered commercial bank and its deposit accounts are insured by the Deposit Insurance Fund ("DIF") administered by the Federal Deposit Insurance Corporation ("FDIC"). The Bank is subject to supervision, examination and regulation by the North Carolina Office of the Commissioner of Banks ("Commissioner") and the FDIC. It is subject to North Carolina and federal statutory and regulatory provisions governing such matters as capital standards, dividends, mergers, subsidiary investments and establishment of branch offices. The Bank is required to file reports with the Commissioner and the FDIC concerning its activities and financial condition and is required to obtain regulatory approval prior to entering into certain transactions, including mergers with, or acquisitions of, other depository institutions.

As a federally insured depository institution, the Bank is subject to various regulations promulgated by the Board of Governors of the Federal Reserve System ("Federal Reserve Board") or ("FRB"), including Regulation B (Equal Credit Opportunity), Regulation D (Reserve Requirements), Regulation E (Electronic Fund Transfers), Regulation O (Loans to Insiders), Regulation W (Transactions with Affiliates), Regulation Z (Truth in Lending), Regulation CC (Availability of Funds and Collection of Checks) and Regulation DD (Truth in Savings).

The system of regulation and supervision applicable to the Bank establishes a comprehensive framework for the operations of the Bank, and is intended primarily for the protection of the FDIC and the depositors of the Bank, rather than shareholders. Changes in the regulatory framework could have a material effect on the Bank that in turn, could have a material effect on the Registrant. This discussion does not purport to be a complete explanation of all such laws and regulations.

State Law. The Bank is subject to extensive supervision and regulation by the Commissioner. The Commissioner oversees state laws that set specific requirements for bank capital and deposits in, and loans and investments by, banks, including the amounts, types, and in some cases, rates. The Commissioner supervises and performs periodic examinations of North Carolina-chartered banks to assure compliance with state banking statutes and regulations, and the Bank is required to make regular reports to the Commissioner describing in detail its resources, assets, liabilities and financial condition. Among other things, the Commissioner regulates mergers and consolidations of state-chartered banks, the payment of dividends, loans to officers and directors, record keeping, types and amounts of loans and investments, and the establishment of branches. The primary state banking laws to which the Bank is subject are set forth in Chapters 53C and 53 of the North Carolina General Statutes. Certain provisions of the North Carolina Business Corporation Act are also applicable to the Bank, as a North Carolina banking corporation.

Dodd-Frank Wall Street Reform and Consumer Protection Act. In 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") was signed into law. This law significantly changed the bank regulatory structure and affected the lending, deposit, investment, trading, and operating activities of financial institutions and their holding companies. The Dodd-Frank Act required various federal agencies to adopt a broad range of rules and regulations, and to prepare numerous studies and reports for Congress. The Dodd-Frank Act included, among other things:

- the creation of a Financial Stability Oversight Council to identify emerging systemic risks posed by financial firms, activities and practices, and to improve cooperation between federal agencies;
- the creation of a Bureau of Consumer Financial Protection authorized to promulgate and enforce consumer protection regulations relating to financial products, which affects both banks and non-bank financial companies;
- the establishment of strengthened capital and prudential standards for banks and bank holding companies;
- enhanced regulation of financial markets, including derivatives and securitization markets;
- the elimination of certain trading activities by banks;
- a permanent increase of FDIC deposit insurance to $250,000 per depository category and an increase in the minimum deposit insurance fund reserve requirement from 1.15% to 1.35%, with assessments be based on assets as opposed to deposits;
- amendments to the Truth in Lending Act aimed at improving consumer protections with respect to mortgage originations, including originator compensation, minimum repayment standards, and prepayment considerations; and
- disclosure and other requirements relating to executive compensation and corporate governance.

Economic Growth, Regulatory Relief, and Consumer Protection Act. On May 24, 2018, the Economic Growth, Regulatory Relief, and Consumer Protection Act ("EGRRCPA") was signed into law, which amended provisions of the Dodd-Frank Act and was intended to ease, and better tailor, regulation, particularly with respect to smaller-sized institutions such as the Registrant. EGRRCPA's highlights include, among other things: (i) exempts banks with less than $10 billion in assets from the ability-to-repay requirements for certain qualified residential mortgage loans held in portfolio; (ii) not requiring appraisals for certain transactions valued at less than $400,000 in rural areas; (iii) clarifies that, subject to various conditions, reciprocal deposits of another depository institution obtained using a deposit broker through a deposit placement network for purposes of obtaining maximum deposit insurance would not be considered brokered deposits subject to the FDIC's brokered-deposit regulations; (iv) raises eligibility for the 18-month exam cycle from $1 billion to banks with $3 billion in assets; and (v) simplifies capital calculations by requiring regulators to establish for institutions under $10 billion in assets a community bank leverage ratio (tangible equity to average consolidated assets) at a percentage not less than 8% and not greater than 10% that such institutions may elect to replace the general applicable risk-based capital requirements for determining well capitalized status. On September 17, 2019, the FDIC passed a final rule on the community bank leverage ratio, setting the minimum required community bank leverage ratio at 9%. The rule went into effect on January 1, 2020. In addition, the Federal Reserve Board was required to raise the asset threshold under its Small Bank Holding Company Policy Statement from $1 billion to $3 billion for bank or savings and loan holding companies that are exempt from consolidated capital requirements, provided that such companies meet certain other conditions such as not engaging in significant nonbanking activities and not having a material amount of debt or equity securities outstanding (other than trust preferred securities) that are registered with the Securities and Exchange Commission. Consistent with EGRRCPA, the Federal Reserve passed an interim final rule that became effective on August 30, 2018, to increase the asset threshold to $3 billion for qualifying for such policy statement.

Deposit Insurance. The Bank's deposits are insured up to limits set by the DIF of the FDIC. The standard FDIC insurance coverage amount is $250,000 per depositor. The DIF was formed on March 31, 2006, upon the merger of the Bank Insurance Fund and the Savings Insurance Fund in accordance with the Federal Deposit Insurance Reform Act of 2005 (the "Reform Act"). The primary purposes of the DIF are: (1) to insure the deposits and protect the depositors of insured banks and (2) to resolve failed banks. The DIF is funded mainly through quarterly assessments on insured banks, but also receives interest income on its securities. The DIF is reduced by loss provisions associated with failed banks and by FDIC operating expenses. The Reform Act established a range of 1.15% to 1.50% within which the FDIC may set the Designated Reserve Ratio (the "reserve ratio" or "DRR"). The DRR is expressed as a percentage of insured deposits. The Dodd-Frank Act gave the FDIC greater discretion to manage the DIF, raised the minimum DIF reserve ratio to 1.35%, and removed the upper limit of 1.50%. In October 2010, the FDIC adopted a restoration plan to ensure that the DIF reserve ratio reaches 1.35% by September 30, 2020, as required by the Dodd-Frank Act. The FDIC also proposed a comprehensive, long-range plan for management of the DIF. As part of this comprehensive plan, the FDIC has adopted a final rule to set the DRR at 2.0%, which acts as a floor rather than a ceiling on the DRR.

The FDIC imposes a risk-based deposit insurance premium assessment on member institutions in order to maintain the DIF. This assessment system was amended by the Reform Act and further amended by the Dodd-Frank Act. Under this system, as amended, the assessment rates for an insured depository institution vary according to the level of risk incurred in its activities, which for established small institutions like the Bank (i.e., those institutions with less than $10 billion in assets and insured for five years or more), is generally determined by reference to the institution's supervisory ratings. The assessment rate schedule can change from time to time, at the discretion of the FDIC, subject to certain limits. The Dodd-Frank Act and its implementing regulations changed the methodology for calculating deposit insurance assessments from the amount of an insured institution's domestic deposits to its total assets minus tangible capital.

The FDIC has authority to increase deposit insurance assessments. A significant increase in insurance premiums would likely have an adverse effect on the operating expenses and results of operations of the Registrant and the Bank. Management cannot predict what insurance assessment rates will be in the future.

Insurance of deposits may be terminated by the FDIC upon a finding that an insured institution has engaged in unsafe or unsound practices, is in an unsafe or unsound condition to continue operations or has violated any applicable law, regulation, rule, order or condition imposed by the FDIC. Management of the Bank is not aware of any practice, condition or violation that might lead to termination of its FDIC deposit insurance.

Capital Requirements. The federal banking regulators have adopted certain risk-based capital guidelines to assist in the assessment of the capital adequacy of a banking organization's operations for both transactions reported on the balance sheet as assets and transactions, such as letters of credit, and recourse arrangements, which are recorded as off balance sheet items. Under these guidelines, nominal dollar amounts of assets and credit equivalent amounts of off balance sheet items are multiplied by one of several risk adjustment percentages which range from 0% for assets with low credit risk, such as certain U.S. Treasury securities, to 1,250% for certain assets with high credit risk, such as securitization exposures.

A banking organization’s risk-based capital ratios are obtained by dividing its qualifying capital by its total risk adjusted assets. The regulators measure risk-adjusted assets, which include off balance sheet items, against both total qualifying capital (the sum of Common Equity Tier 1 capital and limited amounts of Tier 2 capital) and Tier 1 capital. “Common Equity Tier 1,” or core capital, includes common equity, qualifying noncumulative perpetual preferred stock and minority interests in equity accounts of consolidated subsidiaries, less goodwill and other intangibles, subject to certain exceptions. “Additional Tier 1 Capital” includes noncumulative perpetual preferred stock, tier 1 minority interests, grandfathered Trust preferred securities, and Troubled Asset Relief Program instruments less applicable regulatory adjustments and deductions. “Tier 2,” or supplementary capital, includes among other things, limited-life preferred stock, hybrid capital instruments, mandatory convertible securities, qualifying subordinated debt, and the allowance for loan and lease losses, subject to certain limitations and less required deductions. The inclusion of elements of Tier 2 capital is subject to certain other requirements and limitations of the federal banking agencies. Banks and bank holding companies subject to the risk-based capital guidelines are required to maintain a ratio of Tier 1 capital to risk-weighted assets of at least 5% and a ratio of total capital to risk-weighted assets of at least 10% to meet well capitalized thresholds. The appropriate regulatory authority may set higher capital requirements when particular circumstances warrant.

The federal banking agencies have adopted regulations specifying that they will include, in their evaluations of a bank’s capital adequacy, an assessment of the bank’s interest rate risk exposure. The standards for measuring the adequacy and effectiveness of a banking organization’s interest rate risk management include a measurement of board of director and senior management oversight, and a determination of whether a banking organization’s procedures for comprehensive risk management are appropriate for the circumstances of the specific banking organization.

Failure to meet applicable capital guidelines could subject a banking organization to a variety of enforcement actions, including limitations on its ability to pay dividends or expand with new branch offices or through acquisitions, the issuance by the applicable regulatory authority of a capital directive to increase capital and, in the case of depository institutions, the termination of deposit insurance by the FDIC, as well as the measures described under “Prompt Corrective Action” below, as applicable to undercapitalized institutions. In addition, future changes in regulations or practices could further reduce the amount of capital recognized for purposes of capital adequacy. Such a change could affect the ability of the Bank to grow and could restrict the amount of profits, if any, available for the payment of dividends to the Registrant and its shareholders.

On July 2, 2013, the Federal Reserve approved a final rule that establishes an integrated regulatory capital framework that addresses shortcomings in certain capital requirements. The FDIC adopted a substantially similar interim final rule on July 9, 2013. The capital rule implements in the United States the Basel III regulatory capital reforms from the Basel Committee on Banking Supervision and certain changes required by the Dodd-Frank Act.

The major provisions of the rule applicable to us are:

- The rule implemented higher minimum capital requirements, including a new common equity Tier1 capital requirement, and established criteria that instruments must meet in order to be considered Common Equity Tier 1 capital, additional Tier 1 capital, or Tier 2 capital. The minimum capital to risk-weighted assets (“RWA”) requirements under the rule are a common equity Tier 1 capital ratio of 4.5% and a Tier 1 capital ratio of 6.0%, which is an increase from 4.0%, and a total capital ratio that remains at 8.0%. The minimum leverage ratio (Tier 1 capital to total assets) is 4.0%. The rule maintains the general structure of the current prompt corrective action, or PCA, framework while incorporating these increased minimum requirements.

- The rule implemented changes to the definition of capital, including stricter eligibility criteria for regulatory capital instruments that disallows the inclusion of instruments such as trust preferred securities in Tier 1 capital going forward (subject to certain exceptions discussed below), and new constraints on the inclusion of minority interests, mortgage-servicing assets (“MSAs”), deferred tax assets (“DTAs”), and certain investments in the capital of unconsolidated financial institutions.

- Under the rule, in order to avoid limitations on capital distributions, including dividend payments and certain discretionary bonus payments to executive officers, a banking organization must hold a capital conservation buffer composed of common equity Tier 1 capital above its minimum risk-based capital requirements. This buffer is intended to help ensure that banking organizations conserve capital when it is most needed, allowing them to better weather periods of economic stress. The buffer is measured relative to RWA. A banking organization with a buffer greater than 2.5% would not be subject to limits on capital distributions or discretionary bonus payments; however, a banking organization with a buffer of less than 2.5% would be subject to increasingly stringent limitations as the buffer approaches zero. The rule also prohibits a banking organization from making distributions or discretionary bonus payments during any quarter if its eligible retained income is negative in that quarter and its capital conservation buffer ratio was less than 2.5% at the beginning of the quarter. The minimum capital requirements plus the capital conservation buffer exceed the PCA well capitalized thresholds (discussed below).

- The rule also increased the risk weights for past-due loans, certain commercial real estate loans, and some equity exposures, and made selected other changes in risk weights and credit conversion factors.

The Bank was required to comply with the new rule beginning on January 1, 2015. Compliance by the Registrant and the Bank with these capital requirements affects their respective operations by increasing the amount of capital required to conduct operations.

In July 2019, the federal banking agencies released a final rule amending the U.S. Basel III capital rules to simplify the capital treatment of capital deductions and recognition of minority interests for banking organizations such as the Registrant that are not subject to the advanced approaches capital rule. The final rule:

- simplifies the framework of regulatory capital deductions and heightened risk weights for mortgage servicing assets, deferred tax assets arising from temporary differences that an institution could not realize through net operating loss carrybacks, and investments in the capital of unconsolidated financial institutions, resulting in potentially fewer deductions for these items;

- simplifies the recognition and calculation of minority interests that are includable in regulatory capital, resulting in potentially greater recognition of minority interests; and

- makes certain technical amendments to the capital rules.

<u>Community Bank Leverage Ratio</u>. As discussed above, in May 2018, EGRRCPA became law, which directs the federal banking agencies (which includes the FDIC, Federal Reserve Board, and Office of the Comptroller of the Currency, or OCC) to develop a community bank leverage ratio ("CBLR") of not less than 8 percent and not more than 10 percent for qualifying community banking organizations. EGRRCPA defines a qualifying community banking organization as a depository institution or depository institution holding company with total consolidated assets of less than $10 billion, which would include the Registrant and its banking subsidiary. A qualifying community banking organization that exceeds the CBLR level established by the agencies is considered to have met: (i) the generally applicable leverage and risk-based capital requirements under the agencies' capital rule (see discussion above under "Regulation of the Bank – Capital Requirements"); (ii) the capital ratio requirements in order to be considered well capitalized under the agencies' PCA framework (in the case of insured depository institutions) (see discussion below under subheading, "Prompt Corrective Action"); and (iii) any other applicable capital or leverage requirements. Section 201 of EGRRCPA defines the CBLR as the ratio of a banking organization's CBLR tangible equity to its average total consolidated assets, both as reported on the banking organization's applicable regulatory filing.

On September 17, 2019, the FDIC passed a final rule on the CBLR, setting the required minimum required CBLR at 9%. The rule went into effect on January 1, 2020. Under the proposal, a qualifying community banking organization may elect to use the CBLR framework if its CBLR is greater than 9 percent. A qualifying community banking organization that has chosen the proposed framework is not required to calculate the existing risk-based and leverage capital requirements. A bank is also considered to have met the capital ratio requirements to be well capitalized for the agencies' prompt corrective action rules provided it has a CBLR greater than 9 percent.

Prompt Corrective Action. Under the Federal Deposit Insurance Corporation Improvement Act of 1991 (“FDICIA”), the federal banking regulators are required to take prompt corrective action if an insured depository institution fails to satisfy certain minimum capital requirements, including a leverage limit, a risk-based capital requirement, and any other measure deemed appropriate by the federal banking regulators for measuring the capital adequacy of an insured depository institution. All institutions, regardless of their capital levels, are restricted from making any capital distribution or paying any management fees if the institution would thereafter fail to satisfy the minimum levels for any of its capital requirements. An institution that fails to meet the minimum level for any relevant capital measure (an “undercapitalized institution”) may be: (i) subject to increased monitoring by the appropriate federal banking regulator; (ii) required to submit an acceptable capital restoration plan within 45 days; (iii) subject to asset growth limits; and (iv) required to obtain prior regulatory approval for acquisitions, branching and new lines of business. The capital restoration plan must include a guarantee by the institution’s holding company that the institution will comply with the plan until it has been adequately capitalized on average for four consecutive quarters, under which the holding company would be liable up to the lesser of 5% of the institution’s total assets or the amount necessary to bring the institution into capital compliance as of the date it failed to comply with its capital restoration plan. A “significantly undercapitalized” institution, as well as any undercapitalized institution that does not submit an acceptable capital restoration plan, may be subject to regulatory demands for recapitalization, broader application of restrictions on transactions with affiliates, limitations on interest rates paid on deposits, asset growth and other activities, possible replacement of directors and officers, and restrictions on capital distributions by any bank holding company controlling the institution. Any company controlling the institution may also be required to divest the institution or the institution could be required to divest subsidiaries. The senior executive officers of a significantly undercapitalized institution may not receive bonuses or increases in compensation without prior regulatory approval and the institution is prohibited from making payments of principal or interest on its subordinated debt. In their discretion, the federal banking regulators may also impose the foregoing sanctions on an undercapitalized institution if the regulators determine that such actions are necessary to carry out the purposes of the prompt corrective action provisions. If an institution’s ratio of tangible capital to total assets falls below the “critical capital level” established by the appropriate federal banking regulator, the institution will be subject to conservatorship or receivership within specified time periods.

As discussed above, on July 2, 2013, the Federal Reserve Board, and on July 9, 2013, the FDIC, adopted a final rule that implemented the Basel III changes to the international regulatory capital framework, referred to as the “Basel III Rules.” The Basel III Rules apply to both depository institutions and (subject to certain exceptions not applicable to the Registrant) their holding companies.

The Basel III Rules include new risk-based and leverage capital ratio requirements which refine the definition of what constitutes “capital” for purposes of calculating those ratios. The minimum capital level requirements applicable to the Registrant and the Bank under the Basel III Rules are: (i) a common equity Tier 1 risk-based capital ratio of 4.5 percent; (ii) a Tier 1 risk-based capital ratio of 6 percent (increased from 4 percent); (iii) a total risk-based capital ratio of 8 percent (unchanged from prior rules); and (iv) a Tier 1 leverage ratio of 4 percent for all institutions. Common equity Tier 1 capital consists of retained earnings and common stock instruments, subject to certain adjustments.

The Basel III Rules also established a “capital conservation buffer” of 2.5 percent above the new regulatory minimum risk-based capital requirements. The conservation buffer, when added to the capital requirements, result in the following minimum ratios: (i) a common equity Tier 1 risk-based capital ratio of 7.0 percent, (ii) a Tier 1 risk-based capital ratio of 8.5 percent, and (iii) a total risk-based capital ratio of 10.5 percent. An institution is subject to limitations on certain activities including payment of dividends, share repurchases and discretionary bonuses to executive officers if its capital level is below the buffer amount.

The Basel III Rules also revised the prompt corrective action framework, which is designed to place restrictions on insured depository institutions, including the Bank, if their capital levels do not meet certain thresholds. These revisions became effective on January 1, 2015. The prompt corrective action rules were modified to include a common equity Tier 1 capital component and to increase certain other capital requirements for the various thresholds. For example, under the prompt corrective action rules, insured depository institutions are required to meet the following capital levels in order to qualify as "well capitalized:" (i) a new common equity Tier 1 risk-based capital ratio of 6.5 percent; (ii) a Tier 1 risk-based capital ratio of 8 percent (increased from 6 percent); (iii) a total risk-based capital ratio of 10 percent (unchanged from prior rules); and (iv) a Tier 1 leverage ratio of 5 percent (unchanged from prior rules).

The Basel III Rules set forth certain changes in the methods of calculating certain risk-weighted assets, which in turn affect the calculation of risk based ratios. Under the Basel III Rules, higher or more sensitive risk weights would be assigned to various categories of assets, including certain credit facilities that finance the acquisition, development or construction of real property, certain exposures or credits that are 90 days past due or on nonaccrual, foreign exposures and certain corporate exposures. In addition, the Basel III Rules include (i) alternative standards of creditworthiness consistent with the Dodd-Frank Act; (ii) greater recognition of collateral and guarantees; and (iii) revised capital treatment for derivatives and repo-style transactions.

In addition, the final rule includes certain exemptions to address concerns about the regulatory burden on community banks. For example, banking organizations with less than $15 billion in consolidated assets as of December 31, 2009 are permitted to include in Tier 1 capital trust preferred securities and cumulative perpetual preferred stock issued and included in Tier 1 capital prior to May 19, 2010 on a permanent basis, without any phase out. The Bank has opted out of the requirement to include most accumulated other comprehensive income ("AOCI") components in the calculation of CET1 capital and, in effect, retain the AOCI treatment under the prior capital rules and exclude accumulated other comprehensive income from capital.

Under the implementing regulations, the federal banking regulators, including the FDIC, generally measure an institution's capital adequacy on the basis of its total risk-based capital ratio (the ratio of its total capital to risk-weighted assets), Tier 1 risk-based capital ratio (the ratio of its core capital to risk-weighted assets) and leverage ratio (the ratio of its core capital to adjusted total assets).

The following table shows the Bank's actual capital ratios and the required capital ratios for the various prompt corrective action categories as of December 31, 2019.

	Actual	Well Capitalized	Adequately Capitalized	Undercapitalized	Significantly Undercapitalized	Regulatory Minimum Requirement
Total risk-based capital ratio	15.69%	10.0% or more	8.0% or more	Less than 8.0%	Less than 6.0%	11.50% or more
Tier 1 risk-based capital ratio	14.95%	8.0% or more	6.0% or more	Less than 6.0%	Less than 4.0%	8.00% or more
Common equity Tier 1 risk-based capital ratio	14.95%	6.5% or more	4.5% or more	Less than 4.50%	Less than 3.0%	8.00% or more
Leverage ratio	13.59%	5.0% or more	4.0% or more *	Less than 4.0% *	Less than 3.0%	8.00% or more

* 3.0% if institution has the highest regulatory rating and meets certain other criteria.

A "critically undercapitalized" institution is defined as an institution that has a ratio of "tangible equity" to total assets of less than 2.0%. Tangible equity is defined as core capital plus cumulative perpetual preferred stock (and related surplus) less all intangibles other than qualifying supervisory goodwill and certain purchased mortgage servicing rights. The FDIC may reclassify a well-capitalized institution as adequately capitalized and may require an adequately capitalized or undercapitalized institution to comply with the supervisory actions applicable to institutions in the next lower capital category (but may not reclassify a significantly undercapitalized institution as critically undercapitalized) if the FDIC determines, after notice and an opportunity for a hearing, that the institution is in an unsafe or unsound condition or that the institution has received and not corrected a less-than-satisfactory rating for any regulatory examination rating category. See **Note M** of the Notes to Consolidated Financial Statements included under Item 8 of this Annual Report on Form 10-K for additional discussion of regulatory capital.

Safety and Soundness Guidelines. Under FDICIA, as amended by the Riegle Community Development and Regulatory Improvement Act of 1994 (the "CDRI Act"), each federal banking agency was required to establish safety and soundness standards for institutions under its authority. The interagency guidelines require depository institutions to maintain internal controls and information systems and internal audit systems that are appropriate for the size, nature and scope of the institution's business. The guidelines also establish certain basic standards for the documentation of loans, credit underwriting, interest rate risk exposure, asset growth, and information security. The guidelines further provide that depository institutions should maintain safeguards to prevent the payment of compensation, fees and benefits that are excessive or that could lead to material financial loss, and should take into account factors such as comparable compensation practices at comparable institutions. If the appropriate federal banking agency determines that a depository institution is not in compliance with the safety and soundness guidelines, it may require the institution to submit an acceptable plan to achieve compliance with the guidelines. A depository institution must submit an acceptable compliance plan to its primary federal regulator within 30 days of receipt of a request for such a plan. Failure to submit or implement a compliance plan may subject the institution to regulatory sanctions.

International Money Laundering Abatement and Financial Anti-Terrorism Act of 2001. On October 26, 2001, the USA PATRIOT Act of 2001 was enacted. This act contains the International Money Laundering Abatement and Financial Anti-Terrorism Act of 2001, which sets forth anti-money laundering measures affecting insured depository institutions, broker-dealers and other financial institutions. The Act requires U.S. financial institutions to adopt new policies and procedures to combat money laundering and grants the Secretary of the Treasury broad authority to establish regulations and to impose requirements and restrictions on the operations of financial institutions. The Bank's loan and deposit operations are both subject to the Bank Secrecy Act, which governs how banks and other financial institutions report certain currency transactions and maintain appropriate safeguards against "money laundering" activities, including customer due diligence processes.

Office of Foreign Assets Control Regulation. The United States has imposed economic sanctions that affect transactions with designated foreign countries, nationals and others. These are typically known as the "OFAC" rules based on their administration by the U.S. Treasury's Office of Foreign Assets Control (OFAC). The OFAC-administered sanctions targeting countries take many different forms. Generally, however, they contain one or more of the following elements: (i) restrictions on trade with or investment in a sanctioned country, including prohibitions against direct or indirect imports from and exports to a sanctioned country and prohibitions on "U.S. persons" engaging in financial transactions relating to making investments in, or providing investment-related advice or assistance to, a sanctioned country; and (ii) a blocking of assets in which the government or specially designated nationals of the sanctioned country have an interest, by prohibiting transfers of property subject to U.S. jurisdiction (including property in the possession or control of U.S. persons). Blocked assets (e.g., property and bank deposits) cannot be paid out, withdrawn, set off or transferred in any manner without a license from OFAC. Failure of a financial institution to comply with these sanctions could result in legal consequences for the institution.

Privacy. Financial institutions are required by the Gramm-Leach-Bliley Financial Services Modernization Act of 1999 to disclose their policies for collecting and protecting confidential customer information. Customers generally may prevent financial institutions from sharing personal financial information with nonaffiliated third parties except for third parties that market the institutions' own products and services. Additionally, financial institutions generally may not disclose consumer account numbers to any nonaffiliated third party for use in telemarketing, direct mail marketing or other marketing through electronic mail to consumers. The Bank has established a privacy policy that it believes promotes compliance with these federal requirements.

Community Reinvestment Act. The Bank, like other financial institutions, is subject to the Community Reinvestment Act ("CRA"). The purpose of the CRA is to encourage financial institutions to help meet the credit needs of their entire communities, including the needs of low-and moderate-income neighborhoods.

The federal banking agencies have implemented an evaluation system that rates an institution based on its asset size and actual performance in meeting community credit needs. Under these regulations, the institution is first evaluated and rated under two categories: a lending test and a community development test. For each of these tests, the institution is given a rating of either "outstanding," "high satisfactory," "low satisfactory," "needs to improve," or "substantial non-compliance." A set of criteria for each rating has been developed and is included in the regulation. If an institution disagrees with a particular rating, the institution has the burden of rebutting the presumption by clearly establishing that the quantitative measures do not accurately present its actual performance, or that demographics, competitive conditions or economic or legal limitations peculiar to its service area should be considered. The ratings received under the three tests will be used to determine the overall composite CRA rating. The composite ratings currently given are: "outstanding," "satisfactory," "needs to improve" or "substantial non-compliance."

The Bank's CRA rating would be a factor to be considered by the Federal Reserve Board and the FDIC in considering applications submitted by the Bank to acquire branches or to acquire or combine with other financial institutions and take other actions and, if such rating was less than "satisfactory," could result in the denial of such applications. During the Bank's last compliance examination, the Bank received a satisfactory rating with respect to CRA compliance.

The Office of the Comptroller of the Currency and the FDIC have proposed changes to the regulations under the Community Reinvestment Act. The Company will monitor the proposed changes as they make their way through the agency rulemaking process.

Federal Home Loan Bank System. The FHLB System consists of 12 district FHLBs subject to supervision and regulation by the Federal Housing Finance Agency ("FHFA"). The FHLBs provide a central credit facility primarily for member institutions. As a member of the FHLB of Atlanta, the Bank is required to acquire and hold shares of capital stock in the FHLB of Atlanta. The Bank was in compliance with this requirement with investment in FHLB of Atlanta stock of $3.0 million at December 31, 2019. The FHLB of Atlanta serves as a reserve or central bank for its member institutions within its assigned district. It is funded primarily from proceeds derived from the sale of consolidated obligations of the FHLB System. It offers advances to members in accordance with policies and procedures established by the FHFA and the Board of Directors of the FHLB of Atlanta. Long-term advances may only be made for the purpose of providing funds for residential housing finance, small businesses, small farms and small agribusinesses.

Reserves. Pursuant to regulations of the Federal Reserve Board, the Bank must maintain average daily reserves equal to 3% on transaction accounts of $15.2 million up to $110.2 million, plus 10% on the remainder. This percentage is subject to adjustment by the Federal Reserve Board. Because required reserves must be maintained in the form of vault cash or in a noninterest bearing account at a Federal Reserve Bank, the effect of the reserve requirement is to reduce the amount of the institution's interest-earning assets. As of December 31, 2019, the Bank met its reserve requirements.

The Bank is also subject to the reserve requirements of North Carolina commercial banks. North Carolina law requires state nonmember banks to maintain, at all times, a reserve fund in an amount set by the Commissioner.

Liquidity Requirements. FDIC policy requires that banks maintain an average daily balance of liquid assets (cash, certain time deposits, mortgage-backed securities, loans available for sale and specified United States government, state, or federal agency obligations) in an amount which it deems adequate to protect the safety and soundness of the Bank. The FDIC currently has no specific level which it requires. The Bank maintains its liquidity position under policy guidelines based on liquid assets in relationship to deposits and short-term borrowings. Based on its policy calculation guidelines, the Bank's calculated liquidity ratio was 12.93% of total deposits and short-term borrowings at December 31, 2019, which management believes is adequate.

Dividend Restrictions. Under FDIC regulations, the Bank may not pay a dividend if, after the payment of the dividend, the Bank would be undercapitalized pursuant to the agencies' PCA regulations. Moreover, institutions that are poorly rated or subject to written supervisory actions often are specifically directed not to pay dividends in order to ensure adequate capital exists to support their risk profile. The Bank would also be subject to restrictions on paying dividends it its capital conservation buffer fell below 2.5%.

Limits on Loans to One Borrower. The Bank generally is subject to both FDIC regulations and North Carolina law regarding loans to any one borrower, including related entities. Under applicable law, with certain limited exceptions, loans and extensions of credit by a state chartered nonmember bank to a person outstanding at one time and not fully secured by collateral having a market value at least equal to the amount of the loan or extension of credit shall not exceed 15% of the unimpaired capital of the Bank. In addition, the Bank has an internal policy that loans and extensions of credit fully secured by readily marketable collateral having a market value at least equal to the amount of the loan or extension of credit shall not exceed 10% of the unimpaired capital fund of the Bank. Under the internal policy, the Bank's loans to one borrower were limited to $20.0 million at December 31, 2019.

Transactions with Related Parties. Transactions between the Bank and any affiliate are governed by Sections 23A and 23B of the Federal Reserve Act. An affiliate of the Bank is any company or entity which controls, is controlled by or is under common control with the Bank. In a holding company context, the parent holding company of a bank (such as the Registrant) and any companies which are controlled by such parent holding company are affiliates of the bank. Generally, Sections 23A and 23B (i) limit the extent to which an institution or its subsidiaries may engage in "covered transactions" with any one affiliate to an amount equal to 10% of such institution's capital stock and surplus, and contain an aggregate limit on all such transactions with all affiliates to an amount equal to 20% of such capital stock and surplus and (ii) require that all such transactions be on terms substantially the same, or at least as favorable, to the institution or subsidiary as those provided to a non-affiliate. The term "covered transaction" includes the making of loans, purchase of assets, issuance of a guarantee and similar other types of transactions.

Loans to Directors, Executive Officers and Principal Stockholders. The Bank is subject to the restrictions contained in Section 22(h) of the Federal Reserve Act and the applicable regulations thereunder ("Regulation O") on loans to executive officers, directors and principal stockholders. Under Section 22(h), loans to a director, executive officer and to a greater than 10% stockholder of a state nonmember bank and certain affiliated interests of such persons, may not exceed, together with all other outstanding loans to such person and related interests, the institution's loans-to-one-borrower limit and all loans to such persons may not exceed the institution's unimpaired capital and unimpaired surplus. Section 22(h) also prohibits loans above amounts prescribed by the appropriate federal banking agency to directors, executive officers and greater than 10% stockholders of a depository institution, and their respective affiliates, unless such loan is approved in advance by a majority of the board of directors of the institution with any "interested" director not participating in the voting. Regulation O prescribes the loan amount (which includes all other outstanding loans to such person) as to which such prior board of directors approval is required as being the greater of $25,000 or 5% of capital and surplus (or any loans aggregating $500,000 or more). Further, Section 22(h) requires that loans to directors, executive officers and principal stockholders generally be made on terms substantially the same as offered in comparable transactions to other persons. Section 22(h) also generally prohibits a depository institution from paying the overdrafts of any of its executive officers or directors.

The Bank is also subject to the additional requirements and restrictions of Regulation O on loans to executive officers. Section 22(g) of the Federal Reserve Act requires approval by the board of directors of a depository institution for such extensions of credit and imposes reporting requirements for and additional restrictions on the type, amount and terms of credits to such officers. In addition, Section 106 of the Bank Holding Company Act of 1956, as amended ("BHCA") prohibits extensions of credit to executive officers, directors, and greater than 10% stockholders of a depository institution by any other institution which has a correspondent banking relationship with the institution, unless such extension of credit is on substantially the same terms as those prevailing at the time for comparable transactions with other persons and does not involve more than the normal risk of repayment or present other unfavorable features.

The Volcker Rule. Under provisions of the Dodd-Frank Act referred to as the "Volcker Rule," certain limitations are placed on the ability of bank holding companies and their affiliates to engage in sponsoring, investing in and transacting with certain investment funds, including hedge funds and private equity funds. The Volcker Rule also places restrictions on proprietary trading, which could impact certain hedging activities. The Volcker Rule, which became fully effective in July 2015, has not had a material impact on the Bank or the Registrant. Further, pursuant to EGRRCPA enacted in May 2018, community banks are excluded from the restrictions of the Volcker Rule if (i) the community bank, and every entity that controls it, has total consolidated assets equal to or less than $10 billion and (ii) trading assets and liabilities of the community bank, and every entity that controls it, are equal to or less than five percent of its total consolidated assets.

Restrictions on Certain Activities. State chartered nonmember banks with deposits insured by the FDIC are generally prohibited from engaging in equity investments that are not permissible for a national bank. The foregoing limitation, however, does not prohibit FDIC-insured state banks from acquiring or retaining an equity investment in a subsidiary in which the bank is a majority owner. State chartered banks are also prohibited from engaging as a principal in any type of activity that is not permissible for a national bank and, subject to certain exceptions, subsidiaries of state chartered FDIC-insured banks may not engage as a principal in any type of activity that is not permissible for a subsidiary of a national bank, unless in either case, the FDIC determines that the activity would pose no significant risk to the DIF and the bank is, and continues to be, in compliance with applicable capital standards.

The Registrant cannot predict what legislation might be enacted or what regulations might be adopted in the future, or if enacted or adopted, the effect thereof on the Bank's operations.

Regulation of the Registrant

Federal Regulation. The Registrant is a registered bank holding company subject to examination, regulation and periodic reporting under the Bank Holding Company Act of 1956, as administered by the Federal Reserve Board. The Federal Reserve Board has adopted capital adequacy guidelines for bank holding companies on a consolidated basis.

The status of the Registrant as a registered bank holding company under the Bank Holding Company Act does not exempt it from certain federal and state laws and regulations applicable to corporations generally, including, without limitation, certain provisions of the federal securities laws.

The Registrant is required to obtain the prior approval of the Federal Reserve Board to acquire all, or substantially all, of the assets of any bank or bank holding company. Prior Federal Reserve Board approval is required for the Registrant to acquire direct or indirect ownership or control of any voting securities of any bank or bank holding company if, after giving effect to such acquisition, it would, directly or indirectly, own or control more than five percent of any class of voting shares of such bank or bank holding company.

In addition, in certain such cases, an application to, and the prior approval of, the North Carolina Commissioner of Banks may also be required.

The Registrant is required to give the Federal Reserve Board prior written notice of any purchase or redemption of its outstanding equity securities if the gross consideration for the purchase or redemption, when combined with the net consideration paid for all such purchases or redemptions during the preceding 12 months, is equal to 10% or more of the Registrant's consolidated net worth. The Federal Reserve Board may disapprove such a purchase or redemption if it determines that the proposal would constitute an unsafe and unsound practice, or would violate any law, regulation, Federal Reserve Board order or directive, or any condition imposed by, or written agreement with, the Federal Reserve Board. Such notice and approval is not required for a bank holding company that would be treated as "well capitalized" and "well managed" under applicable regulations of the Federal Reserve Board, that has received a composite "1" or "2" rating at its most recent bank holding company inspection by the Federal Reserve Board, and that is not the subject of any unresolved supervisory issues.

In addition, a bank holding company is prohibited generally from engaging in, or acquiring five percent or more of any class of voting securities of any company engaged in, non-banking activities. One of the principal exceptions to this prohibition is for activities found by the Federal Reserve Board to be so closely related to banking or managing or controlling banks as to be a proper incident thereto. Some of the principal activities that the Federal Reserve Board has determined by regulation to be so closely related to banking as to be a proper incident thereto are:

- making or servicing loans;
- performing certain data processing services;
- providing discount brokerage services;
- acting as fiduciary, investment or financial advisor;
- leasing personal or real property;
- making investments in corporations or projects designed primarily to promote community welfare; and
- acquiring a savings and loan association.

In evaluating a written notice of such an acquisition, the Federal Reserve Board will consider various factors, including among others the financial and managerial resources of the notifying bank holding company and the relative public benefits and adverse effects which may be expected to result from the performance of the activity by an affiliate of such company. The Federal Reserve Board may apply different standards to activities proposed to be commenced de novo and activities commenced by acquisition, in whole or in part, of a going concern. The required notice period may be extended by the Federal Reserve Board under certain circumstances, including a notice for acquisition of a company engaged in activities not previously approved by regulation of the Federal Reserve Board. If such a proposed acquisition is not disapproved or subjected to conditions by the Federal Reserve Board within the applicable notice period, it is deemed approved by the Federal Reserve Board.

However, with the passage of the Gramm-Leach-Bliley Financial Services Modernization Act of 1999, the types of activities in which a bank holding company may engage were significantly expanded. Subject to various limitations, the Modernization Act generally permits a bank holding company to elect to become a “financial holding company.” A financial holding company may affiliate with securities firms and insurance companies and engage in other activities that are “financial in nature.” Among the activities that are deemed “financial in nature” are, in addition to traditional lending activities, securities underwriting, dealing in or making a market in securities, sponsoring mutual funds and investment companies, insurance underwriting and agency activities, certain merchant banking activities and activities that the Federal Reserve Board considers to be closely related to banking.

A bank holding company may become a financial holding company under the Modernization Act if each of its subsidiary banks is “well capitalized” under the Federal Deposit Insurance Corporation Improvement Act prompt corrective action provisions, is well managed and has at least a satisfactory rating under the Community Reinvestment Act. In addition, the bank holding company must file a declaration with the Federal Reserve Board that the bank holding company wishes to become a financial holding company. A bank holding company that falls out of compliance with these requirements may be required to cease engaging in some of its activities. The Registrant has not yet elected to become a financial holding company.

Under the Gramm-Leach-Bliley Act, the Federal Reserve Board serves as the primary “umbrella” regulator of financial holding companies, with supervisory authority over each parent company and limited authority over its subsidiaries. Expanded financial activities of financial holding companies generally will be regulated according to the type of such financial activity: banking activities by banking regulators, securities activities by securities regulators and insurance activities by insurance regulators. The Gramm-Leach-Bliley Act also imposes additional restrictions and heightened data privacy and disclosure requirements regarding non-public information collected by financial institutions.

Capital Requirements. The Federal Reserve Board uses capital adequacy guidelines in its examination and regulation of bank holding companies. If capital falls below minimum guidelines, a bank holding company may, among other things, be denied approval to acquire or establish additional banks or non-bank businesses.

The Federal Reserve Board's capital guidelines establish the following minimum regulatory capital requirements for bank holding companies:

- leverage capital requirement expressed as a percentage of adjusted total assets;
- common equity Tier 1 expressed as a percentage of total risk-weighted assets;
- risk-based requirement expressed as a percentage of total risk-weighted assets; and
- Tier 1 leverage requirement expressed as a percentage of adjusted total assets.

The leverage capital requirement consists of a minimum ratio of total capital to total assets of 4.0%, with an expressed expectation that banking organizations generally should operate above such minimum level. The risk-based requirement consists of a minimum ratio of total capital to total risk-weighted assets of 8.0%, of which at least one-half must be Tier 1 capital (which consists principally of shareholders' equity). The Tier 1 leverage requirement consists of a minimum ratio of Tier 1 capital to total assets of 3.0% for the most highly-rated companies, with minimum requirements of 4.0% to 5.0% for all others.

The risk-based and leverage standards presently used by the Federal Reserve Board are minimum requirements, and higher capital levels will be required if warranted by the particular circumstances or risk profiles of individual banking organizations. Further, any banking organization experiencing or anticipating significant growth would be expected to maintain capital ratios, including tangible capital positions (i.e., Tier 1 capital less all intangible assets), well above the minimum levels.

Source of Strength for Subsidiaries. Bank holding companies are required to serve as a source of financial strength for their depository institution subsidiaries, and, if their depository institution subsidiaries become undercapitalized, bank holding companies may be required to guarantee the subsidiaries' compliance with capital restoration plans filed with their bank regulators, subject to certain limits.

Dividends. As a bank holding company that does not, as an entity, currently engage in separate business activities of a material nature, the Registrant's ability to pay cash dividends depends upon the cash dividends the Registrant receives from the Bank. At present, the Registrant's only source of income is dividends paid by the Bank and interest earned on any investment securities the Registrant holds. The Registrant must pay all of its operating expenses from funds it receives from the Bank. Therefore, shareholders may receive dividends from the Registrant only to the extent that funds are available after payment of our operating expenses and the board decides to declare a dividend. In addition, the Federal Reserve Board generally prohibits bank holding companies from paying dividends except out of operating earnings where the prospective rate of earnings retention appears consistent with the bank holding company's capital needs, asset quality and overall financial condition.

Cross Guaranty Liability. Under the Financial Institutions Reform, Recovery, and Enforcement Act of 1989, or FIRREA, depository institutions are liable to the FDIC for losses suffered or anticipated by the FDIC in connection with the default of a commonly controlled depository institution or any assistance provided by the FDIC to such an institution in danger of default.

Transactions with Affiliates. Subsidiary banks of a bank holding company are subject to certain quantitative and qualitative restrictions imposed by the Federal Reserve Act on any extension of credit to, or purchase of assets from, or letter of credit on behalf of, the bank holding company or its subsidiaries, and on the investment in or acceptance of stocks or securities of such holding company or its subsidiaries as collateral for loans. In addition, provisions of the Federal Reserve Act and Federal Reserve Board regulations limit the amounts of, and establish required procedures and credit standards with respect to, loans and other extensions of credit to officers, directors and principal shareholders of the Bank, the Registrant, any subsidiary of the Registrant and related interests of such persons. Moreover, subsidiaries of bank holding companies are prohibited from engaging in certain tying arrangements (with the holding company or any of its subsidiaries) in connection with any extension of credit, lease or sale of property or furnishing of services.

Any loans by a bank holding company to a subsidiary bank are subordinate in right of payment to deposits and to certain other indebtedness of the subsidiary bank. In the event of a bank holding company's bankruptcy, any commitment by the bank holding company to a federal bank regulatory agency to maintain the capital of a subsidiary bank would be assumed by the bankruptcy trustee and entitled to a priority of payment. This priority would also apply to guarantees of capital plans under the FDIC Improvement Act.

Incentive Compensation Policies and Restrictions. In July 2010, the federal banking agencies issued guidance which applies to all banking organizations supervised by the agencies. Pursuant to the guidance, to be consistent with safety and soundness principles, a banking organization's incentive compensation arrangements should: (1) provide employees with incentives that appropriately balance risk and reward; (2) be compatible with effective controls and risk management; and (3) be supported by strong corporate governance including active and effective oversight by the banking organization's board of directors. Monitoring methods and processes used by a banking organization should be commensurate with the size and complexity of the organization and its use of incentive compensation. While the Dodd-Frank Act contemplated additional regulatory action to be taken related to incentive compensation, the administrative agencies have not yet adopted the contemplated regulations.

Tax Cuts and Jobs Act of 2017. On December 22, 2017, the Tax Cuts and Jobs Act of 2017 (the "Tax Act") was signed into law. The Tax Act includes a number of provisions that impact the Registrant, including the following:

- Tax Rate. The Tax Act replaces the graduated corporate tax rates applicable under prior law, which imposed a maximum tax rate of 35%, with a reduced 21% flat tax rate.

- Employee Compensation. A "publicly held corporation" is not permitted to deduct compensation in excess of $1 million per year paid to certain employees. The Tax Act eliminates certain exceptions to the $1 million limit applicable under prior to law related to performance-based compensation, such as equity grants and cash bonuses that are paid only on the attainment of performance goals.

- Business Asset Expensing. The Tax Act allows taxpayers immediately to expense the entire cost (instead of only 50%, as under prior law) of certain depreciable tangible property and real property improvements acquired and placed in service after September 27, 2017 and before January 1, 2023 (with an additional year for certain property). This 100% "bonus" depreciation is phased out proportionately for property placed in service on or after January 1, 2023 and before January 1, 2027 (with an additional year for certain property).

- Interest Expense. The Tax Act limits a taxpayer's annual deduction of business interest expense to the sum of (i) business interest income and (ii) 30% of "adjusted taxable income," defined as a business's taxable income without taking into account business interest income or expense, net operating losses, and, for 2018 through 2021, depreciation, amortization and depletion.

Future Legislation

The Registrant cannot predict what legislation might be enacted or what regulations might be adopted, or if enacted or adopted, the effect thereof on the Registrant's operations.

ITEM 1A – RISK FACTORS

An investment in the Registrant's common stock involves certain risks. The following discussion highlights the risks that management believes are material for the Registrant, but does not necessarily include all the risks that we may face. Additional risks and uncertainties that are not currently known or that management does not currently deem material could also have a material adverse impact on our business, results of our operations and financial condition. As a result, the trading price of our common stock could decline, and you could lose some or all of your investment. You should carefully consider the risk factors and uncertainties described below and elsewhere in this Report in evaluating an investment in the Registrant's common stock.

Risks Related to Our Business

We may experience unexpected credit losses in connection with the loans we make, which could have a material adverse effect on our capital, financial condition, and results of operations.

As a lender, we face the risk that our borrowers will not repay their loans and guarantors or other related parties will also fail to perform in accordance with the loan terms. A borrower's failure to repay us is usually preceded by missed monthly payments. In some instances, however, a borrower may declare bankruptcy prior to missing payments, and, following a borrower filing bankruptcy, a lender's recovery of the credit extended is often limited. Since many of our loans are secured by collateral, we may attempt to seize the collateral if and when a borrower defaults on a loan. However, the value of the collateral might not equal the amount of the unpaid loan, and we may be unsuccessful in recovering the remaining balance from our borrower. The resolution of nonperforming assets, including the initiation of foreclosure proceedings, requires significant commitments of time from management, which can be detrimental to the performance of their other responsibilities, and which expose us to additional legal costs. Elevated levels of loan delinquencies and bankruptcies in our market areas, generally, and among our borrowers specifically, can be precursors of future charge-offs and may require us to increase our allowance for loan losses. Higher charge-off rates, delays in the foreclosure process or in obtaining judgments against defaulting borrowers or an increase in our allowance for loan losses may negatively impact our overall financial performance, may increase our cost of funds, and could materially adversely affect our business, results of operations and financial condition.

Our allowance for loan losses may be insufficient and significant loan losses could require us to increase our allowance for loan losses through a charge to earnings.

To account for the risk that our borrowers will not repay their loans, we maintain an allowance for loan losses, which is a reserve established through a charge to earnings. The level of the allowance reflects management's continuing evaluation of industry concentrations; specific credit risks; loan loss experience; current loan portfolio quality and trends; present economic, political, and regulatory conditions and unidentified losses inherent in the current loan portfolio. The determination of the appropriate level of the allowance for loan losses inherently involves a high degree of subjectivity and requires us to make significant estimates and assumptions regarding current credit risks and future trends, all of which may undergo material changes. We might underestimate the loan losses inherent in our loan portfolio and have loan losses in excess of the amount recorded in our allowance for loan losses. Changes in economic conditions affecting borrowers, new information regarding existing loans, identification of additional problem loans and other factors, both within and outside our control, may require an increase in the allowance for loan losses. There may be a significant increase in the number of borrowers who are unable or unwilling to repay their loans, resulting in our charging off more loans and increasing our allowance. Furthermore, when real estate values decline, the potential severity of loss on a real estate-secured loan can increase significantly, especially in the case of loans with high combined loan-to-value ratios. Downturns in the national economy and the local economies of the areas in which our loans are concentrated could result in an increase in loan delinquencies, foreclosures or repossessions resulting in increased charge-off amounts and the need for additional loan loss provisions in future periods. If charge-offs in future periods exceed the allowance for probable loan losses; we will need additional provisions to increase the allowance for loan losses. Any increases in the allowance for loan losses will result in a decrease in net income and, possibly, capital, and may have a material adverse effect on our financial condition and results of operations.

In addition, our determination as to the amount of our allowance for loan losses is subject to review by our primary regulators, the FDIC and the Commissioner, as part of their examination process, which may result in the establishment of an additional allowance based upon the judgment of either of these regulators after a review of the information available at the time of their examination. Our allowance for loan losses amounted to $8.3 million and $8.7 million, or 0.81% and 0.88% of total loans outstanding and 69% and 75% of nonperforming loans, at December 31, 2019 and 2018, respectively. See Item 7 of Part II, Management's Discussion and Analysis of Financial Condition and Results of Operations, and **Note E** to our consolidated financial statements presented under Item 8 of Part II of this Form 10-K, for further discussion related to our process for determining the appropriate level of the allowance for probable loan losses.

An increase in our nonperforming assets will negatively affect our earnings.

Our nonperforming assets adversely affect our net income in various ways. We do not record interest income on non-accrual loans or other real estate owned. We must reserve for probable losses, which is established through a current period charge to the provision for loan losses, and, from time to time as appropriate, write down the value of properties in our other real estate owned portfolio to reflect changing market values. Additionally, there are legal fees associated with the resolution of problem assets as well as carrying costs such as taxes, insurance and maintenance related to our other real estate owned. Further, the resolution of nonperforming assets requires the active involvement of management, which can distract them from other responsibilities. Finally, if our estimate for the recorded allowance for loan losses proves to be incorrect and our allowance is inadequate, we will have to increase the allowance accordingly, which would decrease our net income and may have a material adverse effect on our financial condition and results of operations.

The geographic concentration of our loan portfolio and lending activities makes us vulnerable to a downturn in the local economy.

Nearly all of our loans are secured by real estate or made to businesses in our market area, which includes portions of central and eastern North Carolina, southeastern Virginia and northwestern South Carolina. As a result of this geographic concentration, our results may correlate to the economic conditions in these areas. Declines in these markets' economic conditions may adversely affect the quality of our loan portfolio and the demand for our products and services, and accordingly, our results of operations. Adverse conditions in the local economy such as inflation, unemployment, recession or other factors beyond our control could impact the ability of our borrowers to repay their loans, which could impact our financial condition and results of operations.

A decline in local economic conditions could adversely affect the values of real property used as collateral for our loans. Consequently, a decline in local economic conditions may have a greater effect on our earnings and capital than on the earnings and capital of larger financial institutions whose real estate loan portfolios are more geographically diverse. At December 31, 2019, approximately 91.9% of the Bank's loans had real estate as a primary or secondary component of collateral. The real estate collateral in each case provides an alternate source of repayment in the event of default by the borrower and may deteriorate in value during the time the credit is extended. If the value of real estate in our market area were to decline materially, a significant portion of our loan portfolio could become under-collateralized and/or cause us to realize a loss in the event of a foreclosure. If we are required to liquidate the collateral securing a loan to satisfy the debt during a period of reduced real estate values, our earnings and capital could be adversely affected.

A significant portion of our loan portfolio consists of loans for commercial real estate and construction, which carry greater historical credit risk than residential mortgage loans.

We originate commercial real estate loans and commercial and industrial loans, most often secured by commercial properties and construction loans primarily within our market area. These loans tend to involve larger loan balances to a single borrower or groups of related borrowers, more complex underlying collateral, and are most susceptible to a risk of loss during a downturn in the business cycle. These loans also have historically had greater credit risk than residential real estate loans for the following reasons:

- *Commercial Real Estate Loans.* Repayment is dependent on income being generated in amounts sufficient to cover operating expenses and debt service. These loans also involve greater risk because they are generally not fully amortizing over a loan period, but rather have a balloon payment due at maturity. A borrower's ability to make a balloon payment typically will depend on being able to either refinance the loan or timely sell the underlying property. As of December 31, 2019, commercial real estate loans were approximately 44.6% of the Bank's total loan portfolio.

- *Construction Loans.* Repayment is dependent on completion of the project and the subsequent financing of the completed project as a commercial real estate or residential real estate loan, and in some instances on the rent or sale of the underlying project. The risk of loss is largely dependent on our initial estimate of whether the property's value at completion equals or exceeds the cost of property construction and the availability of take-out financing. During the construction phase, a number of factors can result in delays or cost overruns. If our estimate is inaccurate or if actual construction costs exceed estimates, the value of the property securing our loan may be insufficient to ensure full repayment when completed through a permanent loan, sale of the property, or by seizure of collateral. As of December 31, 2019, construction loans were approximately 21.6% of the Bank's total loan portfolio.

- *Commercial and Industrial Loans.* Repayment is generally dependent upon the successful operation of the borrower's business. In addition, the collateral securing the loans may depreciate over time, be difficult to appraise, be more difficult to liquidate than residential real estate, or fluctuate in value based on the success of the business. As of December 31, 2019, commercial and industrial loans were approximately 7.4% of the Bank's total loan portfolio.

Our commercial real estate loans include both owner and non-owner occupied properties. Non-owner occupied properties expose us to a greater risk of non-payment and loss than loans secured by owner-occupied properties because repayment of such loans depends primarily on the tenant's continuing ability to pay rent to the property owner, who is our borrower, or, if the property owner is unable to find a tenant, the property owner's ability to repay the loan without the benefit of a rental income stream, or other events beyond the borrower's control. In addition, the physical condition of non-owner-occupied properties is often below that of owner-occupied properties due to lax property maintenance standards, which has a negative impact on the value of the collateral properties. Furthermore, some of our non-owner-occupied borrowers have more than one loan outstanding with us, which may expose us to a greater risk of loss compared to residential and commercial borrowers with only one loan.

We are exposed to risks in connection with residential mortgage loans.

We originate fixed and adjustable rate loans secured by one-to-four family residential real estate. As of December 31, 2019, we had $151.7 million in residential mortgage loans, which represented 14.7% of our total loan portfolio. The residential loans in our loan portfolio are sensitive to regional and local economic conditions that significantly impact the ability of borrowers to meet their loan payment obligations, making loss levels difficult to predict. Residential loans with high combined loan-to-value ratios generally are more sensitive and may experience a higher incidence of default and severity of losses. In addition, if the borrowers sell their homes, the borrowers may be unable to repay their loans in full from the sale proceeds. As a result, these loans may experience higher rates of delinquencies, defaults and losses, which could in turn adversely affect our financial condition and results of operations.

We depend on the accuracy and completeness of information about clients and counterparties.

In deciding whether to extend credit or enter into other transactions with clients and counterparties, we may rely on information furnished to us by or on behalf of clients and counterparties, including financial statements and other financial information. We also may rely on representations of clients and counterparties as to the accuracy and completeness of that information and, with respect to financial statements, on reports of independent auditors. For example, in deciding whether to extend credit to clients, we may assume that a customer's audited financial statements conform to accounting principles generally accepted in the United States of America ("GAAP") and present fairly, in all material respects, the financial condition, results of operations and cash flows of the customer. Our earnings are significantly affected by our ability to properly originate, underwrite and service loans. Our financial condition and results of operations could be negatively impacted to the extent we incorrectly assess the creditworthiness of our borrowers, fail to detect or respond to deterioration in asset quality in a timely manner, or rely on financial statements that do not comply with GAAP or are materially misleading.

We may be forced to foreclose on the collateral property securing our loans and own the underlying real estate, which may subject us to the increased risks and costs associated with the ownership of real property.

We originate loans secured by real estate and from time to time are forced to foreclose on the collateral property to protect our investment and may thereafter own and operate such property, which exposes us to the inherent risks of real property ownership. The amount that we, as a lender, may realize after a default is dependent upon factors outside of our control, including, but not limited to:

- general or local economic conditions;
- environmental cleanup liability;
- neighborhood values;
- interest rates;
- real estate tax rates;
- operating expenses of the mortgaged properties;
- supply of and demand for rental units or properties;
- ability to obtain and maintain adequate occupancy of the properties;
- zoning laws;
- governmental rules, regulations and fiscal policies; and
- natural or other disasters.

Certain expenditures associated with the ownership of real estate, principally real estate taxes and maintenance costs, may adversely affect the income from the real estate. Therefore, the cost of operating real property may exceed the rental income earned from such property, and we may have to advance funds in order to protect our investment or we may be required to dispose of the real property at a loss. This may result in reduced net income, which may have a material adverse effect on our financial condition and results of operations.

Our expansion strategy may expose us to additional risks related to our acquisition of other financial institutions.

Our acquisition of other financial institutions, or parts of other institutions, such as with branch acquisitions, involves a number of risks, including the risk that:

- we may incur substantial costs in identifying and evaluating potential acquisitions and merger partners, or in evaluating new markets, hiring experienced, local managers, and opening new offices;
- our estimates and judgments used to evaluate credit, operations, management and market risks relating to target institutions may not be accurate;
- the institutions we acquire may have distressed assets and there can be no assurance that we will be able to realize the value we predict from those assets or that we will make sufficient provisions or have sufficient capital for future losses;
- we may be required to take write-downs or write-offs, restructuring and impairment, or other charges related to the institutions we acquire that could have a significant negative effect on our financial condition and results of operations;
- there may be substantial lag-time between completing an acquisition and generating sufficient assets and deposits to support costs of the expansion;
- our management's attention in negotiating a transaction and integrating the operations and personnel of the combining businesses may be diverted from our existing business and we may not be able to successfully integrate such operations and personnel;
- we may enter new markets where we lack local experience or that introduce new risks to our operations, or that otherwise result in adverse effects on our results of operations;
- we may introduce new products and services we are not equipped to manage or that introduce new risks to our operations, or that otherwise result in adverse effects on our results of operations;
- we may incur intangible assets in connection with an acquisition, or the intangible assets we incur may become impaired, which could result in adverse short-term effects on our results of operations;
- we may assume liabilities in connection with an acquisition, including unrecorded liabilities that are not discovered at the time of the transaction, and the repayment of those liabilities may have an adverse effect on our results of operations, financial condition and stock price; or
- we may lose key employees and customers that were part of the reason we pursued an acquisition.

We cannot assure you that we will be able to successfully integrate any banks or banking offices that we acquire into our operations or retain the customers that we acquire in any acquisition. If any of these risks occur in connection with our expansion efforts, it may have a material and adverse effect on our results of operations and financial condition.

We face additional risk of litigation due to our acquisition strategy.

In addition to the ordinary risk of litigation that we face in connection with our day-to-day banking activities, we also face litigation risk in connection with our strategy to grow through acquisition of other financial institutions or parts of other institutions, such as with branch acquisitions. The Company, as well as our directors and officers and the companies we seek to acquire, may face claims from shareholders related to transaction disclosures or alleged breaches of fiduciary duties in connection with entering into such acquisition transactions. The defense or settlement of any such lawsuit or claims, or the delay that any such lawsuit may cause on the strategic acquisitions that we pursue, may adversely affect the Company's business, financial condition, results of operations and cash flows.

We may be subject to environmental liability associated with our lending activities.

A significant portion of our loan portfolio is secured by real property. During the ordinary course of business, we may foreclose on and take title to properties securing certain loans. In doing so, there is a risk that hazardous or toxic substances could be found on these properties. If hazardous or toxic substances are found, we may be liable for remediation costs, as well as for personal injury and property damage. Environmental laws may require us to incur substantial expenses and may materially reduce the affected property's value or limit our ability to use or sell the affected property. In addition, future laws or more stringent interpretations or enforcement policies with respect to existing laws may increase our exposure to environmental liability. Although we have policies and procedures to perform an environmental review before initiating any foreclosure action on nonresidential real property, these reviews may not be sufficient to detect all potential environmental hazards. The remediation costs and any other financial liabilities associated with an environmental hazard could have a material adverse effect on our financial condition and results of operations.

Changes in interest rates affect our profitability and the value of our interest-earning assets.

The Bank derives its income primarily from the difference or "spread" between the interest earned on loans, securities and other interest-earning assets, and interest paid on deposits, borrowed funds and other interest-bearing liabilities. In general, the larger the spread, the more the Bank earns. When market rates of interest change, the interest the Bank receives on its assets and the interest the Bank pays on its liabilities will fluctuate. Changes in market interest rates could adversely affect our interest rate spread and, as a result, our net interest income. Although the yield we earn on our assets and our funding costs tend to move in the same direction in response to changes in interest rates, one can rise or fall faster than the other, causing our interest rate spread to expand or contract. Our liabilities are shorter in duration than our assets, so they will adjust faster in response to changes in interest rates. As a result, when interest rates rise, our funding costs generally will rise faster than the yield we earn on our assets, causing our interest rate spread to contract until the yield catches up. Changes in the slope of the "yield curve"—or the spread between short-term and long-term interest rates—will also reduce our interest rate spread. Normally, the yield curve is upward sloping, meaning short-term rates are lower than long-term rates. Because our liabilities are shorter in duration than our assets, when the yield curve flattens or even inverts, we will experience pressure on our interest rate spread as our cost of funds increases relative to the yield we can earn on our assets. In addition, our mortgage banking income is sensitive to changes in interest rates. During periods of rising and relatively higher interest rates, mortgage originations for purchased homes can decline considerably and refinanced mortgage activity can severely decrease. During periods of falling and relatively lower interest rates, the opposite effects can occur.

Changes in market interest rates could reduce the value of the Bank's financial assets. Fixed-rate investments, mortgage-backed and related securities and mortgage loans generally decrease in value as interest rates rise. In addition, interest rates affect how much money the Bank lends. For example, when interest rates rise, the cost of borrowing increases and the loan originations tend to decrease.

Interest rates are highly sensitive to many factors that are beyond our control, including general economic conditions and policies of various governmental and regulatory agencies and, in particular, the Federal Open Market Committee of the Federal Reserve Board. Changes in monetary policy, including changes in interest rates, could influence not only the interest we receive on loans and securities and the amount of interest we pay on deposits and borrowings, but such changes could also affect our ability to originate loans and obtain deposits. If the Bank is unsuccessful in managing the effects of changes in interest rates, the financial condition and results of operations could suffer. Any substantial, unexpected, prolonged change in market interest rates could have a material adverse effect on our business, financial condition and results of operations.

Hurricanes or other adverse weather events could disrupt our operations, which could have an adverse effect on our business or results of operations.

North Carolina's coastal region and inland areas of eastern North Carolina are affected, from time to time, by adverse weather events, particularly hurricanes. We cannot predict whether, or to what extent, damage caused by future hurricanes or other weather events will affect our operations. Weather events could cause a disruption in our day-to-day business activities and could have a material adverse effect on our business, results of operations and financial condition.

We are subject to extensive regulation that could restrict our activities, have an adverse impact on our operations, and impose financial requirements or limitations on the conduct of our business.

We operate in a highly regulated industry and are subject to examination, supervision, and comprehensive regulation by various regulatory agencies. The Company is subject to Federal Reserve Board regulation, and the Bank is subject to extensive regulation, supervision, and examination by the FDIC and the Commissioner. In addition, as a member of the FHLB of Atlanta, the Bank must comply with applicable regulations of the Federal Housing Finance Agency and the FHLB. The Bank's activities are also regulated under consumer protection laws applicable to our lending, deposit, and other activities. A claim against us under these laws could have a material adverse effect on our results of operations.

Regulation by these agencies is intended primarily for the protection of our depositors and the deposit insurance fund and not for the benefit of our shareholders. Federal and state regulators have the ability to impose substantial sanctions, restrictions, and requirements on us if they identify violations of laws with which we must comply or weaknesses or failures with respect to general standards of safety and soundness. Such enforcement may be formal or informal and can include directors' resolutions, memoranda of understanding, written supervisory agreements, cease-and-desist orders, civil money penalties and termination of deposit insurance and bank closures. Enforcement actions may be taken regardless of the capital levels of the institutions, and regardless of prior examination findings. Any of these consequences could damage our reputation, restrict our ability to expand our business or could require us to raise additional capital or sell assets on terms that are not advantageous to us or our shareholders and could have a material adverse effect on our business, financial condition and results of operations. While we have policies and procedures designed to prevent any such violations, such violations may occur despite our best efforts.

Changes in laws and regulations and the cost of regulatory compliance with new laws and regulations may adversely affect our operations.

Congress and federal regulatory agencies continually review banking laws, regulations and policies for possible changes. The Dodd-Frank Wall Street Reform and Consumer Protection Act, enacted in July 2010, instituted major changes to the banking and financial institutions regulatory regimes and is one example of how legislative changes can greatly impact our business. Changes to statutes, regulations or regulatory policies or supervisory guidance, including changes in interpretation or implementation of statutes, regulations, policies or supervisory guidance, could affect us in substantial and unpredictable ways, including, among other things, subjecting us to increased capital requirements, liquidity and risk management requirements, creating additional costs, limiting the types of financial services and products we may offer and/or increasing the ability of non-banks to offer competing financial services and products. While we cannot predict the extent to which additional legislation will be enacted or the extent we will become subject to increased regulatory scrutiny by any of these regulatory agencies, any regulatory changes or scrutiny could increase or decrease the cost of doing business, limit or expand our permissible activities, or affect the competitive balance among banks, credit unions, savings and loan associations, and other institutions.

We face a risk of noncompliance and enforcement action with the Bank Secrecy Act and other anti-money laundering statutes and regulations.

The federal Bank Secrecy Act, the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (the "Patriot Act") and other laws and regulations require financial institutions, among other duties, to institute and maintain effective anti-money laundering programs, conduct enhanced customer due diligence, and file suspicious activity and currency transaction reports as appropriate. The federal Financial Crimes Enforcement Network, established by the U.S. Treasury Department to administer the Bank Secrecy Act, is authorized to impose significant civil money penalties for violations of those requirements and has recently engaged in coordinated enforcement efforts with the individual federal banking regulators, as well as the U.S. Department of Justice, Drug Enforcement Administration and Internal Revenue Service. There is also increased scrutiny of compliance with the rules enforced by the U.S. Treasury's Office of Foreign Assets Control. Federal and state bank regulators also focus on compliance with the Bank Secrecy Act and anti-money laundering regulations. If our policies, procedures and systems are deemed deficient or the policies, procedures and systems of the financial institutions that we have already acquired or may acquire in the future are deficient, we would be subject to liability, including fines and regulatory actions such as restrictions on our ability to proceed with certain aspects of our business plan, including our acquisition plans, which would negatively impact our business, financial condition and results of operations. Failure to maintain and implement adequate programs to combat money laundering and terrorist financing could also have serious reputational consequences for us.

Federal, state and local consumer lending laws may restrict our ability to originate certain mortgage loans or increase our risk of liability with respect to such loans and could increase our cost of doing business.

Federal, state and local laws have been adopted that are intended to eliminate certain lending practices considered “predatory.” These laws prohibit practices such as steering borrowers away from more affordable products, selling unnecessary insurance to borrowers, repeatedly refinancing loans and making loans without a reasonable expectation that the borrowers will be able to repay the loans irrespective of the value of the underlying property. Loans with certain terms and conditions and that otherwise meet the definition of a “qualified mortgage” may be protected from liability to a borrower for failing to make the necessary determinations. It is our policy not to make predatory loans and to determine borrowers’ ability to repay in accordance with regulatory standards, but the law and related rules create the potential for increased liability with respect to our lending and loan investment activities. They increase our cost of doing business and, ultimately, may prevent us from making certain loans and impact the cost and pricing of loans that we make.

We are subject to federal and state fair lending laws, and failure to comply with these laws could lead to material penalties.

Federal and state fair lending laws and regulations, such as the Equal Credit Opportunity Act and the Fair Housing Act, impose nondiscriminatory lending requirements on financial institutions. The Department of Justice, Consumer Financial Protection Bureau and other federal and state agencies are responsible for enforcing these laws and regulations. Private parties may also have the ability to challenge an institution’s performance under fair lending laws in private class action litigation. A successful challenge to our performance under the fair lending laws and regulations could adversely impact our rating under the Community Reinvestment Act and result in a wide variety of sanctions, including the required payment of damages and civil money penalties, injunctive relief, imposition of restrictions on merger and acquisition activity and restrictions on expansion activity, which could negatively impact our reputation, business, financial condition and results of operations.

The Federal Reserve Board may require us to commit capital resources to support the Bank.

The Federal Reserve Board requires a bank holding company to act as a source of financial and managerial strength to a subsidiary bank and to commit resources to support such subsidiary bank. Under the “source of strength” doctrine, the Federal Reserve Board may require a bank holding company to make capital injections into a troubled subsidiary bank and may charge the bank holding company with engaging in unsafe and unsound practices for failure to commit resources to such a subsidiary bank. In addition, the Dodd-Frank Act directs the federal bank regulators to require that all companies that directly or indirectly control an insured depository institution serve as a source of strength for the institution. Under these requirements, in the future, we could be required to provide financial assistance to our Bank if the Bank experiences financial distress.

A capital injection may be required at times when we do not have the resources to provide it, and therefore we may be required to borrow the funds. In the event of a bank holding company’s bankruptcy, the bankruptcy trustee will assume any commitment by the holding company to a federal bank regulatory agency to maintain the capital of a subsidiary bank. Moreover, bankruptcy law provides that claims based on any such commitment will be entitled to a priority of payment over the claims of the holding company’s general unsecured creditors, including the holders of its note obligations. Thus, any borrowing that must be done by the holding company in order to make the required capital injection becomes more difficult and expensive and will adversely impact the holding company’s cash flows, financial condition, results of operations and prospects.

If we fail to maintain an effective system of internal control over financial reporting, we may not be able to accurately report our financial results. As a result, current and potential shareholders could lose confidence in our financial reporting, which would harm our business and the trading price of our securities.

If we identify material weaknesses in our internal control over financial reporting or are otherwise required to restate our financial statements, we could be required to implement expensive and time-consuming remedial measures and could lose investor confidence in the accuracy and completeness of our financial reports. We may also face regulatory enforcement or other actions, including the potential delisting of our securities from NASDAQ. This could have a material adverse effect on our business, financial condition and results of operations, and could subject us to litigation.

Changes in accounting standards and management's selection of accounting methods, including assumptions and estimates, could materially impact our financial statements.

We are subject to the accounting rules and regulations of the Securities and Exchange Commission (the "SEC") and the Financial Accounting Standards Board (the "FASB"). From time to time, the SEC and the FASB update accounting principles generally accepted in the United States that govern the preparation of our financial statements. These updates may require extraordinary efforts or additional costs to implement. Any of these rules or regulations may be modified or changed from time to time, and there can be no assurance that such modifications or changes will not adversely affect us. These changes can be hard to predict and can materially impact how we record and report our financial condition and results of operations. In some cases, we could be required to apply a new or revised standard retroactively, resulting in changes to previously reported financial results, or a cumulative charge to retained earnings. In addition, management is required to use certain assumptions and estimates in preparing our financial statements, including determining the fair value of certain assets and liabilities, among other items. If the assumptions or estimates are incorrect, we may experience unexpected material adverse consequences that could negatively affect our business, results of operations and financial condition.

The FASB has issued an accounting standard update that will result in a significant change in how we recognize credit losses and may have a material impact on our financial condition or results of operations.

In June 2016, the FASB issued an accounting standard update, "Financial Instruments-Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments," which replaces the current "incurred loss" model for recognizing credit losses with an "expected loss" model referred to as the Current Expected Credit Loss ("CECL") model. Under the CECL model, we will be required to present certain financial assets carried at amortized cost, such as loans held for investment and held-to-maturity debt securities, at the net amount expected to be collected over the contractual life of the financial instrument. The measurement of expected credit losses is to be based on information about past events, including historical experience, current conditions, and reasonable and supportable forecasts that affect the collectability of the reported amount. This measurement will take place at the time the financial asset is first added to the balance sheet and periodically thereafter. This differs significantly from the "incurred loss" model required under current GAAP, which delays recognition until it is probable a loss has been incurred. Accordingly, we expect that the adoption of the CECL model will materially affect how we determine our allowance for loan losses and could require us to significantly increase our allowance. Moreover, the CECL model may create more volatility in the level of our allowance for loan losses. If we are required to materially increase our level of allowance for loan losses for any reason, such increase could adversely affect our business, financial condition and results of operations.

The new CECL standard will become effective for us on January 1, 2023 based on our qualifying metrics on December 31, 2019. The new effective date remains in place even if our qualifying metrics change to those applicable for institutions required to adopt CECL as of December 31, 2019. We are currently evaluating the impact the CECL model will have on our accounting, but we expect to recognize a one-time cumulative-effect adjustment to our allowance for loan losses as of the beginning of the first reporting period in which the new standard is effective, consistent with regulatory expectations set forth in interagency guidance issued at the end of 2016. Since the magnitude of the anticipated change in the allowance for loan losses will be impacted by economic conditions and trends in the loan portfolio at the time of adoption, we cannot yet reasonably determine the magnitude of any such one-time cumulative adjustment or of the overall impact of the new standard on our financial condition or results of operations.

We may be required to raise additional capital in the future, including to comply with minimum capital thresholds established by our regulators, but that capital may not be available when it is needed and could be dilutive to our existing shareholders, which could adversely affect our financial condition and results of operations.

Bank holding companies and federally insured banks are required to maintain minimum levels of regulatory capital. Compliance by the Registrant and the Bank with these capital requirements affects our business by increasing the amount of capital required to conduct operations. In order to support the operations at the Bank, we may need to raise capital in the future. Our ability to raise capital will depend in part on conditions in the capital markets at that time, which are outside our control. Accordingly, we may be unable to raise capital on terms acceptable to us, if at all. If we cannot raise capital when needed, our ability to operate or further expand our operations could be materially impaired. In addition, if we decide to raise equity capital under such conditions, the interests of our shareholders could be diluted.

We may need additional access to capital, which we may be unable to obtain on attractive terms or at all.

We may need to incur additional debt or equity financing in the future to make strategic acquisitions or investments, for future growth, to fund losses or additional provisions for loan losses in the future, or to strengthen our capital ratios. Our ability to raise additional capital, if needed, will depend in part on conditions in the capital markets at that time, which are outside our control, and on our financial performance. Accordingly, we may be unable to raise additional capital, if and when needed, on terms acceptable to us, or at all. If we cannot raise additional capital when needed, our ability to further expand our operations through internal growth and acquisitions could be materially impaired and our stock price could be negatively affected. In addition, if we decide to raise additional equity capital, our current shareholders' interests could be diluted.

We are subject to liquidity risk that may affect our ability to meet our obligations and fund our operations.

The primary sources of our Bank's funds are client deposits and loan repayments. While scheduled loan repayments are a relatively stable source of funds, they are subject to the ability of borrowers to repay the loans. The ability of borrowers to repay loans can be adversely affected by a number of factors, including changes in economic conditions, adverse trends or events affecting business industry groups, reductions in real estate values or markets, business closings or lay-offs, inclement weather, natural disasters, and international instability. Additionally, deposit levels may be affected by a number of factors, including rates paid by competitors, general interest rate levels, regulatory capital requirements, returns available to clients on alternative investments and general economic conditions.

Accordingly, we may be required from time to time to rely on secondary sources of liquidity to meet withdrawal demands or otherwise fund operations. Such sources include FHLB advances, sales of securities and loans, and federal funds lines of credit from correspondent banks, as well as out-of-market time deposits. While we believe that these sources are currently adequate, there can be no assurance they will be sufficient to meet future liquidity demands, particularly if we continue to grow and experience increasing loan demand. We may be required to slow or discontinue loan growth, capital expenditures or other investments or liquidate assets should such sources not be adequate, which could have a material adverse effect on our earnings and financial condition.

Increases in FDIC insurance premiums may adversely affect our net income and profitability.

The last economic recession caused a high level of bank failures, which dramatically increased FDIC resolution costs and led to a significant reduction in the balance of the DIF. As a result, the FDIC significantly increased the initial base assessment rates paid by financial institutions for deposit insurance. We are generally unable to control the amount of premiums that the Bank is required to pay for FDIC insurance. If there are bank or financial institution failures that exceed the FDIC's expectations, the Bank may be required to pay higher FDIC premiums than those currently in force. Any future increases or required prepayments of FDIC insurance premiums may adversely impact our earnings and financial condition.

We rely on other companies to provide key components of our business infrastructure.

Third-party vendors provide key components of our business infrastructure such as internet connections, network access, core application processing, and operational software. While we have selected these third-party vendors carefully, we do not control their actions. Any problems caused by these third parties, including as a result of their not providing us their services for any reason or their performing their services poorly, could adversely affect our ability to deliver products and services to our customers and otherwise to conduct our business. Any such failures could damage our reputation, which could negatively affect our operating results. Replacing these third-party vendors could also entail significant delay and expense.

Security breaches and other information system disruptions, such as cyber-attacks, could compromise our information and expose us to liability, which would cause our business and reputation to suffer.

The banking industry has experienced increasing efforts on the part of third parties, including through cyber-attacks, to breach data security at financial institutions or with respect to financial transactions. There have been several recent instances involving financial services and consumer-based companies reporting the unauthorized disclosure of client or customer information or the destruction or theft of corporate data. In addition, because the techniques used to cause such security breaches change frequently, often are not recognized until launched against a target and may originate from less regulated and remote areas around the world, we may be unable to proactively address these techniques or to implement adequate preventative measures. The ability of our customers to bank remotely, including online and through mobile devices, requires secure transmission of confidential information and increases the risk of data security breaches.

In the ordinary course of our business, we collect and store sensitive data, including our proprietary business information and that of our customers, and personally identifiable information of our customers and employees, on our networks. The secure processing, maintenance and transmission of this information is critical to our operations. Despite our security measures, our information technology and infrastructure may be vulnerable to attacks by hackers or breached due to employee error, malfeasance or other disruptions. Any failure, interruption, or breach in security or operational integrity of these systems could compromise our networks and the information stored there could be accessed, publicly disclosed, lost or stolen. Any such access, disclosure or other loss of information could result in legal claims or proceedings, liability under laws that protect the privacy of personal information, and regulatory penalties, disrupt our operations and the services we provide to customers, damage our reputation, and cause a loss of confidence in our products and services, which could adversely affect our financial condition, revenues and competitive position.

Regulations relating to privacy, information security and data protection could increase our costs, affect or limit how we collect and use personal information and adversely affect our business opportunities.

We are subject to various privacy, information security and data protection laws, including requirements concerning security breach notification, and we could be negatively impacted by these laws. For example, our business is subject to the Gramm-Leach-Bliley Act which, among other things: (i) imposes certain limitations on our ability to share non-public personal information about our customers with non-affiliated third parties; (ii) requires that we provide certain disclosures to customers about our information collection, sharing and security practices and afford customers the right to “opt out” of any information sharing by us with non-affiliated third parties (with certain exceptions) and (iii) requires we develop, implement and maintain a written comprehensive information security program containing appropriate safeguards based on our size and complexity, the nature and scope of our activities, and the sensitivity of customer information we process, as well as plans for responding to data security breaches. Various state and federal banking regulators and states have also enacted data security breach notification requirements with varying levels of individual, consumer, regulatory or law enforcement notification in certain circumstances in the event of a security breach. Moreover, legislators and regulators in the United States are increasingly adopting or revising privacy, information security and data protection laws that potentially could have a significant impact on our current and planned privacy, data protection and information security-related practices, our collection, use, sharing, retention and safeguarding of consumer or employee information, and some of our current or planned business activities. This could also increase our costs of compliance and business operations and could reduce income from certain business initiatives. This includes increased privacy-related enforcement activity at the federal level, by the Federal Trade Commission, as well as at the state level, such as with regard to mobile applications.

Compliance with current or future privacy, data protection and information security laws (including those regarding security breach notification) affecting customer or employee data to which we are subject could result in higher compliance and technology costs and could restrict our ability to provide certain products and services, which could have a material adverse effect on our business, financial conditions or results of operations. Our failure to comply with privacy, data protection and information security laws could result in potentially significant regulatory or governmental investigations or actions, litigation, fines, sanctions and damage to our reputation, which could have a material adverse effect on our business, financial condition or results of operations.

Failure to keep pace with technological change could adversely affect our business.

The banking industry undergoes frequent technological changes with introductions of new technology-driven products and services. In addition to improving customer services, the effective use of technology increases efficiency and enables financial institutions to reduce costs. Our future success will depend, in part, on our ability to address the needs of our customers by using technology to provide products and services that will satisfy customer demands for convenience as well as to create additional efficiencies in our operations. Many of our competitors have substantially greater resources to invest in continuous technological improvements than we do. We may not be able to quickly deploy these new products and services or be successful in marketing these products and services to our customers. Additionally, the implementation of changes and maintenance to current systems may cause service interruptions, transaction processing errors and system conversion delays. Failure to successfully keep pace with technological change affecting the banking industry while avoiding interruptions, errors and delays could have a material adverse effect on our business, financial condition or results of operations.

We generally outsource a portion of the operational and technological modifications and improvements we make to third parties, and they may experience errors or disruptions that could adversely impact us and over which we may have limited control. In addition, these third parties could also be the source of an attack on, or breach of, our operational systems, data or infrastructure. We also face risk from the integration of new infrastructure platforms and/or new third-party providers of such platforms into our existing businesses.

We may not be able to realize the remaining benefit of our deferred tax assets.

As of December 31, 2019 and 2018, we had a net deferred tax asset of $2.8 million and $3.7 million, respectively. A deferred tax asset is reduced by a valuation allowance if, based on the weight of the evidence available, it is more likely than not that some portion or all of the total deferred tax asset will not be realized. In assessing the future ability of the Company to realize the deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. The Company will continue to monitor its deferred tax assets closely to evaluate whether we will be able to realize the full benefit of our net deferred tax asset or whether there is any need for a valuation allowance. Significant negative trends in credit quality, losses from operations, or other factors could impact the realization of the deferred tax asset in the future. If we are unable to realize the full benefit of the deferred tax assets, it could negatively impact our results of operations.

If our goodwill becomes impaired, we may be required to record a significant charge to earnings.

We have goodwill recorded on our balance sheet as an asset with a carrying value as of December 31, 2019 of $24.6 million. Under GAAP, goodwill is required to be tested for impairment at least annually and between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount. The test for goodwill impairment involves comparing the fair value of a company's reporting units to their respective carrying values. The Bank is our only reporting unit. The price of our common stock is one of several factors available for estimating the fair value of our reporting units. Although the price of our common stock is currently trading above book value, it has traded below book value in the past and may do so again in the future. Subject to the results of other valuation techniques, if this situation were to return and persist, it could indicate that a portion of our goodwill is impaired. Accordingly, for this reason or other reasons that indicate that the goodwill at any of our reporting units is impaired, we may be required to record a significant charge to earnings in our financial statements during the period in which any impairment of our goodwill is determined, which could have a negative impact on our results of operations.

We may not be able to effectively compete with larger financial institutions for business.

Commercial banking in North Carolina, South Carolina and Virginia is extremely competitive. The Bank competes with some of the largest banking organizations in the state and the country and other financial institutions, such as federally and state-chartered savings and loan institutions and credit unions, as well as consumer finance companies, mortgage companies and other lenders engaged in the business of extending credit. Many of these competitors have broader geographic markets, higher lending limits, more services, and more media advertising than we do. We may not be able to compete effectively in our markets, and our results of operations could be adversely affected by the nature or pace of change in competition.

Consumers may decide not to use banks to complete their financial transactions.

Technology and other changes are allowing parties to complete financial transactions that historically have involved banks through alternative methods. For example, consumers can now maintain funds that historically would have been held as bank deposits in brokerage accounts or mutual funds. Consumers can also complete transactions such as peer-to-peer payments, paying bills and/or transferring funds directly without the assistance of banks. The process of eliminating banks as intermediaries could result in the loss of fee income, as well as the loss of customer deposits resulting in reduced liquidity and loss of income generated from those deposits. Additionally, our customer base of consumers and small businesses has increasing non-bank options for credit. Now that credit is available through the Internet, competition for small balance loans is expected to increase. The loss of these revenue streams and the lower cost deposits as a source of funds could have a material adverse effect on our financial condition and results of operations.

We may not be able to attract and retain skilled people and the lack of sufficient talent could adversely impact our operations.

Our success depends in part on our ability to retain key executives and to attract and retain additional qualified management personnel who have experience both in sophisticated banking matters and in operating a small- to mid-size bank. Competition for such personnel is strong in the banking industry and we may not be successful in attracting or retaining the personnel we require. Consequently the loss of one or more members of our executive management team may have a material adverse effect on our operations.

Our business reputation is important and any damage to it could have a material adverse effect on our business.

Our reputation is very important to sustain our business, as we rely on our relationships with our current, former and potential customers and shareholders, and the industries that we serve. Any damage to our reputation, whether arising from legal, regulatory, supervisory or enforcement actions, matters affecting our financial reporting or compliance with SEC and exchange listing requirements, negative publicity, the conduct of our business or otherwise could have a material adverse effect on our business, results of operations and financial condition.

Risks Related to an Investment in Our Common Stock

The relatively low trading volume in our common stock may adversely affect your ability to resell shares at prices that you find attractive or at all.

Our common stock is listed for quotation on the Nasdaq Global Market under the ticker symbol "SLCT". The average daily trading volume for our common stock is less than that of larger financial institutions. Due to its relatively low trading volume, sales of our common stock may place significant downward pressure on the market price of our common stock. Furthermore, it may be difficult for holders to resell their shares at prices they find attractive, or at all.

The market price of our common stock may be volatile and subject to fluctuations in response to numerous factors, including, but not limited to, the factors discussed in other risk factors and the following:

- actual or anticipated fluctuation in our operating results;
- changes in interest rates;
- changes in the legal or regulatory environment in which we operate;
- press releases, announcements or publicity relating to us or our competitors or relating to trends in our industry;
- changes in expectations as to our future financial performance, including financial estimates or recommendations by securities analysts and investors;
- future sales of our common stock;
- changes in economic conditions in our market, general conditions in the U.S. economy, financial markets or the banking industry; and
- other developments affecting our competitors or us.

These factors may adversely affect the trading price of our common stock, regardless of our actual operating performance, and could prevent a shareholder from selling common stock at or above the current market price. These factors may also adversely affect our ability to raise capital in the open market if needed. In addition, we cannot say with any certainty that a more active and liquid trading market for its common stock will develop.

Additional issuances of common stock or securities convertible into common stock may dilute holders of our common stock.

We may, in the future, determine that it is advisable, or we may encounter circumstances where it is determined that it is necessary, to issue additional shares of common stock, securities convertible into, exchangeable for or that represent an interest in common stock, or common stock-equivalent securities to fund strategic initiatives or other business needs or to build additional capital. Our board of directors is authorized to cause us to issue additional shares of common stock from time to time for adequate consideration without any additional action on the part of our shareholders in some cases. The market price of our common stock could decline as a result of other offerings, as well as other sales of a large block of common stock or the perception that such sales could occur.

Our ability to pay cash dividends on our securities is limited and we may be unable to pay future dividends.

We have not historically paid cash dividends on our common stock, and we may not declare or pay dividends on our securities, including our common stock, in the future. Any future determination relating to dividend policy will be made at the discretion of our board of directors and will depend on a number of factors, including our future earnings, capital requirements, financial condition, future prospects, regulatory restrictions, and other factors that our board of directors may deem relevant. The holders of our capital stock are entitled to receive dividends when, and if, declared by our board of directors out of funds legally available for that purpose. As part of our consideration of whether to pay cash dividends, we intend to retain adequate funds from future earnings to support the development and growth of our business. In addition, our ability to pay dividends is restricted by federal policies and regulations. It is the current policy of the Federal Reserve that bank holding companies should pay cash dividends on capital stock only out of net income available over the past year and only if prospective earnings retention is consistent with the organization's expected future needs and financial condition. Further, our principal source of funds to pay dividends is cash dividends that we receive from the Bank, which, in turn, will be highly dependent upon the Bank's historical and projected results of operations, liquidity, cash flows and financial condition, as well as various legal and regulatory prohibitions and other restrictions on the ability of the Bank to pay dividends, extend credit or otherwise transfer funds to us.

Our stock repurchase plan may not enhance long-term shareholder value and stock repurchases, if any, could increase the volatility of the price of our common stock and will diminish our cash reserves. Stock repurchases may be subject to regulatory approval in some cases.

In September 2019, our Board of Directors authorized a stock repurchase plan pursuant to which the Company may purchase up to 937,248 shares of its issued and outstanding common stock. The timing and actual number of shares repurchased depend on a variety of factors including the timing of open trading windows, price, corporate and regulatory requirements, available cash, and other market conditions. The plan may be suspended or discontinued at any time without prior notice. Repurchases pursuant to our stock repurchase plan could affect our stock price and increase its volatility. The existence of a stock repurchase plan could also cause our stock price to be higher than it would be in the absence of such a plan and could potentially reduce the market liquidity for our stock. Additionally, repurchases under our stock repurchase plan will diminish our cash reserves, which impacts our ability to pursue possible future strategic opportunities and acquisitions, support our operations, invest in securities and pay dividends and could result in lower overall returns on our cash balances. Stock repurchases may not enhance shareholder value because the market price of our common stock may decline below the levels at which we repurchased shares of stock, and short-term stock price fluctuations could reduce the program's effectiveness. In some cases, stock repurchases may be subject to regulatory approval. If required, we cannot guarantee that any such approval will be obtained in a timely manner, or at all.

Our stock price might fluctuate significantly, which could cause the value of your investment in our common stock to decline, and you might not be able to resell your shares at a price at or above the public offering price.

From January 1, 2017 to December 31, 2019, the price of our common stock, as reported by NASDAQ Global Market, has ranged from a low closing sale price of $9.71 on January 10, 2017, to a high closing sale price of $14.05 on July 9, 2018. In addition, securities markets worldwide have experienced, and are likely to continue to experience, significant price and volume fluctuations. This market volatility, as well as general economic, market or political conditions, could reduce the market price of our common stock regardless of our results of operations. Factors that impact the market for our stock include:

- our operating performance and the operating performance of similar companies;
- the overall performance of the equity markets;
- prevailing interest rates;
- economic, financial, geopolitical, regulatory or judicial events affecting us or the financial markets generally;
- the market for similar securities;
- announcements by us or our competitors of acquisitions, business plans, or commercial relationships;
- threatened or actual litigation;
- changes in the composition of our board of directors or management;
- publication of research reports or news stories about us, our competitors, or our industry, or positive or negative recommendations or withdrawal of research coverage by securities analysts;
- whether we declare dividends on our common stock from time to time;
- our creditworthiness;
- the ratings given to our securities by credit rating agencies, if any;
- large volumes of sales of our shares of common stock by existing shareholders; and
- general political and economic conditions.

In addition, the stock market in general, and the market for banks and financial services companies in particular, has experienced significant price and volume fluctuations that have often been unrelated or disproportionate to the operating performance of those companies. During the financial crisis of 2008–2009, financial institution stocks saw significant loss of value, with some stocks losing all their value due to the failure or bankruptcy of the issuer. Securities class action litigation has often been instituted against companies following periods of volatility in the overall market and in the market price of a company's securities. This litigation, if instituted against us, could result in substantial costs, divert our management's attention and resources, and harm our business, operating results, and financial condition.

We are subject to extensive regulation, and ownership of our common stock may have regulatory implications for holders thereof.

We are subject to extensive federal and state banking laws, including the Bank Holding Company Act of 1956, as amended (the "BHCA"), and federal and state banking regulations, that will impact the rights and obligations of owners of our common stock, including, for example, our ability to declare and pay dividends on our common stock. Shares of our common stock are voting securities for purposes of the BHCA and any bank holding company or foreign bank that is subject to the BHCA may need approval to acquire or retain more than 5% of the then-outstanding shares of our common stock, and any holder (or group of holders deemed to be acting in concert) may need regulatory approval to acquire or retain 10% or more of the shares of our common stock. A holder or group of holders may also be deemed to control us if they own 25% or more of our total equity. Under certain limited circumstances, a holder or group of holders acting in concert may exceed the 25% percent threshold and not be deemed to control us until they own 33% percent or more of our total equity. The amount of total equity owned by a holder or group of holders acting in concert is calculated by aggregating all shares held by the holder or group, whether as a combination of voting or non-voting shares or through other positions treated as equity for regulatory or accounting purposes and meeting certain other conditions. Holders of our common stock should consult their own counsel with regard to regulatory implications of acquiring shares of our common stock.

Holders should not expect us to redeem outstanding shares of our common stock.

Our common stock is a perpetual equity security. This means that it has no maturity or mandatory redemption date and will not be redeemable at the option of the holders. Any decision we may make at any time to propose the repurchase or redemption of shares of our common stock will depend upon, among other things, our evaluation of our capital position, the composition of our shareholders' equity, general market conditions at that time and other factors we deem relevant. Our ability to redeem shares of our common stock is subject to regulatory restrictions and limitations, including those of the Federal Reserve.

We may issue shares of preferred stock in the future, which could make it difficult for another company to acquire us or could otherwise adversely affect the rights of the holders of our common stock, which could depress the price of our common stock.

Our articles of incorporation authorize us to issue up to 5,000,000 shares of one or more series of preferred stock. Our board of directors, in its sole discretion, has the authority to determine the preferences, limitations and relative rights of shares of preferred stock and to fix the number of shares constituting any series, the designation of such series, and the dividend rate for each series, without any further vote or action by our shareholders. Our preferred stock may be issued with voting, liquidation, dividend and other rights superior to the rights of our common stock. The potential issuance of preferred stock may delay or prevent a change in control of us, discouraging bids for our common stock at a premium over the market price, and materially adversely affect the market price and the voting and other rights of the holders of our common stock.

Offerings of debt, which would rank senior to our common stock upon liquidation, may adversely affect the market price of our common stock.

We may attempt to increase our capital resources or, if regulatory capital ratios fall below the required minimums, we could be forced to raise additional capital by making additional offerings of debt or equity securities, senior or subordinated notes, preferred stock and common stock. Upon liquidation, holders of our debt securities and lenders with respect to other borrowings will receive distributions of available assets prior to the holders of our common stock.

Anti-takeover provisions could adversely affect our shareholders.

In some cases, shareholders would receive a premium for their shares if we were acquired by another company. However, state and federal law and our articles of incorporation and bylaws make it difficult for anyone to acquire us without approval of our board of directors. For example, our articles of incorporation require a supermajority vote of two-thirds of our outstanding common stock in order to effect a sale or merger of the Company in certain circumstances. Consequently, a takeover attempt may prove difficult, and shareholders may not realize the highest possible price for their securities.

An investment in our common stock is not an insured deposit and may lose value.

Shares of our common stock are not savings accounts, deposits or other obligations of any depository institution and are not insured or guaranteed by the FDIC or any other governmental agency or instrumentality, any other deposit insurance fund or by any other public or private entity. An investment in our common stock is inherently risky for the reasons described in this “Risk Factors” section. As a result, if you acquire shares of our common stock, you may lose some or all of your investment.

ITEM 1B – UNRESOLVED STAFF COMMENTS

None.

ITEM 2 - PROPERTIES

The following table sets forth the location of the main office, branch offices, and operation centers of the Registrant's subsidiary depository institution, Select Bank & Trust Company, as well as certain information relating to these offices.

Office Location	Year Opened	Approximate Square Footage	Owned or Leased
Select Bank & Trust Main Office 700 West Cumberland Street Dunn, NC 28334	2001	12,600	Owned
Blacksburg Office 203 W Cherokee Street Blacksburg, SC 29702	2017	2,898	Owned
Burlington Office 3158 South Church Street Burlington, NC 27217	2015	5,056	Owned
Charlotte Office 13024 Ballantyne Corporate Place Charlotte, NC 28277	2017	15,191	Leased
Clinton Office 111 Northeast Boulevard Clinton, NC 28328	2008	3,100	Owned
Elizabeth City Office 416 Hughes Boulevard Elizabeth City, NC 27909	2014	3,229	Owned
Fayetteville Office 2818 Raeford Road Fayetteville, NC 28303	2004	10,000	Owned
Goldsboro Office 431 North Spence Avenue Goldsboro, NC 27534	2005	6,300	Building Owned, Land Leased
Greenville Charles Blvd Office 3600 Charles Blvd. Greenville, NC 27858	2014	6,860	Owned
Holly Springs Office 5070 Kentworth Drive Holly Springs, NC 27540	2019	4,160	Leased
Leland Office 1101 New Pointe Boulevard Leland, NC 28451	2015	3,731	Owned
Lillington Office 818 McKinney Parkway Lillington, NC 27546	2007	4,500	Owned
Lumberton Office 4400 Fayetteville Road Lumberton, NC 28358	2006	3,500	Owned

Morehead City Office 168 N.C. 24 Morehead City, NC 28577	2015	3,731	Leased
Raleigh Office 4505 Falls of Neuse Road, Suite #100 Raleigh, NC 27609	2016	6,538	Leased
Rock Hill Office 201 Oakland Avenue Rock Hill, SC 29730	2017	2,030	Leased
Virginia Beach Office 651 Nevan Road Virginia Beach, VA 23451	2019	13,000	Building Owned, Land Leased
Wilmington Office 1001 Military Cutoff Road, Suite 100 Wilmington, NC 28405	2017	8,500	Leased
Operations Center 861 Tilghman Drive Dunn, NC 28335	2010	7,500	Owned
Operations Center - Annex 863 Tilghman Drive Dunn, NC 28335	2010	5,000	Owned

ITEM 3 – LEGAL PROCEEDINGS

In the ordinary course of operations, the Registrant and the Bank are at times involved in legal proceedings. In the opinion of management, as of December 31, 2019, there were no material pending legal proceedings to which the Registrant, or any of its subsidiaries, was a party, or of which any of their property was the subject.

ITEM 4 – MINE SAFETY DISCLOSURES

Not applicable.

PART II

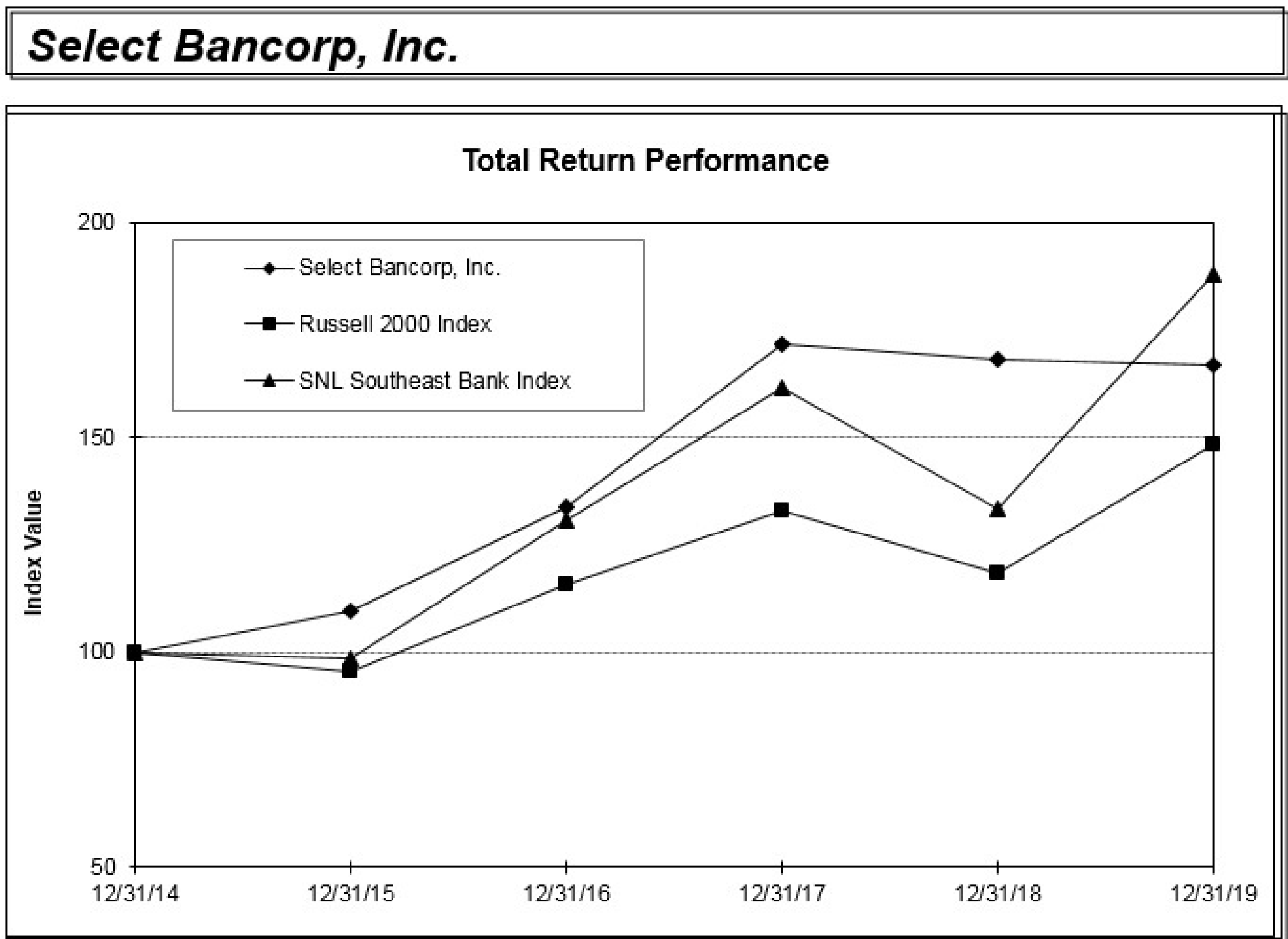
ITEM 5 - MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

The Registrant's common stock is quoted on the NASDAQ Global Market under the trading symbol "SLCT." At February 7, 2020, there were 18,330,058 shares of common stock issued and outstanding, which were held by 1,066 shareholders of record.

The Registrant did not declare or pay common stock cash dividends during 2019 and 2018, and it is not currently anticipated that cash dividends will be declared and paid to common shareholders at any time in the foreseeable future.

Securities Authorized for Issuance under Equity Compensation Plans

See Item 12 of this report for disclosure regarding securities authorized for issuance under equity compensation plans required by Item 201(d) of Regulation S-K.



Index	*Period Ending* 12/31/14	12/31/15	12/31/16	12/31/17	12/31/18	12/31/19
Select Bancorp, Inc.	100.00	109.77	133.65	171.51	167.98	166.89
Russell 2000 Index	100.00	95.59	115.95	132.94	118.30	148.49
SNL Southeast Bank Index	100.00	98.44	130.68	161.65	133.56	188.08

Source: S&P Global Market Intelligence
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Issuer Purchases of Equity Securities

The following table sets forth information regarding the Registrant's repurchases of its common stock. There were 194,853 shares repurchased during the fourth quarter of the fiscal year covered by this annual report.

Period	Total number of shares purchased	Average price paid per share	Total number of shares purchased as part of publicly announced plans or programs(2)	Maximum number of shares that may yet be purchased under the plans or programs(2)
October 2019 Beginning Date: 10/1 Ending Date: 10/31	--	$ --	--	705,359
November 2019 Beginning Date: 11/1 Ending Date: 11/30	175,707	11.79	175,707	529,652
December 2019 Beginning Date: 12/1 Ending Date: 12/31	19,146	12.03	194,853	510,506

(1) On September 17, 2019, the Registrant announced that its board of directors had authorized a repurchase plan under which the Registrant may repurchase up 937,248 shares of its common stock through open market purchases or privately negotiated transactions. The Registrant's purchase plan has no time limit.

ITEM 6 – SELECTED FINANCIAL DATA

	At or for the year ended December 31,				
	2019	2018	2017	2016	2015
	(dollars in thousands, except per share data)				
Operating Data:					
Total interest income	$ 58,446	$ 56,835	$ 39,617	$ 34,709	$ 33,341
Total interest expense	11,556	9,450	5,106	3,733	3,542
Net interest income	46,890	47,385	34,511	30,976	29,799
Provision (recovery) for loan losses	438	(156)	1,367	1,516	890
Net interest income after provision (recovery) for loan losses	46,452	47,541	33,144	29,460	28,909
Total non-interest income	5,419	4,701	3,072	3,222	3,292
Merger related expenses	406	1,826	2,166	-	378
Other non-interest expense	34,734	32,724	25,153	22,281	21,852
Income before income taxes	16,731	17,692	8,897	10,401	9,971
Provision for income taxes	3,696	3,910	5,712	3,647	3,418
Net Income	13,035	13,782	3,185	6,754	6,553
Dividends on Preferred Stock	-	-	-	4	77
Net income available to common Shareholders	$ 13,035	$ 13,782	$ 3,185	$ 6,750	$ 6,476
Per Share Data:					
Earnings per share - basic	$ 0.69	$ 0.87	$ 0.27	$ 0.58	$ 0.56
Earnings per share - diluted	0.68	0.87	0.27	0.58	0.56
Market Price					
High	12.48	14.05	12.70	10.48	8.47
Low	11.61	11.73	9.71	7.70	6.62
Close	12.30	12.38	12.64	9.85	8.09
Book value	11.61	10.85	9.72	8.95	8.38
Tangible book value (5)	10.18	9.47	7.72	8.29	7.67
Selected Year-End Balance Sheet Data:					
Loans, gross of allowance	$ 1,029,975	$ 986,040	$ 982,626	$ 677,195	$ 617,398
Allowance for loan losses	8,324	8,669	8,835	8,411	7,021
Other interest-earning assets	137,882	133,304	89,531	93,093	134,368
Goodwill	24,579	24,579	24,904	6,931	6,931
Core deposit intangible	1,610	2,085	3,101	810	1,241
Total assets	1,275,076	1,258,525	1,194,135	846,640	817,015
Deposits	992,838	980,427	995,044	679,661	651,161
Borrowings	57,372	64,372	47,651	60,129	58,376
Shareholders' equity	212,775	209,611	136,115	104,273	104,702
Selected Average Balances:					
Total assets	$ 1,268,728	$ 1,228,576	$ 898,943	$ 829,315	$ 765,274
Loans, gross of allowance	1,004,051	987,634	732,089	639,412	578,759
Total interest-earning assets	1,164,149	1,119,344	813,773	744,024	686,663
Goodwill	24,579	24,656	7,719	9,931	9,931
Core deposit intangible	1,812	2,547	640	1,020	1,330
Deposits	981,132	989,838	738,310	665,764	607,214
Total interest-bearing liabilities	1,041,918	1,060,588	787,073	723,111	659,676
Shareholders' equity	214,324	161,953	108,709	102,110	102,068
Selected Performance Ratios:					
Return on average assets	1.03%	1.12%	0.35%	0.81%	0.86%
Return on average equity	6.08%	8.51%	2.93%	6.61%	6.42%
Net interest margin (4)	4.04%	4.19%	4.14%	4.06%	4.34%
Net interest spread (4)	3.58%	3.98%	4.09%	4.04%	4.18%
Efficiency ratio(1)	66.40%	62.83%	72.69%	65.15%	67.18%
Asset Quality Ratios:					
Nonperforming loans to period-end loans (2)	1.18%	1.18%	0.71%	1.39%	1.41%
Allowance for loan losses to period-end loans (3)	0.81%	0.88%	0.90%	1.24%	1.14%
Net loan charge-offs (recoveries) to average loans	0.07%	0.00%	0.13%	0.02%	0.12%

	At or for the year ended December 31,				
	2019	2018	2017	2016	2015
	(dollars in thousands, except per share data)				
Capital Ratios:					
Total risk-based capital	18.26%	19.26%	11.86%	15.12%	16.01%
Tier 1 risk-based capital	17.52%	18.44%	11.04%	14.03%	15.04%
Common equity Tier 1 Capital	16.46%	17.30%	9.94%	12.48%	12.33%
Leverage ratio	15.84%	15.65%	12.64%	12.99%	13.81%
Tangible equity to assets	14.63%	14.54%	9.05%	11.40%	10.88%
Equity to assets ratio	16.69%	16.66%	11.40%	12.57%	13.68%
Additional Information:					
Loans, nonperforming [(2)]	$ 12,148	$ 11,635	$ 6,978	$ 9,430	$ 8,712
Interest income that would be recorded using original terms of nonperforming loans	838	737	251	410	446
Actual interest income recorded on restructured and nonperforming loans	520	451	308	217	164
Other Data:					
Number of banking offices	17	18	18	13	14
Number of full time equivalent employees	213	205	202	150	153

(1) Efficiency ratio is calculated as non-interest expenses divided by the sum of net interest income and non-interest income.
(2) Nonperforming loans consist of non-accrual loans and restructured loans.
(3) Allowance for loan losses to period-end loans ratio excludes loans held for sale.
(4) Fully taxable equivalent basis.
(5) Tangible book value per share (a non-GAAP financial measure) is equal to total shareholders' equity less goodwill, preferred stock and core deposit intangibles, divided by the number of outstanding shares of our common stock at the end of the relevant period. Please refer to the table below for a reconciliation of this non-GAAP financial measure.

Use of Non-GAAP Financial Measures

Tangible book value per share is a non-GAAP financial measure generally used by financial analysts, investment bankers, and other investors to evaluate financial institutions. For tangible book value per share, the most directly comparable financial measure calculated in accordance with GAAP is the Registrant's book value per common share. A reconciliation of tangible book value per share to book value per share is included below. The Registrant believes that this measure is important to many investors in the marketplace who are interested in changes from period to period in book value per common share exclusive of changes in intangible assets. Goodwill and other intangible assets have the effect of increasing total book value while not increasing the Company's tangible book value.

Any non-GAAP financial measures presented in this Report should not be considered in isolation or as a substitute for the most directly comparable or other financial measures calculated in accordance with GAAP. Moreover, the manner in which the Registrant calculates a non-GAAP financial measure may differ from that of other companies reporting measures with similar names. You should understand how such other banking organizations calculate their financial measures similar or with names similar to the non-GAAP financial measures that the Registrant has discussed or disclosed in this Report when comparing such non-GAAP financial measures.

Reconciliation of GAAP to Non-GAAP Measures
($ in thousands, except share and per share data)
(Unaudited)

	December 31, 2019	December 31, 2018	December 31, 2017	December 31, 2016	December 31, 2015
Tangible common equity					
Total shareholders' equity	$ 212,775	$ 209,611	$ 136,115	$ 104,273	$ 104,702
Adjustments:					
Goodwill	24,579	24,579	24,904	6,931	6,931
Core deposit intangibles	1,610	2,085	3,101	810	1,241
Tangible common equity	$ 186,586	$ 182,947	$ 108,110	$ 96,532	$ 96,530
Common shares outstanding(1)	18,330,058	19,311,505	14,009,137	11,645,413	11,583,011
Book value per common share(2)	$ 11.61	$ 10.85	$ 9.72	$ 8.95	$ 9.04
Tangible book value per common share(3)	$ 10.18	$ 9.47	$ 7.72	$ 8.29	$ 8.33

(1) Excludes the dilutive effect of common stock issuable upon exercise of outstanding stock options. The number of exercisable options outstanding was 121,660 as of December 31, 2019; 113,013 as of December 31, 2018; 63,927 as of December 31, 2017; 44,406 as of December 31, 2016 and 65,011 as of December 31, 2015.

(2) We calculate book value per common share as shareholders' equity less preferred stock at the end of the relevant period divided by the outstanding number of shares of our common stock at the end of the relevant period.

(3) We calculate tangible book value per common share as total shareholders' equity less goodwill, preferred stock and core deposit intangibles, divided by the number of outstanding shares of our common stock at the end of the relevant period.

ITEM 7 – MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following presents management's discussion and analysis of our financial condition and results of operations and should be read in conjunction with the financial statements and related notes contained elsewhere in this annual report. This discussion contains forward-looking statements that involve risks and uncertainties. Readers are directed to the "Note Regarding Forward-Looking Statements" that appears at the end of this discussion. The following discussion is intended to assist in understanding the financial condition and results of operations of Select Bancorp, Inc. Because Select Bancorp, Inc. has no material operations and conducts no business on its own other than owning its consolidated subsidiary, Select Bank & Trust Company, and its unconsolidated subsidiary, New Century Statutory Trust I, the discussion contained in this Management's Discussion and Analysis concerns primarily the business of the bank subsidiary. However, for ease of reading and because the financial statements are presented on a consolidated basis, Select Bancorp, Inc. and Select Bank & Trust are collectively referred to herein as the Company unless otherwise noted.

DESCRIPTION OF BUSINESS

The Company is a commercial bank holding company that was incorporated on May 14, 2003 and has one wholly owned banking subsidiary, Select Bank & Trust Company (referred to as the "Bank"), which became a subsidiary of the Company as part of a holding company reorganization. In September 2004, the Company formed New Century Statutory Trust I, which issued trust preferred securities to provide additional capital for general corporate purposes, including the expansion of the Bank. New Century Statutory Trust I is not a consolidated subsidiary of the Company. The Company's only business activity is the ownership of the Bank. Accordingly, this discussion focuses primarily on the financial condition and operating results of the Bank.

The Bank's lending activities are oriented to the consumer/retail customer as well as to the small-to-medium sized businesses located in the Bank's market areas. The Bank offers the standard complement of commercial, consumer, and mortgage lending products, as well as the ability to structure products to fit specialized needs. The deposit services offered by the Bank include small business and personal checking, savings accounts and certificates of deposit. The Bank concentrates on customer relationships in building its customer deposit base and competes aggressively in the area of transaction accounts. Readers are directed to "Part I – Item 1 – Business" of this annual report for a description of the Bank's market areas.

FINANCIAL CONDITION
DECEMBER 31, 2019 AND 2018

Overview

Total assets at December 31, 2019 were $1.3 billion, which represents an increase of $16.6 million or 1.3% from December 31, 2018. Interest earning assets at December 31, 2019 totaled $1.2 billion and consisted of $1.0 billion in net loans, $72.4 million in investment securities, and $60.0 million in overnight investments and interest-bearing deposits in other banks. Total deposits and shareholders' equity at December 31, 2019 were $992.8 million and $212.8 million, respectively.

On December 15, 2017 the Company acquired Premara Financial, Inc. (which we refer to herein as "Premara") through the merger of Premara with and into the Company. Immediately following the parent merger, Premara's wholly owned subsidiary, Carolina Premier Bank, was merged with and into the Bank. As a result of the mergers, the Company acquired a branch in Charlotte, North Carolina and branches in Rock Hill, Blacksburg and Six Mile, South Carolina. The Company also added additional assets of $278.8 million, net loans of $198.4 million and $226.3 million in deposits through the acquisition. On November 15, 2019, the Bank ceased operations at the Six Mile, South Carolina branch upon consummation of a purchase and assumption transaction pursuant to which another depository institution assumed the deposit liabilities and leasehold rights associated with the Six Mile location.

The Company now operates 18 full-service offices in three states, having opened a new Virginia Beach, Virginia branch and Holly Springs, North Carolina branch during the 2019 fiscal year. The Holly Springs branch is located in the Raleigh-Cary, NC Metropolitan Statistical Area, and the Virginia Beach branch is located in the Virginia Beach-Norfolk-Newport News, VA-NC Metropolitan Statistical Area.

Investment Securities

Investment securities increased to $72.4 million at December 31, 2019 from $51.5 million at December 31, 2018. The Company's investment portfolio at December 31, 2019, which consisted of U.S. government sponsored entities agency securities (GSE's), mortgage-backed securities, corporate bonds and bank-qualified municipal securities, aggregated $72.4 million with a weighted average taxable equivalent yield of 3.19%. The Company also holds an investment of $3.0 million in Federal Home Loan Bank Stock with a weighted average yield of 6.58%. The investment portfolio increased $20.9 million in 2019 as a result of $38.7 million in purchases which was offset by $3.4 million of maturities and $13.8 million of principal payments, sales of $1.1 million, as well as an increase in unrealized gains and losses of $1.2 million in the market value of securities available for sale and net accretion of investment discounts of $767,000.

The following table summarizes the securities portfolio by major classification as of December 31, 2019:

Securities Portfolio Composition
(dollars in thousands)

	Amortized Cost	Fair Value	Tax Equivalent Yield
U. S. government agency securities - GSE's:			
Due within one year	$ 122	$ 123	3.12%
Due after one but within five years	7,517	7,620	3.10%
Due after five but within ten years	1,855	1,909	4.25%
Due after ten years	345	344	3.49%
	9,839	9,996	3.32%
Mortgage-backed securities:			
Due within one year	4,455	4,449	2.30%
Due after one but within five years	33,217	33,802	2.68%
Due after five but within ten years	710	719	2.39%
Due after ten years	8,544	8,773	3.24%
	46,926	47,743	2.74%
Corporate bonds:			
Due within one year	276	280	8.61%
Due after one but within five years	-	-	-%
Due after five but within ten years	1,256	1,269	6.49%
Due after ten years	750	750	5.38%
	2,282	2,299	6.38%
State and local governments:			
Due within one year	4,048	4,062	4.75%
Due after one but within five years	220	220	4.99%
Due after five but within ten years	747	764	3.21%
Due after ten years	7,137	7,283	3.93%
	12,152	12,329	4.19%
Total securities available for sale:			
Due within one year	8,901	8,914	3.62%
Due after one but within five years	40,954	41,642	2.77%
Due after five but within ten years	4,568	4,661	4.41%
Due after ten years	16,776	17,150	3.63%
	$ 71,199	$ 72,367	3.19%

Loans Receivable

The loan portfolio at December 31, 2019 totaled $1.0 billion, which was a $43.9 million, or 4.5%, increase from December 31, 2018. At December 31, 2019, the portfolio was composed of $946.3 million in real estate loans, $75.7 million in commercial and industrial loans, and $10.0 million in loans to individuals. Also included in loans outstanding at December 31, 2019, was $2.1 million in net deferred loan fees.

The following table describes the Company's loan portfolio composition by category at the dates indicated:

	At December 31,									
	2019		2018		2017		2016		2015	
	Amount	% of Total Loans	Amount	% of Total Loans	Amount	% of Total Loans	Amount	% of Total Loans	Amount	% of Total Loans
	(dollars in thousands)									
Real estate loans:										
1-to-4 family residential	$ 151,697	14.7%	$159,597	16.2%	$156,901	16.0%	$ 97,978	14.5%	$ 87,955	14.2%
Commercial real estate	459,115	44.6%	457,611	46.4%	403,100	41.0%	281,723	41.6%	259,259	42.0%
Multi-family residential	69,124	6.7%	63,459	6.4%	76,983	7.8%	56,119	8.3%	40,738	6.6%
Construction	221,878	21.6%	170,404	17.3%	177,933	18.1%	100,911	14.9%	107,688	17.4%
Home equity lines of credit	44,514	4.3%	49,713	5.0%	52,606	5.3%	41,158	6.1%	42,002	6.8%
Total real estate loans	946,328	91.9%	900,784	91.3%	867,523	88.2%	577,889	85.4%	537,642	87.0%
Other loans:										
Commercial and industrial	75,748	7.4%	74,181	7.6%	106,164	10.8%	90,678	13.4%	73,491	11.9%
Loans to individuals & overdrafts	10,013	0.9%	12,814	1.3%	10,244	1.1%	9,827	1.4%	7,255	1.2%
Total other loans	85,761	8.3%	86,995	8.9%	116,408	11.9%	100,505	14.8%	80,746	13.1%
Less:										
Deferred loan origination (fees) cost, net	(2,114)	(0.2)%	(1,739)	(0.2)%	(1,305)	(0.1)%	(1,199)	(0.2)%	(990)	(0.1)%
Total loans	1,029,975	100.0%	986,040	100.0%	982,626	100.0%	677,195	100.0%	617,398	100.0%
Allowance for loan losses	(8,324)		(8,669)		(8,835)		(8,411)		(7,021)	
Total loans, net	$1,021,651		$977,371		$973,791		$668,784		$610,377	

As demonstrated by the above table, the majority of the Company's loan portfolio is comprised of real estate loans. This category, which includes both commercial and consumer loan balances, increased from 91.3% of the loan portfolio at December 31, 2018 to 91.9% at December 31, 2019. There was a $1.5 million increase in commercial real estate loans, a $7.9 million decrease in 1-to-4 family residential loans, a $5.2 million decrease in HELOC loans, a $51.5 million increase in construction loans, and a $5.7 million increase in multi-family residential loans. The increase in construction loans was the biggest factor in the year-over-year increase in total loans.

Management monitors trends in the loan portfolio that may indicate more than normal risk. A discussion of certain risk factors follows. Some loans or groups of loans may contain one or more of these individual loan risk factors. Therefore, an accumulation of the amounts or percentages of the individual loan risk factors may not necessarily be an indication of the cumulative risk in the total loan portfolio.

Acquisition, Development and Construction Loans

The Company originates construction loans for the purpose of acquisition, development, and construction ("ADC") of both residential and commercial properties.

Acquisition, Development and Construction Loans
As of December 31, 2019
(dollars in thousands)

	Construction	Land and Land Development	Total
Total ADC loans	$ 186,038	$ 35,840	$ 221,878
Average Loan Size	$ 331	$ 607	
Percentage of total loans	18.06%	3.48%	21.55%
Non-accrual loans	$ 181	$ -	$ 181

Management closely monitors the ADC portfolio as to collateral value, funding based on project completeness, and the performance of similar loans in the Company's market areas.

Included in ADC loans and residential real estate loans as of December 31, 2019 were certain loans that exceeded regulatory loan to value ("LTV") guidelines. As of that date, the Company had $27.7 million in non-1-to-4 family residential loans that exceeded the regulatory LTV limits and $10.0 million of 1-to-4 family residential loans that exceeded the regulatory LTV limits. The banking regulators recognize that it may be appropriate in individual cases to originate or purchase loans with LTV ratios in excess of regulatory limits based on the support provided by other credit factors. The Bank has established a review and approval procedure for such loans. Under applicable guidance, the total amount of all loans in excess of regulatory LTV limits should not exceed 100% of total capital. The total amount of these loans represented 23.2% of total risk-based capital as of December 31, 2019, which is less than the 100% maximum specified in regulatory guidance. These loans may present more than ordinary risk to the Company if the real estate market softens for both market activity and collateral valuations. Similar information with respect to the Company's ADC portfolio at December 31, 2018 is set forth below:

Acquisition, Development and Construction Loans
As of December 31, 2018
(dollars in thousands)

	Construction	Land and Land Development	Total
Total ADC loans	$ 145,736	$ 24,668	$ 170,404
Average Loan Size	$ 267	$ 308	
Percentage of total loans	14.78%	2.50%	17.28%
Non-accrual loans	$ 587	$ -	$ 587

Included in ADC loans and residential real estate loans as of December 31, 2018 were certain loans that exceeded regulatory loan to value ("LTV") guidelines. As of that date, the Company had $27.7 million in non-1-to-4 family residential loans that exceeded the regulatory LTV limits and $10.0 million of 1-to-4 family residential loans that exceeded the regulatory LTV limits. The total amount of these loans represented 23.2% of total risk-based capital as of December 31, 2018, which is less than the 100% maximum specified in regulatory guidance.

Business Sector Concentrations

Loan concentrations in certain business sectors impacted by lower than normal retail sales, higher unemployment, higher vacancy rates, and weakened real estate market values may also pose additional risk to the Company's capital position. The Company has established an internal commercial real estate guideline of 40% of Risk-Based Capital for any single product type.

At December 31, 2019, the Company had three product types exceeded the 40% guideline. The following product types were in excess of the 40% guidelines; apartments, commercial construction and office buildings. All other commercial and residential real estate product types were under the 40% threshold.

At December 31, 2018, the Company did not exceed the 40% guideline in any product types. All commercial and residential real estate product types were under the 40% threshold.

Geographic Concentrations

Certain risks exist arising from the geographic location of specific types of higher than normal risk real estate loans. Below is a table showing geographic concentrations for ADC and home equity lines of credit ("HELOC") loans at December 31, 2019. Except as otherwise noted, the counties identified in the following table are located in North Carolina.

	ADC Loans	Percent	HELOC	Percent
	(dollars in thousands)			
Harnett County	$ 9,637	4.34%	$ 5,156	11.58%
Alamance County	845	0.38%	1,072	2.41%
Brunswick County	15,456	6.97%	1,629	3.67%
Carteret County	5,352	2.41%	2,190	4.92%
Cherokee County (SC)	-	-%	22	0.05%
Cumberland County	24,601	11.09%	2,285	5.13%
Mecklenburg County	18,142	8.18%	2,689	6.04%
New Hanover County	40,518	18.26%	2,885	6.48%
Pasquotank County	1,997	0.90%	1,693	3.80%
Pitt County	16,098	7.25%	5,442	12.23%
Robeson County	1,165	0.53%	2,939	6.60%
Sampson County	23	0.01%	1,743	3.92%
Virginia Beach County (VA)	142	0.06%	99	0.22%
Wake County	23,407	10.56%	1,640	3.68%
Wayne County	1,572	0.71%	3,183	7.15%
Wilson County	477	0.21%	72	0.16%
York County (SC)	1,931	0.87%	1,123	2.52%
All other locations	60,515	27.27%	8,652	19.44%
Total	$ 221,878	100.00%	$ 44,514	100.00%

For comparative purposes, below is a table showing geographic concentrations for ADC and HELOC loans at December 31, 2018.

	ADC Loans	Percent	HELOC	Percent
	(dollars in thousands)			
Harnett County	$ 5,389	3.16%	$ 5,367	10.80%
Alamance County	740	0.43%	1,350	2.72%
Beaufort County	908	0.53%	1,113	2.24%
Brunswick County	8,440	4.95%	1,492	3.00%
Carteret County	1,544	0.91%	2,676	5.38%
Craven County	1,060	0.62%	319	0.64%
Cherokee County (SC)	-	-%	52	0.11%
Cumberland County	21,019	12.34%	3,116	6.27%
Mecklenburg County	24,853	14.59%	3,635	7.31%
New Hanover County	23,396	13.73%	2,721	5.47%
Pasquotank County	1,145	0.67%	1,915	3.85%
Pickens County (SC)	-	-%	99	0.20%
Pitt County	10,574	6.21%	6,334	12.74%
Robeson County	1,076	0.63%	3,505	7.05%
Sampson County	149	0.09%	1,835	3.69%
Wake County	18,528	10.87%	1,744	3.51%
Wayne County	2,212	1.30%	3,457	6.95%
Wilson County	392	0.23%	73	0.15%
York County (SC)	124	0.07%	1,053	2.12%
All other locations	48,855	28.67%	7,857	15.80%
Total	$ 170,404	100.00%	$ 49,713	100.00%

Interest Only Payments

Another risk factor that exists in the total loan portfolio pertains to loans with interest only payment terms. At December 31, 2019, the Company had $249.9 million in loans that had terms permitting interest only payments. This represented 24.26% of the total loan portfolio. At December 31, 2018, the Company had $224.6 million in loans that had terms permitting interest only payments. This represented 22.77% of the total loan portfolio. In light of the risk inherent with interest only loans, it is customary and general industry practice that loans in the ADC portfolio are interest only payments during the acquisition, development, and construction phases of such projects but then convert to amortizing term loans with scheduled payments of principal and interest.

Large Dollar Concentrations

Concentrations of high dollar loans or large customer relationships may pose additional risk in the total loan portfolio. The Company’s ten largest loans or lines of credit concentrations totaled $82.0 million or 8.0% of total loans at December 31, 2019 compared to $70.6 million or 7.2% of total loans at December 31, 2018. The Company’s ten largest customer loan relationship concentrations totaled $129.5 million, or 12.6% of total loans, at December 31, 2019 compared to $106.8 million, or 10.8% of total loans at December 31, 2018. Deterioration or loss in any one or more of these high dollar loan or customer concentrations could have a material adverse impact on the capital position of the Company and on our results of operations.

Maturities and Sensitivities of Loans to Interest Rates

The following table presents the maturity distribution of the Company’s loans at December 31, 2019. The table also presents the portion of loans that have fixed interest rates or variable interest rates that fluctuate over the life of the loans in accordance with changes in an interest rate index such as the prime rate:

	At December 31, 2019			
	Due within one year	Due after one year but within five years	Due after five years	Total
	(dollars in thousands)			
Fixed rate loans:				
1-to-4 family residential	$ 6,928	$ 101,081	$ 26,325	$ 134,334
Commercial real estate	47,883	277,798	85,652	411,333
Multi-family residential	3,897	43,331	12,125	59,353
Construction	10,751	78,633	12,600	101,984
Home equity lines of credit	30	1,628	50	1,708
Commercial and industrial	7,048	34,531	8,905	50,484
Loans to individuals & overdrafts	1,451	4,273	665	6,389
Total at fixed rates	77,988	541,275	146,322	765,585
Variable rate loans:				
1-to-4 family residential	1,821	4,242	10,795	16,858
Commercial real estate	12,538	21,875	11,536	45,949
Multi-family residential	2,710	5,234	1,827	9,771
Construction	87,815	19,626	12,272	119,713
Home equity lines of credit	1,812	17,703	22,848	42,363
Commercial and industrial	15,006	4,943	2,492	22,441
Loans to individuals & overdrafts	1,625	1,383	460	3,469
Total at variable rates	123,327	75,006	62,230	260,563
Subtotal	201,315	616,281	208,552	1,026,148
Non-accrual loans	2,855	2,076	1,010	5,941
Gross loans	$ 204,170	$ 618,357	$ 209,562	$ 1,032,089
Deferred loan origination (fees) costs, net				(2,114)
Total loans				$ 1,029,975

The Company may renew loans at maturity when requested by a customer whose financial strength appears to support such renewal or when such renewal appears to be in the Company’s best interest. In such instances, the Company generally requires payment of accrued interest and may require a principal reduction or modify other terms of the loan at the time of renewal.

Past Due Loans and Nonperforming Assets

At December 31, 2019, the Company had $4.7 million in loans that were 30 days or more past due. This represented 0.34% of gross loans outstanding on that date. This is a decrease from December 31, 2018 when there were $5.1 million in loans that were past due 30 days or more, or 0.51% of gross loans outstanding. Non-accrual loans decreased to $5.9 million at December 31, 2019 from $7.3 million at December 31, 2018. As of December 31, 2019, the Company had forty-two loans totaling $9.4 million that were considered to be troubled debt restructurings, of which twenty-eight loans totaling $6.2 million were still accruing interest. As of December 31, 2018, the Company had thirty-six loans totaling $6.9 million that were considered to be troubled debt restructurings, of which twenty loans totaling $4.4 million were still accruing interest. There were six loans in the aggregate amount of $1.2 million greater than 90 days past due and still accruing interest at December 31, 2019, and there were eleven loans in the amount of $3.2 million greater than 90 days past due and still accruing interest at December 31, 2018. Tables included in **Note E** of the Notes to Consolidated Financial Statements included under Item 8 of this report present an age analysis of past due loans, including acquired credit-impaired loans, or PCI Loans, segregated by class of loans as of December 31, 2019.

The table below sets forth, for the periods indicated, information about the Company's non-accrual loans, loans past due 90 days or more and still accruing interest, total non-performing loans (non-accrual loans plus restructured loans), and total non-performing assets.

	As December 31,				
	2019	2018	2017	2016	2015
			(dollars in thousands)		
Non-accrual loans	$ 5,941	$ 7,257	$ 2,115	$ 5,805	$ 6,635
Restructured loans	6,207	4,378	4,863	3,625	2,077
Total non-performing loans	12,148	11,635	6,978	9,430	8,712
Foreclosed real estate	3,533	1,088	1,258	599	1,401
Total non-performing assets	$ 15,681	$ 12,723	$ 8,236	$ 10,029	$ 10,113
Accruing loans past due 90 days or more	$ 1,231	$ 3,167	$ 1,476	$ 529	$ 142
Allowance for loan losses	$ 8,324	$ 8,669	$ 8,835	$ 8,411	$ 7,021
Non-performing loans to period end loans	1.18%	1.18%	0.71%	1.39%	1.41%
Non-performing loans and accruing loans past due 90 days or more to period end loans	1.30%	1.50%	0.86%	1.47%	1.43%
Allowance for loan losses to period end loans	0.81%	0.88%	0.90%	1.24%	1.14%
Allowance for loan losses to non-performing loans	69%	75%	127%	89%	81%
Allowance for loan losses to non-performing assets	53%	68%	107%	84%	69%
Allowance for loan losses to non-performing assets and accruing loans past due 90 days or more	49%	55%	91%	80%	68%
Non-performing assets to total assets	1.23%	1.01%	0.69%	1.18%	1.24%
Non-performing assets and accruing loans past due 90 days or more to total assets	1.33%	1.26%	0.81%	1.25%	1.26%

In addition to the above, at December 31, 2019 the Company had $6.2 million in loans that were considered to be impaired for reasons other than their past due, accrual or restructured status. In total, there were $11.2 million in loans that were considered to be impaired at December 31, 2019, which is a $500,000 decrease from the $11.7 million that was impaired at December 31, 2018. Impaired loans have been evaluated by management in accordance with Accounting Standards Codification ("ASC") 310 and $413,000 has been included in the allowance for loan losses as of December 31, 2019 for these loans. All troubled debt restructurings and other non-performing loans are included within impaired loans as of December 31, 2019.

Allowance for Loan Losses

The allowance for loan losses is a reserve established through provisions for loan losses charged to expense and represents management's best estimate of probable loan losses that will be incurred within the existing portfolio of loans. The allowance, in the judgment of management, is necessary to reserve for estimated losses and risk inherent in the loan portfolio. The Company's allowance for loan loss methodology is based on historical loss experience by type of credit and internal risk grade, specific homogeneous risk pools and specific loss allocations, with adjustments for current events and conditions. The Company's process for determining the appropriate level of reserves is designed to account for changes in credit quality as they occur. The provision for loan losses reflects loan quality trends, including the levels of and trends related to past due loans and economic conditions at the local and national levels. It also considers the quality and risk characteristics of the Company's loan origination and servicing policies and practices. Individual reserves are calculated according to ASC 310-10-35 against loans evaluated individually and deemed to most likely be impaired. Impaired loans include all loans in non-accrual status, all troubled debt restructures, all substandard loans that are deemed to be collateral dependent, and other loans that management determines require reserves.

The following table presents the Company's allowance for loan losses by loan type as well as each loan type as a percentage of total loans at December 31 for the years indicated.

	At December 31,									
	2019	% of Total loans	2018	% of Total loans	2017	% of Total loans	2016	% of Total loans	2015	% of Total loans
	(dollars in thousands)									
1-to-4 family residential	$ 1,493	14.73%	$ 1,667	16.19%	$ 1,058	11.98%	$ 846	10.05%	$ 605	14.25%
Commercial real estate	2,851	44.58%	3,409	46.41%	3,370	38.15%	3,448	41.12%	3,005	41.99%
Multi-family residential	434	6.71%	471	6.44%	791	8.95%	628	7.48%	393	6.60%
Construction	1,737	21.55%	1,385	17.28%	1,955	22.13%	1,301	15.47%	1,386	17.44%
Home equity lines of credit	329	4.32%	555	5.04%	549	6.21%	623	7.42%	573	6.80%
Commercial and industrial	1,305	7.35%	976	7.52%	807	9.13%	1,248	14.84%	922	11.90%
Loans to individuals & overdrafts	175	0.97%	206	1.30%	305	3.60%	317	3.76%	137	1.18%
Deferred loan origination (fees) cost, net	-	(0.21)%	-	(0.18)%	-	(0.15)%	-	(0.14)%	-	(0.16)%
Total	$ 8,324		$ 8,669		$ 8,835		$ 8,411		$ 7,021	

The allowance for loan losses as a percentage of gross loans outstanding decreased by 0.07% during 2019 to 0.81% of gross loans at December 31, 2019. The change in the allowance during 2019 resulted from net charge-offs of $783,000 and a provision of $438,000. Loan loss reserves totaled $8.3 million or 0.81% of gross loans outstanding as of December 31, 2019, as compared to year-end 2018 when they totaled $8.7 million or 0.88% of loans outstanding. At December 31, 2019, specific reserves on impaired loans constituted $413,000 or 0.04% of gross loans outstanding compared to $87,000 or 0.03% of loans outstanding as of December 31, 2018. The loans that were acquired in our 2017 acquisition of Premara are included in the gross loan number used in the calculations above. The acquired loans are accounted for under ASC 310-20 and ASC 310-30 which results in initial credit marks for the inherent loss risk for those loans being established as part of the initial fair value mark and is not included in the allowance for loan losses. Total acquired loans represented $190.1 million of the gross loan total at December 31, 2018 of which $19.3 million were purchased credit impaired loans compared to total acquired loans representing $129.6 million of the gross loan total at December 31, 2019 of which $15.4 million were purchased credit impaired loans.

The following table presents information regarding changes in the allowance for loan losses in detail for the years indicated:

	As of December 31,				
	2019	2018	2017	2016	2015
	(dollars in thousands)				
Allowance for loan losses at beginning of year	$ 8,669	$ 8,835	$ 8,411	$ 7,021	$ 6,844
Provision (recovery) for loan losses	438	(156)	1,367	1,516	890
	9,107	8,679	9,778	8,537	7,734
Loans charged off:					
Commercial and industrial	(790)	(196)	(73)	(182)	(141)
Construction	-	-	(17)	(2)	(79)
Commercial real estate	(10)	(2)	(914)	(189)	(663)
Multi-family residential	-	-	-	-	(5)
Home equity lines of credit	(150)	(68)	(179)	(205)	(115)
1-to-4 family residential	-	(12)	(22)	(7)	(70)
Loans to individuals& overdrafts	(206)	(191)	(101)	(90)	(54)
Total charge-offs	(1,156)	(469)	(1,306)	(675)	(1,127)
Recoveries of loans previously charged off:					
Commercial and industrial	12	239	211	22	48
Construction	18	6	29	22	29
Multi-family residential	-	-	2	-	106
Commercial real estate	194	48	16	151	84
Home equity lines of credit	93	43	25	35	21
1-to-4 family residential	33	32	46	299	102
Loans to individuals& overdrafts	23	91	34	20	24
Total recoveries	373	459	363	549	414
Net recoveries (charge-offs)	(783)	(10)	(943)	(126)	(713)
Allowance for loan losses at end of year	$ 8,324	$ 8,669	$ 8,835	$ 8,411	$ 7,021
Ratios:					
Net charge-offs (recoveries) as a percent of average loans	0.07%	0.00%	0.13%	0.02%	0.12%
Allowance for loan losses as a percent of loans at end of year	0.81%	0.88%	0.90%	1.24%	1.14%

While the Company believes that it uses the best information available to establish the allowance for loan losses, future adjustments to the allowance may be necessary and results of operations could be adversely affected if circumstances differ substantially from the assumptions used in making determinations regarding the allowance.

The table below presents information detailing the allowance for loan losses for originated and purchased credit impaired acquired loans:

Analysis of Allowance for Credit Losses
(dollars in thousands)

	Beginning Balance	Charge Offs	Recoveries	Provision	Ending Balance
Year ended December 31, 2019					
Total loans					
Commercial and Industrial	$ 976	$ (790)	$ 12	$ 1,107	$ 1,305
Construction	1,385	-	18	334	1,737
Commercial real estate	3,409	(10)	194	(742)	2,851
Multi-family residential	471	-	-	(37)	434
Home Equity Lines of credit	555	(150)	93	(169)	329
1-to-4 family residential	1,667	-	33	(207)	1,493
Loans to individuals & overdrafts	206	(206)	23	152	175
Total	$ 8,669	$ (1,156)	$ 373	$ 438	$ 8,324
PCI loans					
Commercial and Industrial	$ 214	$ -	$ -	$ (36)	$ 178
Construction	-	-	-	6	6
Commercial real estate	385	-	-	(371)	14
Multi-family residential	-	-	-	15	15
Home Equity Lines of credit	-	-	-	-	-
1-to-4 family residential	4	-	-	52	56
Loans to individuals & overdrafts	-	-	-	-	-
Total	$ 603	$ -	$ -	$ (334)	$ 269
Loans – excluding PCI					
Commercial and Industrial	$ 762	$ (790)	$ 12	$ 1,143	$ 1,127
Construction	1,385	-	18	328	1,731
Commercial real estate	3,024	(10)	194	(371)	2,837
Multi-family residential	471	-	-	(52)	419
Home Equity Lines of credit	555	(150)	93	(169)	329
1-to-4 family residential	1,663	-	33	(259)	1,437
Loans to individuals & overdrafts	206	(206)	23	152	175
Total	$ 8,066	$ (1,156)	$ 373	$ 772	$ 8,055

Determining the fair value of PCI loans at acquisition required the Company to estimate cash flows expected to result from those loans and to discount those cash flows at appropriate rates of interest. For such loans, the excess of cash flows expected to be collected at acquisition over the estimated fair value is recognized as interest income over the remaining lives of the loans and is called the accretable yield. The difference between contractually required payments at acquisition and the cash flows expected to be collected at acquisition reflects the impact of estimated credit losses and is called the nonaccretable difference. In accordance with GAAP, there was no carry-over of previously established allowance for credit losses from the acquired company.

Management believes the level of the allowance for loan losses as of December 31, 2019 is appropriate in light of the risk inherent within the Company's loan portfolio.

Other Assets

At December 31, 2019, non-earning assets totaled $78.0 million, an increase of $4.4 million from $73.6 million at December 31, 2018. Non-earning assets at December 31, 2019 consisted of: cash and due from banks of $19.1 million, premises and equipment totaling $17.8 million, foreclosed real estate totaling $3.5 million, accrued interest receivable of $4.2 million, goodwill of $24.6 million and other assets totaling $8.8 million, including net deferred taxes of $2.8 million.

The Company had an investment in bank owned life insurance of $29.8 million at December 31, 2019, as compared to $29.1 million at December 31, 2018. The increase in BOLI in 2019 was from earnings of $672,000. Since the income on this investment is included in non-interest income, the asset is not included in the Company's calculation of earning assets.

Deposits

Total deposits at December 31, 2019 were $992.8 million and consisted of $240.3 million in non-interest-bearing demand deposits, $280.1 million in money market and NOW accounts, $43.1 million in savings accounts, and $429.3 million in time deposits. Total deposits increased by $12.4 million from $980.4 million as of December 31, 2018. Non-interest-bearing demand deposits decreased by $6.7 million from $247.0 million as of December 31, 2018. Money market deposit accounts and NOW accounts increased by $25.7 million from $254.5 million as of December 31, 2018. Savings accounts decreased by $8.7 million from $51.8 million as of December 31, 2018. Time deposits increased by $2.1 million during 2019. The increase in deposits during 2019 was due to the acquisition of the Virginia Beach Branch.

The following table shows historical information regarding the average balances outstanding and average interest rates for each major category of deposits:

	For the Period Ended December 31,									
	2019		2018		2017		2016		2015	
	Average Amount	Average Rate	Average Amount	Average Rate	Average Amount	Average Rate	Average Amount	Average Rate	Average Amount	Average Rate
	(dollars in thousands)									
Savings, NOW and money market deposits	$ 319,930	0.51%	$ 315,849	0.42%	$ 220,249	0.25%	$ 209,769	0.19%	$ 205,792	0.19%
Time deposits >$100,000	299,451	2.04%	321,387	1.50%	258,141	1.09%	204,120	0.82%	158,704	0.85%
Other time deposits	115,025	1.70%	115,603	1.28%	94,420	1.03%	91,573	1.08%	104,388	1.19%
Total interest-bearing deposits	734,406	1.32%	752,839	1.01%	572,810	0.76%	505,462	0.60%	468,884	0.64%
Noninterest-bearing deposits	246,726	-	236,999	-	173,608	-	160,302	-	138,330	-
Total deposits	$ 981,132	0.99%	$ 989,838	0.77%	$ 746,418	0.58%	$ 665,764	0.46%	$ 607,214	0.49%

The acquisition of Premara in December 2017 was the primary driver in the increase in average deposits in 2018 versus 2017.

Short-Term and Long-Term Debt

As of December 31, 2019, the Company had $57.4 million of debt, of which $45.0 million is long-term debt in the form of FHLB advances, plus $12.4 million in junior subordinated debentures issued to New Century Statutory Trust I in connection with the Company's 2004 issuance of trust preferred securities.

Shareholders' Equity

Total shareholders' equity at December 31, 2019 was $212.8 million, an increase of $3.2 million from $209.6 million as of December 31, 2018. Changes in shareholders' equity included $13.0 million in net income, $369,000 in stock-based compensation, proceeds of $228,000 from stock option exercises, other comprehensive income of $959,000 related to the increase in the unrealized gain in the Company's available for sale investment security portfolio offset by $11.4 million of common stock repurchases. During 2018, the Company completed a follow-on public offering which resulted in net proceeds of approximately $59.8 million. Our share repurchase program remains active, and we are able to return capital to shareholders by buying our shares when market conditions warrant. We intend to retain adequate capital for any acquisitions which meet our criteria.

RESULTS OF OPERATIONS
FOR THE YEARS ENDED DECEMBER 31, 2019 AND 2018

Overview

During 2019, the Company had net income of $13.0 million compared to net income of $13.8 million for 2018. Basic and diluted net income per share for the year ended December 31, 2019 were $0.69 and $0.68, respectively compared with basic and diluted net income per share of $0.87 for 2018.

Embedded in the Company's net income numbers for the year ended December 31, 2019, are net after tax integration expenses of $316,000, related to the acquisition of the Virginia Beach branch, the sale of the Six Mile branch and consolidation of the Washington branch. Embedded in the Company's net income numbers for the year ended December 31, 2018, are net after tax merger expenses of $1.4 million, related to the acquisition of Carolina Premier Bank.

Net Interest Income

Like most financial institutions, the primary component of earnings for the Company is net interest income. Net interest income is the difference between interest income, principally from loans and investment securities portfolios, and interest expense, principally on customer deposits and borrowings. Changes in net interest income result from changes in volume, spread and margin. For this purpose, volume refers to the average dollar level of interest-earning assets and interest-bearing liabilities, spread refers to the difference between the average yield on interest-earning assets and the average cost of interest-bearing liabilities, and margin refers to net interest income divided by the average interest-earning assets. Margin is influenced by the level and relative mix of interest-earning assets and interest-bearing liabilities, as well as by the levels of non-interest bearing liabilities and capital.

Net interest income decreased by $495,000 to $46.9 million for the year ended December 31, 2019. The Company’s total interest income was impacted by an increase in interest earning assets and a reducing interest rate environment in 2019. Average total interest-earning assets were $1.2 billion in 2019 compared with $1.1 billion in 2018. The yield on those assets increased by 1 basis point from 5.02% in 2018 to 5.03% in 2019. Factors impacting yield during 2019 were increasing investment yields of 5 basis points, decreasing loan yields of 1 basis points and increased yield on other interest earning assets of 37 basis points. Meanwhile, average interest-bearing liabilities decreased by $28.4 million from $823.6 million for the year ended December 31, 2018 to $795.2 million for the year ended December 31, 2019. Cost of these funds increased by 30 basis points in 2019 to 1.45% from 1.15% in 2018, which was primarily due to an increase of 42 basis points on larger time deposits which was offset by an increase of 52 basis points on borrowings. In 2019, the Company’s net interest margin was 4.04% and net interest spread was 3.58%. In 2018, net interest margin was 4.19% and net interest spread was 3.88%.

Provision for Loan Losses

The allowance for loan losses is a reserve established through provisions for loan losses charged to income and represents management’s best estimate of probable loan losses that have been incurred within the existing portfolio of loans. The allowance, in the judgment of management, is necessary to reserve for estimated losses and risk inherent in the loan portfolio. The Company’s allowance for loan loss methodology is based on historical loss experience by type of credit and internal risk grade, specific homogeneous risk pools and specific loss allocations, with adjustments for current events and conditions. The Company’s process for determining the appropriate level of reserves is designed to account for changes in credit quality as they occur. The provision for loan losses reflects loan quality trends, including the levels of and trends related to past due loans and economic conditions at the local and national levels. It also considers the quality and risk characteristics of the Company’s loan origination and servicing policies and practices.

The Company recorded a $438,000 provision for loan losses in 2019 compared to a reverse provision of $156,000 recorded in 2018. The increase in provision was due to improving regulatory concentration levels and was offset by loan growth. For more information on changes in the allowance for loan losses, refer to ***Note E*** of the notes to the consolidated financial statements in the section titled ***Allowance for Loan Losses***.

Non-Interest Income

Non-interest income for the year ended December 31, 2019 was $5.4 million, an increase of $718,000 from $4.7 million for the comparative 2018 period. Contributing to the increase was an increase in deposit service charges of $37,000 due to a higher number of deposits accounts from the growth of deposit accounts, an increase in fees on sale of mortgages of $256,000 from our mortgage department that was launched in 2018, a $48,000 gain on the sale of securities and an increase in other non-interest income of $377,000 primarily due to an increased number of debit cards.

Non-Interest Expenses

Non-interest expenses increased by $590,000 or 1.7% to $35.1 million for the year ended December 31, 2019, from $34.6 million for the same period in 2018. The following are highlights of the significant changes in non-interest expenses from 2018 to 2019.

- Personnel expenses increased $2.0 million to $20.3 million, due to net additions in branch staff, employment taxes and benefit costs.
- Occupancy and equipment expenses increased by $29,000 due to branch acquisition and start-up which is offset by a reduction of repairs and maintenance expenses.
- Core Deposit Intangible (“CDI”) amortization expense decreased by $191,000 in 2019 due to normal amortization.
- Deposit insurance expense decreased $441,000 due to receiving a credit from the FDIC as a result of regulatory changes in the premium calculation.
- Information systems expense increased $120,000 due primarily to additional software and security costs.
- Merger/integration related expenses decreased by $1.4 million compared to the non-recurring 2018 merger cost associated with the Premara acquisition.
- Foreclosed real estate expenses increased $25,000 due to increased property taxes and write downs in 2019.
- Professional fees increased $492,000 due to costs associated with branch closures, branch opening, internal audit fees, repurchase plan and various other consultants.
- Other non-interest expenses increased by $5,000, due to small increases in several categories of other non-interest expenses.

Provision for Income Taxes

The Company’s effective tax rate in 2019 was 22.1%, compared to 22.1% in 2018. Included in the effective tax rates for 2019 and 2018 is the effect of the tax law legislation change enacted December 22, 2017. For further discussion pertaining to the Company’s tax position, refer to **Note L** of the consolidated financial statements.

RESULTS OF OPERATIONS
FOR THE YEARS ENDED DECEMBER 31, 2018 AND 2017

Overview

During 2018, the Company had net income of $13.8 million compared to net income of $3.2 million for 2017. Both basic and diluted net income per share for the year ended December 31, 2018 were $0.87, compared with basic and diluted net income per share of $0.27 for 2017.

Embedded in the Company's net income numbers for the year ended December 31, 2018, are net after tax merger expenses of $1.4 million, related to the acquisition of Carolina Premier. During 2017, due to the Tax Act that was signed into law on December 22, 2017, the Company was required to calculate a "tax re-measurement" for the associated rate change for its deferred taxes. This tax re-calculation resulted in an increase of approximately $2.6 million of income tax expense for the year, which directly impacted the Company's reported GAAP results for 2017.

Net Interest Income

Like most financial institutions, the primary component of earnings for the Company is net interest income. Net interest income is the difference between interest income, principally from loans and investment securities portfolios, and interest expense, principally on customer deposits and borrowings. Changes in net interest income result from changes in volume, spread and margin. For this purpose, volume refers to the average dollar level of interest-earning assets and interest-bearing liabilities, spread refers to the difference between the average yield on interest-earning assets and the average cost of interest-bearing liabilities, and margin refers to net interest income divided by the average interest-earning assets. Margin is influenced by the level and relative mix of interest-earning assets and interest-bearing liabilities, as well as by the levels of non-interest bearing liabilities and capital.

Net interest income increased by $12.9 million to $47.4 million for the year ended December 31, 2018. The Company’s total interest income was impacted by an increase in interest earning assets and a rising interest rate environment in 2018. Average total interest-earning assets were $1.1 billion in 2018 compared with $835.6 million in 2017. The yield on those assets increased by 25 basis points from 4.77% in 2017 to 5.02% in 2018 because of increasing investment yields of 11 basis points, increasing loan yields of 33 basis points and increased yield on other interest earning assets of 55 basis points. Meanwhile, average interest-bearing liabilities increased by $200.1 million from $622.7 million for the year ended December 31, 2017 to $823.6 million for the year ended December 31, 2018. Cost of these funds increased by 33 basis points in 2018 to 1.15% from 0.82% in 2017, which was primarily due to an increase of 25 basis points on larger time deposits and 101 basis points on borrowings. In 2018, the Company’s net interest margin was 4.19% and net interest spread was 3.98%. In 2017, net interest margin was 4.16% and net interest spread was 3.95%.

Provision for Loan Losses

The allowance for loan losses is a reserve established through provisions for loan losses charged to income and represents management’s best estimate of probable loan losses that have been incurred within the existing portfolio of loans. The allowance, in the judgment of management, is necessary to reserve for estimated losses and risk inherent in the loan portfolio. The Company’s allowance for loan loss methodology is based on historical loss experience by type of credit and internal risk grade, specific homogeneous risk pools and specific loss allocations, with adjustments for current events and conditions. The Company’s process for determining the appropriate level of reserves is designed to account for changes in credit quality as they occur. The provision for loan losses reflects loan quality trends, including the levels of and trends related to past due loans and economic conditions at the local and national levels. It also considers the quality and risk characteristics of the Company’s loan origination and servicing policies and practices.

The Company recorded a $156,000 reverse provision for loan losses in 2018 compared to a provision of $1.4 million recorded in 2017. The decrease in provision was due to improving regulatory concentration levels and was offset by loan growth. For more information on changes in the allowance for loan losses, refer to ***Note E*** of the notes to the consolidated financial statements in the section titled ***Allowance for Loan Losses***.

Non-Interest Income

Non-interest income for the year ended December 31, 2018 was $4.7 million, an increase of $1.6 million from $3.1 million for the comparative 2017 period partly due to the start-up of a mortgage department. Contributing to the increase was an increase in deposit service charges of $225,000 due to a higher number of deposits accounts from the Premara acquisition, an increase in fees on sale of mortgages of $497,000 and an increase in other non-interest income of $908,000 primarily due to an increased number of debit cards from the acquisition.

Non-Interest Expenses

Non-interest expenses increased by $7.2 million or 26.5% to $34.6 million for the year ended December 31, 2017, from $27.3 million for the same period in 2017. The following are highlights of the significant changes in non-interest expenses from 2017 to 2018.

- Personnel expenses increased $3.8 million to $18.3 million primarily due to additional staff costs from the acquisition of Carolina Premier Bank, cost of living increases, the expansion of the mortgage department and starting a SBA loan department.
- Occupancy and equipment expenses increased $1.5 million to $3.7 million primarily due to additional branches from the Carolina Premier Bank acquisition and increases in repairs and maintenance.
- Information systems increased $1.1 million to $3.4 million from $2.3 million in 2017 due largely to the increase in security related applications and increased number of accounts from the acquisition.
- Professional fees increased to $1.4 million in 2018 from $1.2 million in 2017, an 18.0% increase due to legal fees and consulting fees.
- Merger /acquisition related expenses recognized were $1.8 million in 2018 compared to $2.2 million in 2017.
- Other operating expense increased $586,000 primarily due to additional sundry expenses associated with acquisition of Carolina Premier Bank.

Provision for Income Taxes

The Company’s effective tax rate in 2018 was 22.1%, compared to 64.2% in 2017. Included in the effective tax rate for 2017 is the effect of the tax law legislation change enacted December 22, 2017. The tax law change required a re-measurement of the deferred taxes of the Company that resulted in a corresponding increase in income tax expense of $2.6 million. For further discussion pertaining to the Company’s tax position, refer to Note L of the consolidated financial statements included under Item 8 of this annual report.

NET INTEREST INCOME

The following table sets forth, for the periods indicated, information with regard to average balances of assets and liabilities, as well as the total dollar amounts of interest income from interest-earning assets and interest expense on interest-bearing liabilities, resultant yields or costs, net interest income, net interest spread, net interest margin and ratio of average interest-earning assets to average interest-bearing liabilities. Non-accrual loans have been included in determining average loans.

	For the Years Ended December 31,								
	2019			2018			2017		
	(dollars in thousands)								
	Average balance	Interest	Average rate	Average balance	Interest	Average rate	Average balance	Interest	Average rate
INTEREST-EARNING ASSETS:									
Loans, gross of allowance	$ 995,699	$ 54,645	5.49%	$ 978,499	$ 53,822	5.50%	$ 732,289	$ 37,853	5.17%
Investment securities	76,875	2,110	2.74%	57,505	1,545	2.69%	59,082	1,523	2.58%
Other interest-earning assets	91,575	1,838	2.01%	98,460	1,618	1.64%	44,204	480	1.09%
Total interest-earning assets	1,164,149	58,593	5.03%	1,134,464	56,985	5.02%	835,575	39,856	4.77%
Other assets	104,579			94,112			75,269		
Total assets	$ 1,268,728			$ 1,228,576			$ 910,844		
INTEREST-BEARING LIABILITIES:									
Deposits:									
Savings, NOW and money market	$ 319,930	1,616	0.51%	$ 315,849	1,339	0.42%	$ 220,249	547	0.25%
Time deposits over $100,000	299,451	6,104	2.04%	321,387	4,811	1.50%	258,141	2,811	1.09%
Other time deposits	115,025	1,957	1.70%	115,603	1,482	1.28%	94,420	968	1.03%
Borrowings	60,799	1,879	3.09%	70,750	1,818	2.57%	49,891	780	1.56%
Total interest-bearing liabilities	795,205	11,556	1.45%	823,589	9,450	1.15%	622,701	5,106	0.82%
Non-interest-bearing deposits	246,726			236,999			173,608		
Other liabilities	12,473			6,035			4,712		
Shareholders' equity	214,324			161,953			109,823		
Total liabilities and shareholders' equity	$ 1,268,728			$ 1,228,576			$ 910,844		
Net interest income/interest rate spread (taxable-equivalent basis)		$ 47,037	3.58%		$ 47,535	3.98%		$ 34,750	3.95%
Net interest margin (taxable-equivalent basis)			4.04%			4.19%			4.16%
Ratio of interest-earning assets to interest-bearing liabilities	146.40%			135.91%			134.19%		
Reported net interest income									
Net interest income/net interest margin (taxable-equivalent basis)		$ 47,037	4.03%		$ 47,685	4.19%		$ 34,750	4.00%
Less:									
taxable-equivalent adjustment		147			150			239	
Net Interest Income		$ 46,890			$ 47,535			$ 34,511	

RATE/VOLUME ANALYSIS

The following table analyzes the dollar amount of changes in interest income and interest expense for major components of interest-earning assets and interest-bearing liabilities. The table distinguishes between (i) changes attributable to volume (changes in volume multiplied by the prior period's rate), (ii) changes attributable to rate (changes in rate multiplied by the prior period's volume), and (iii) net change (the sum of the previous columns). The change attributable to both rate and volume (changes in rate multiplied by changes in volume) has been allocated equally to both the changes attributable to volume and the changes attributable to rate.

	Year Ended December 31, 2019 vs. 2018 Increase (Decrease) Due to			Year Ended December 31, 2018 vs. 2017 Increase (Decrease) Due to			Year Ended December 31, 2017 vs. 2016 Increase (Decrease) Due to		
	Volume	Rate	Total	Volume	Rate	Total	Volume	Rate	Total
	(dollars in thousands)								
Interest income:									
Loans	$ 945	$ (122)	$ 823	$ 13,135	$ 2,834	$ 15,969	$ 5,227	$ (436)	$ 4,791
Investment securities	526	39	565	(42)	64	22	(318)	208	(110)
Other interest-earning assets	(126)	346	220	740	398	1,138	36	187	223
Total interest income (taxable-equivalent basis)	1,345	263	1,608	13,833	3,296	17,129	4,945	(41)	4,904
Interest expense:									
Deposits:									
Savings, NOW and money market	19	258	277	321	471	792	23	134	157
Time deposits over $100,000	(388)	1,681	1,293	818	1,182	2,000	516	617	1,133
Other time deposits	(9)	484	475	244	270	514	30	(48)	(18)
Borrowings	(282)	343	61	431	607	1,038	(102)	203	101
Total interest expense	(660)	2,766	2,106	1,814	2,530	4,344	466	906	1,373
Net interest income									
Increase/(decrease) (taxable-equivalent basis)	$ 2,005	$ (2,503)	(498)	$ 12,019	$ 766	12,785	$ 4,478	$ (947)	3,531
Less:									
Taxable-equivalent adjustment			(3)			(88)			(9)
Net interest income Increase/(decrease)			$ (495)			$ 12,873			$ 3,540

During 2019, we experienced an overall increase in the interest rate component of our net interest income with a small decrease for loan volume and an increase in funding costs which was offset by a reduction in deposit balances. The changes in 2019 caused an overall decrease in net interest income. In 2018 and 2017, increasing loan volume was the major contributor to increased net interest income. In 2018, interest rates increased for both interest income and interest expense. The volume component had a positive variance which also resulted in an overall increase in net interest income.

LIQUIDITY

Market and public confidence in the Company's financial strength and in the strength of financial institutions in general will largely determine the Company's access to appropriate levels of liquidity. This confidence depends significantly on the Company's ability to maintain sound asset quality and appropriate levels of capital resources. The term "liquidity" refers to the Company's ability to generate adequate amounts of cash to meet current needs for funding loan originations, deposit withdrawals, maturities of borrowings and operating expenses. Management measures the Company's liquidity position by giving consideration to both on and off-balance sheet sources of, and demands for, funds on a daily and weekly basis.

Liquid assets (consisting of cash and due from banks, interest-earning deposits with other banks, federal funds sold and investment securities classified as available for sale) comprised 11.9% and 15.2% of total assets at December 31, 2019 and 2018, respectively.

The Company has been a net seller of federal funds, maintaining liquidity sufficient to fund new loan demand. When the need arises, the Company has the ability to sell securities classified as available for sale, sell loan participations to other banks, or to borrow funds as necessary. The Company has established credit lines with other financial institutions to purchase up to $241.0 million in federal funds. Also, as a member of the Federal Home Loan Bank of Atlanta ("FHLB"), the Company may obtain advances of up to 10% of assets, subject to our available collateral. A floating lien of $110.4 million on qualifying loans is pledged to FHLB to secure such borrowings. In addition, the Company may borrow at the Federal Reserve discount window and has pledged $606,000 in securities for that purpose. As another source of short-term borrowings, the Company, from time to time, also utilizes securities sold under agreements to repurchase. At December 31, 2019 and 2018, the Company has no borrowings outstanding under securities sold under agreements to repurchase.

At December 31, 2019, the Company's outstanding commitments to extend credit totaled $238.6 million, which consisted of loan commitments and undisbursed lines of credit of $236.2 million, and letters of credit of $2.4 million. The Company believes that its combined aggregate liquidity position from all sources is sufficient to meet the funding requirements of loan demand and deposit maturities and withdrawals in the near term.

Total deposits were $992.8 million and $980.4 million at December 31, 2019 and 2018, respectively. Time deposits, which are the only deposit accounts that have stated maturity dates, are generally considered to be rate sensitive. Time deposits represented 43.2% and 43.6% of total deposits at December 31, 2019 and 2018, respectively. Time deposits of more than $250,000 represented 15.1% and 12.3%, respectively, of the total deposits at December 31, 2019 and 2018. Management believes most other time deposits are relationship-oriented. While competitive rates will need to be paid to retain these deposits at their maturities, there are other subjective factors that will determine their continued retention. Based upon prior experience, management anticipates that a substantial portion of outstanding certificates of deposit will renew upon maturity.

Management believes that current sources of funds provide adequate liquidity for the Bank's current cash flow needs. The Company maintains minimal cash balances. Management believes that the current cash balances plus taxes receivable will provide adequate liquidity for the Company's current cash flow needs. Subject to certain regulatory dividend restrictions and maintenance of required capital levels, dividends paid by the Bank to the Company may also be a source of liquidity for the Company.

CAPITAL

A significant measure of the strength of a financial institution is its capital base. Federal regulations have classified and defined capital into the following components: (1) Tier 1 capital, which includes common shareholders' equity and qualifying preferred equity (including qualifying trust preferred securities), and (2) Tier 2 capital, which includes a portion of the allowance for loan losses, certain qualifying long-term debt and preferred stock which does not qualify as Tier 1 capital. Financial institutions and holding companies became subject to the Basel III capital requirements beginning on January 1, 2015. A relatively new part of the capital ratios profile is the Common Equity Tier 1 risk-based ratio, which does not include limited life components such as trust preferred securities. Minimum capital levels are regulated by risk-based capital adequacy guidelines that require a financial institution to maintain capital as a percent of its assets and certain off-balance sheet items adjusted for predefined credit risk factors (risk-adjusted assets). A financial institution is required to maintain, at a minimum, Tier 1 capital as a percentage of risk-adjusted assets of 6.0% and combined Tier 1 and Tier 2 capital as a percentage of risk-adjusted assets of 8.0%. In addition to the risk-based guidelines, federal regulations require that we maintain a minimum leverage ratio (Tier 1 capital as a percentage of tangible assets) of 4.0%. The new capital rules that took effect in 2015 require banks to hold Common Equity Tier 1 capital in excess of minimum risk-based capital ratios by at least 2.5 percent to avoid limits on capital distributions and certain discretionary bonus payments to executive officers and similar employees. The Company's equity to assets ratio was 16.7% at December 31, 2019. As the following table indicates, at December 31, 2019, the Company and its bank subsidiary exceeded minimum regulatory capital requirements.

	At December 31, 2019	
	Actual Ratio	Minimum Requirement
Select Bancorp, Inc.		
Total risk-based capital ratio	18.26%	8.00%
Tier 1 risk-based capital ratio	17.52%	6.00%
Common equity Tier 1 risk-based capital ratio	16.46%	4.50%
Leverage ratio	15.84%	4.00%
Select Bank & Trust		
Total risk-based capital ratio	15.69%	8.00%
Tier 1 risk-based capital ratio	14.95%	6.00%
Common equity Tier 1 risk-based capital ratio	14.95%	4.50%
Leverage ratio	13.59%	4.00%

During 2004, the Company issued $12.4 million of junior subordinated debentures to a special purpose subsidiary, New Century Statutory Trust I, which in turn issued $12.0 million of trust preferred securities to investors. The proceeds provided additional capital for the expansion of the Bank. Under the current applicable regulatory guidelines, all of the trust preferred securities qualify as Tier 1 capital. Management expects that the Company and the Bank will remain "well capitalized" for regulatory purposes, although there can be no assurance that additional capital will not be required in the future.

The Company's amended Articles of Incorporation, subject to certain limitations, authorize the Company's board of directors from time to time by resolution and without further shareholder action, to provide for the issuance of shares of preferred stock, in one or more series, and to fix the preferences, limitations and relative rights of such shares of preferred stock. The Company does not currently have any preferred stock outstanding.

ASSET/LIABILITY MANAGEMENT

The Company's results of operations depend substantially on its net interest income. Like most financial institutions, the Company's interest income and cost of funds are affected by general economic conditions and by competition in the marketplace.

The purpose of asset/liability management is to provide stable net interest income growth by protecting the Company's earnings from undue interest rate risk, which arises from volatile interest rates and changes in the balance sheet mix, and by managing the risk/return relationships between liquidity, interest rate risk, market risk, and capital adequacy. The Company maintains, and has complied with, a board approved asset/liability management policy that provides guidelines for controlling exposure to interest rate risk by utilizing the following ratios and trend analyses: liquidity, equity, volatile liability dependence, portfolio maturities, maturing assets and maturing liabilities. The Company's policy is to control the exposure of its earnings to changing interest rates by generally endeavoring to maintain a position within a narrow range around an "earnings neutral position," which is defined as the mix of assets and liabilities that generate a net interest margin that is least affected by interest rate changes.

When suitable lending opportunities are not sufficient to utilize available funds, the Company has generally invested such funds in securities, primarily securities issued by governmental agencies, mortgage-backed securities and municipal obligations. The securities portfolio contributes to the Company's income and plays an important part in overall interest rate management. However, management of the securities portfolio alone cannot balance overall interest rate risk. The securities portfolio must be used in combination with other asset/liability techniques to actively manage the balance sheet. The primary objectives in the overall management of the securities portfolio are safety, liquidity, yield, asset/liability management (interest rate risk), and investing in securities that can be pledged for public deposits.

In reviewing the needs of the Company with regard to proper management of its asset/liability program, the Company's management estimates its future needs, taking into consideration historical periods of high loan demand and low deposit balances, estimated loan and deposit increases (due to increased demand through marketing), and forecasted interest rate changes.

The analysis of an institution's interest rate gap (the difference between the re-pricing of interest-earning assets and interest-bearing liabilities during a given period of time) is a standard tool for the measurement of exposure to interest rate risk. The following table sets forth the amounts of interest-earning assets and interest-bearing liabilities outstanding at December 31, 2019, of which are projected to re-price or mature in each of the future time periods shown. Except as stated below, the amounts of assets and liabilities shown which re-price or mature within a particular period were determined in accordance with the contractual terms of the assets or liabilities. Loans with adjustable rates are shown as being due at the end of the next upcoming adjustment period. Money market deposit accounts and negotiable order of withdrawal or other transaction accounts are assumed to be subject to immediate re-pricing and depositor availability and have been placed in the shortest period. In making the gap computations, none of the assumptions sometimes made regarding prepayment rates and deposit decay rates have been used for any interest-earning assets or interest-bearing liabilities. In addition, the table does not reflect scheduled principal payments that will be received throughout the lives of the loans. The interest rate sensitivity of the Company's assets and liabilities illustrated in the following table would vary substantially if different assumptions were used or if actual experience differs from that indicated by such assumptions.

	Terms to Re-pricing at December 31, 2019				
	1 Year or Less	More Than 1 Year to 3 Years	More Than 3 Years to 5 Years	More Than 5 Years	Total
	(dollars in thousands)				
Interest-earning assets:					
Loans	$ 277,523	$ 191,618	$ 280,680	$ 280,154	$ 1,029,975
Securities, available for sale	4,753	4,083	2,189	61,342	72,367
Interest-earning deposits in other banks	50,920	-	-	-	50,920
Federal funds sold	9,047	-	-	-	9,047
Stock in the Federal Home Loan Bank of Atlanta	3,045	-	-	-	3,045
Other non-marketable securities	719	-	-	-	719
Total interest-earning assets	$ 346,007	$ 195,701	$ 282,869	$ 341,496	$ 1,166,073
Interest-bearing liabilities:					
Deposits:					
Savings, NOW and money market	$ 323,273	$ -	$ -	$ -	$ 323,273
Time	88,824	21,563	1,482	-	111,869
Time over $100,000	243,430	70,203	3,758	-	317,391
Short-term debt	-	-	-	-	-
Long-term debt	-	20,000	25,000	12,372	57,372
Total interest-bearing liabilities	$ 655,527	$ 111,766	$ 30,240	$ 12,372	$ 809,905
Interest sensitivity gap per period	$ (309,520)	$ 83,935	$ 252,629	$ 329,124	$ 356,168
Cumulative interest sensitivity gap	$ (309,520)	$ (225,585)	$ 27,044	$ 356,168	$ 356,168
Cumulative gap as a percentage of total interest-earning assets	(89.45)%	(41.64)%	3.28%	30.54%	30.54%
Cumulative interest-earning assets as a percentage of interest-bearing liabilities	52.78%	70.60%	103.39%	143.98%	143.98%

CRITICAL ACCOUNTING POLICIES

A critical accounting policy is one that is both very important to the portrayal of the Company's financial condition and results, and requires management to make difficult, subjective or complex judgments. What makes these judgments difficult, subjective and/or complex is the need to make estimates about the effects of matters that are inherently uncertain. The following is a summary of the Company’s most complex accounting policies: the allowance for loan losses, business combinations and deferred tax asset.

Asset Quality and the Allowance for Loan Losses

The financial statements are prepared on the accrual basis of accounting, including the recognition of interest income on the loan portfolio, unless a loan is placed on a non-accrual basis. Loans are placed on a non-accrual basis when there are serious doubts about the collectability of principal or interest. Amounts received on non-accrual loans generally are applied first to principal and then to interest only after all principal has been collected. Restructured loans are those for which concessions, including the reduction of interest rates below a rate otherwise available to that borrower or which the deferral of interest or principal have been granted due to the borrower’s weakened financial condition. Interest on restructured loans is accrued at the restructured rates when it is anticipated that no loss of original principal will occur. See the previous section titled “Past Due Loans and Nonperforming Assets” for a discussion on past due loans, non-performing assets and other impaired loans.

The allowance for loan losses is maintained at a level considered appropriate in light of the risk inherent within the Company's loan portfolio, based on management's assessment of various factors affecting the loan portfolio, including a review of problem loans, business conditions and loss experience and an overall evaluation of the quality of the underlying collateral. The allowance is increased by provisions charged to operations and reduced by loans charged off, net of recoveries. Additional information regarding the Company's allowance for loan losses and loan loss experience is presented below in the discussion of the allowance for loan losses and in **Note E** to the accompanying notes to consolidated financial statements.

Business combinations and method of accounting for loans acquired

The Company accounts for acquisitions under FASB ASC Topic 805, *Business Combinations*, which requires the use of the acquisition method of accounting. All identifiable assets acquired, including loans, and liabilities assumed, are recorded at fair value along with the identifiable intangible assets. The recognized net goodwill is associated with the difference from the fair value and the acquired book value of the assets and liabilities of the transaction. No allowance for credit losses related to the acquired loans is recorded on the acquisition date because the fair value of the loans acquired incorporates assumptions regarding credit risk.

The acquired loans were segregated between those considered to be performing ("acquired performing") and those with evidence of credit deterioration based on such factors as past due status, nonaccrual status and credit risk ratings. Acquired credit-impaired loans (PCI loans) are accounted for under the accounting guidance for loans and debt securities acquired with deteriorated credit quality, found in FASB ASC Topic 310-30, *Receivables—Loans and Debt Securities Acquired with Deteriorated Credit Quality,* formerly American Institute of Certified Public Accountants ("AICPA") Statement of Position (SOP) 03-3, *Accounting for Certain Loans or Debt Securities Acquired in a Transfer*, and initially measured at fair value, which includes estimated future credit losses expected to be incurred over the lives of the loans. Loans acquired in business combinations with evidence of credit deterioration are considered impaired. Loans acquired through business combinations that do not meet the specific criteria of FASB ASC Topic 310-30, but for which a discount is attributable, at least in part to credit quality, are also accounted for under this guidance. Certain acquired loans, such as acquired performing loans and lines of credit (consumer and commercial) are accounted for in accordance with FASB ASC Topic 310-20, where the discount is accreted through earnings based on estimated cash flows over the estimated lives of the loans.

For further discussion of the Company's loan accounting and acquisitions, see **Note B**—Summary of Significant Accounting Policies, **Note C**—Business Combinations, and **Note E**—Loans of the Notes to Consolidated Financial Statements included under Item 8 of this annual report.

Allowance for loan losses

The allowance for loan losses reflects the estimated losses that will result from the inability of the Bank's borrowers to make required loan payments. The allowance for loan losses is established for estimated credit losses through a provision for credit losses charged to earnings. Credit losses are charged against the allowance when management believes that the collectability of the principal is unlikely. Subsequent recoveries, if any, are credited to the allowance.

The Company's allowance for loan loss methodology incorporates several quantitative and qualitative risk factors used to establish an appropriate allowance for credit losses at each reporting date. Quantitative factors include our historical loss experience, delinquency and charge-off trends, collateral values, changes in the level of nonperforming loans and other factors. Qualitative factors include the economic condition of our operating markets, composition of the loan portfolio and the state of certain industries. Specific changes in the risk factors are based on actual loss experience, as well as perceived risk of similar groups of loans classified by collateral type, purpose and term. A three-year loss history is incorporated into the allowance calculation model. Due to the credit concentration of our loan portfolio in real estate secured loans, the value of collateral is heavily dependent on real estate values within our market footprint.

Allowance for loan losses for acquired loans

Subsequent to the acquisition date, decreases in cash flows expected to be received on FASB ASC Topic 310-30 acquired loans from the Company's initial estimates are recognized as impairment through the provision for credit losses. Probable and significant increases in cash flows (in a loan pool where an allowance for acquired credit losses was previously recorded) reduces the remaining allowance for acquired credit losses before recalculating the amount of accretable yield percentage for the loan pool in accordance with ASC 310-30.

Acquired loans that are not subject to FASB ASC Topic 310-30 are accounted for in accordance with FASB ASC Topic 310-20, where the discount is accreted through earnings based on contractual cash flows over the estimated life of the loan. The allowance for these loans will be determined in a similar manner to the non-acquired credit losses.

Deferred Tax Asset

The Company’s net deferred tax asset was $2.8 million at December 31, 2019. In evaluating whether we will realize the full benefit of our net deferred tax asset, we consider both positive and negative evidence, including, among other things, recent earnings trends, projected earnings, and asset quality. As of December 31, 2019, management concluded that the Company’s net deferred tax assets were fully realizable. The Company will continue to monitor deferred tax assets closely to evaluate whether we will be able to realize the full benefit of our net deferred tax asset or whether there is any need for a valuation allowance. Significant negative trends in credit quality, losses from operations, tax law changes or other factors could impact the realization of the deferred tax asset in the future.

OFF-BALANCE SHEET ARRANGEMENTS

Information about the Company’s off-balance sheet risk exposure is presented in **Note N** to the accompanying consolidated financial statements. During 2004, the Company formed an unconsolidated subsidiary trust to which the Company issued $12.4 million of junior subordinated debentures (see **Note K** to the consolidated financial statements). Otherwise, as part of its ongoing business, the Company has not participated in, nor does it anticipate participating in, transactions that generate relationships with unconsolidated entities or financial partnerships, such as entities often referred to as special purpose entities, which generally are established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes.

RECENT ACCOUNTING PRONOUNCEMENTS

See **Note B** to the Company’s audited consolidated financial statements for a full description of recent accounting pronouncements, including the respective expected dates of adoption and anticipated effects on results of operations and financial condition.

IMPACT OF INFLATION AND CHANGING PRICES

A commercial bank has an asset and liability make-up that is distinctly different from that of a company with substantial investments in plant and inventory because the major portions of a commercial bank’s assets are monetary in nature. As a result, a bank’s performance may be significantly influenced by changes in interest rates. Although the banking industry is more affected by changes in interest rates than by inflation in the prices of goods and services, inflation is a factor that may influence interest rates. However, the frequency and magnitude of interest rate fluctuations do not necessarily coincide with changes in the general inflation rate. Inflation does affect operating expenses in that personnel expenses and the cost of supplies and outside services tend to increase more during periods of high inflation.

CONTRACTUAL OBLIGATIONS AND COMMITMENTS

In the normal course of business there are various outstanding contractual obligations of the Company that will require future cash outflows. In addition, there are commitments and contingent liabilities, such as commitments to extend credit that may or may not require future cash outflows. The following table reflects contractual obligations of the Company outstanding as of December 31, 2019.

	Payments Due by Period				
Contractual Obligations	Total	On Demand Or Within 1 Year	1-3 Years	4-5 Years	After 5 Years
			(dollars in thousands)		
Long-term debt	$ 57,372	$ -	$ 20,000	$ 25,000	$ 12,372
Lease obligations	12,392	1,099	2,282	2,120	6,891
Deposits	992,838	895,830	91,768	5,238	2
Total contractual cash obligations	$ 1,062,602	$ 896,929	$ 114,050	$ 32,358	$ 19,265

The following table reflects other commitments outstanding as of December 31, 2019.

	Amount of Commitment Expiration Per Period (dollars in thousands)				
Other Commitments	Total Amounts Committed	Less than 1 Year	1-3 Years	4-5 Years	After 5 Years
Undisbursed home equity credit lines	$ 44,826	$ 3,331	$ 9,067	$ 5,450	$ 26,978
Other commitments and credit lines	56,011	31,178	6,759	10,683	7,391
Un-disbursed portion of constructions loans	133,354	91,124	7,418	11,595	23,217
Letters of credit	2,367	1,952	298	117	-
Total loan commitments	$ 236,558	$ 127,585	$ 23,542	$ 27,845	$ 57,586

In addition, the Company has legally binding delayed equity commitments to private investment funds. These commitments are not currently expected to be called, and therefore, are not reflected in the financial statements. The amount of these commitments at December 31, 2019 and 2018 was $525,000 and $525,000, respectively.

NOTE REGARDING FORWARD-LOOKING STATEMENTS

This document contains forward-looking statements. Statements contained in this annual report, which are not historical facts, are forward-looking statements, as that term is defined in the Private Securities Litigation Reform Act of 1995. Such forward-looking statements are subject to risks and uncertainties that could cause actual results to differ materially from those results currently anticipated. Such forward-looking statements may be identified by the use of such words as “believe,” “expect,” “anticipate,” “should,” “might,” “planned,” “estimated,” and “potential.” Factors that could cause results and outcomes to vary include, but are not limited to: fluctuations in general economic conditions; changes in interest rates, deposit flows, loan demand, real estate values, and competition; changes in accounting principles, policies, or guidelines; changes in legislation or regulation; and other economic, competitive, governmental, regulatory, and technological factors affecting the Company's operations, pricing, products and services. Additionally, any of the risks identified under Item 1A of this annual report could also cause actual results to differ materially from those indicated in the Company’s forward-looking statements. The Company does not undertake a duty to update any forward-looking statements in this report, whether as a result of new information, future developments or otherwise.

ITEM 7A – QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK

The Company intends to reach its strategic financial objectives through the effective management of market risk. Like many financial institutions, the Company's most significant market risk exposure is interest rate risk. The Company's primary goal in managing interest rate risk is to minimize the effect that changes in market interest rates have on earnings and capital. This goal is accomplished through the active management of the balance sheet. The goal of these activities is to structure the maturity and repricing of assets and liabilities to produce stable net interest income despite changing interest rates. The Company's overall interest rate risk position is governed by policies approved by the Board of Directors and guidelines established and monitored by the Bank's Asset/Liability Committee ("ALCO").

To measure, monitor, and report on interest rate risk, the Company begins with two models: (1) net interest income ("NII") at risk, which measures the impact on NII over the next twelve and twenty-four months to immediate changes in interest rates and (2) net economic value of equity ("EVE"), which measures the impact on the present value of net assets to immediate changes in interest rates. NII at risk is designed to measure the potential short-term impact of changes in interest rates on NII. EVE is a long-term measure of interest rate risk to the Company's balance sheet, or equity. Gap analysis, which is the difference between the amount of balance sheet assets and liabilities repricing within a specified time period, is used as a secondary measure of the Company's interest rate risk position. All of these models are subject to ALCO guidelines and are monitored regularly.

In calculating NII at risk, the Company begins with a base amount of NII that is projected over the next twelve and twenty-four months, assuming that the balance sheet is static and the yield curve remains unchanged over the period. The current yield curve is then "shocked," or moved immediately, ±1.0 percent, ±2.0 percent, ±3.0 percent and ±4.0 percent in a parallel fashion, or at all points along the yield curve. New twelve-month and twenty four-month NII projections are then developed using the same balance sheet but with the new yield curves and these results are compared to the base scenario. The Company also models other scenarios to evaluate potential NII at risk such as a gradual ramp in interest rates, a flattening yield curve, a steepening yield curve, and others that management deems appropriate.

EVE at risk is based on the change in the present value of all assets and liabilities under different interest rate scenarios. The present value of existing cash flows with the current yield curve serves as the base case. The Company then applies an immediate parallel shock to that yield curve of ±1.0 percent, ±2.0 percent, ±3.0 percent and ±4.0 percent and recalculates the cash flows and related present values.

Key assumptions used in the models described above include the timing of cash flows, the maturity and repricing of assets and liabilities, changes in market conditions, and interest-rate sensitivities of the Company's non-maturity deposits with respect to interest rates paid and the level of balances. These assumptions are inherently uncertain and, as a result, the models cannot precisely calculate future NII or predict the impact of changes in interest rates on NII and EVE. Actual results could differ from simulated results due to the timing, magnitude and frequency of changes in interest rates and market conditions, changes in spreads and management strategies, among other factors. Projections of NII are assessed as part of the Company's forecasting process.

NII and EVE Analysis. The following table presents the estimated exposure to NII for the next twelve months due to immediate changes in interest rates and the estimated exposure to EVE due to immediate changes in interest rates. All information is presented as of September 30, 2019.

(Dollars in thousands)	September 30, 2019 Estimated Effect on NII	Estimated Effect on EVE
Immediate change in interest rates:		
+ 4.0%	11.5%	12.8%
+ 3.0%	8.9	10.5
+ 2.0%	5.9	7.6
+ 1.0%	2.8	4.0
No change	-	-
- 1.0%	(1.8)	(4.8)

While the measures presented in the table above are not a prediction of future NII or EVE valuations, they do suggest that if all other variables remained constant, immediate increases in interest rates at all points on the yield curve may produce higher NII in the short term. Other important factors that impact the levels of NII are balance sheet size and mix, interest rate spreads, the slope of the yield curve, the speed of interest rates changes, and management actions taken in response to the preceding conditions.

Item 8 – FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA
Selected Quarterly Financial Data (Unaudited)

(dollars in thousands, except share and per share data)

	2019			
	Quarterly Periods Ended			
	December 31	September 30	June 30	March 31
Selected Results of Operations				
Total interest income	$ 14,816	$ 15,008	$ 14,572	$ 14,050
Total interest expense	2,948	3,140	2,875	2,593
Net interest income	11,868	11,868	11,697	11,457
Provision for (recovery of) loan losses	302	231	(207)	112
Net interest income after provision	11,566	11,637	11,904	11,345
Noninterest income	1,446	1,448	1,328	1,197
Merger/acquisition related expenses	171	128	107	-
Noninterest expense	8,923	8,803	8,704	8,304
Income before income taxes	3,918	4,154	4,421	4,238
Provision for income taxes	877	915	973	931
Net income	$ 3,041	$ 3,239	$ 3,448	$ 3,307
Common Share Data				
Basic earnings per share	$ 0.17	$ 0.17	$ 0.18	$ 0.17
Diluted earnings per share	$ 0.16	$ 0.17	$ 0.18	$ 0.17
Cash dividends declared per share	$ -	$ -	$ -	$ -
Weighted Average Common Shares Outstanding				
Basic	18,414,393	19,028,572	19,318,358	19,315,686
Diluted	18,460,118	19,073,235	19,359,492	19,365,354
Market Data				
High Sales Price	$ 12.47	$ 11.65	$ 12.28	$ 12.48
Low Sales Price	11.02	10.61	11.01	10.83
Period-end Closing	12.30	11.60	11.44	11.37
Average Daily Trading Volume	23,168	44,452	18,544	19,479

(dollars in thousands, except share and per share data)

	2018			
	Quarterly Periods Ended			
	December 31	September 30	June 30	March 31
Selected Results of Operations				
Total interest income	$ 14,544	$ 14,382	$ 14,187	$ 13,722
Total interest expense	2,644	2,530	2,258	2,018
Net interest income	11,900	11,852	11,929	11,704
Provision for (recovery of) loan losses	(395)	(459)	557	141
Net interest income after provision	12,295	12,311	11,372	11,563
Noninterest income	1,244	1,066	1,226	1,165
Merger/acquisition related expenses	-	-	-	1,826
Noninterest expense	7,864	7,800	8,602	8,458
Income before income taxes	5,675	5,577	3,996	2,444
Provision for income taxes	1,221	1,256	886	547
Net income	$ 4,454	$ 4,321	$ 3,110	$ 1,897
Common Share Data				
Basic earnings per share	$ 0.23	$ 0.27	$ 0.22	$ 0.14
Diluted earnings per share	$ 0.23	$ 0.27	$ 0.22	$ 0.13
Cash dividends declared per share	$ -	$ -	$ -	$ -
Weighted Average Common Shares Outstanding				
Basic	19,302,263	15,858,455	14,019,273	14,011,707
Diluted	19,360,050	15,916,734	14,086,671	14,081,776
Market Data				
High Sales Price	$ 12.69	$ 14.05	$ 13.47	$ 13.58
Low Sales Price	11.73	12.21	12.63	12.52
Period-end Closing	12.38	12.40	13.47	13.36
Average Daily Trading Volume	43,449	38,551	34,553	19,365

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Shareholders and the Board of Directors
Select Bancorp, Inc.
Dunn, North Carolina

Opinion on Internal Control Over Financial Reporting

We have audited Select Bancorp, Inc. (the "Company")'s internal control over financial reporting as of December 31, 2019, based on criteria established in *Internal Control—Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission. In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2019, based on criteria established in *Internal Control—Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) ("PCAOB"), the consolidated financial statements of Select Bancorp, Inc. for each of the three years in the period ended December 31, 2019, and our report dated March 11, 2020, expressed an unqualified opinion on those consolidated financial statements.

Basis for Opinion

The Company's management is responsible for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Annual Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audit in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

Definition and Limitations of Internal Control Over Financial Reporting

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ Dixon Hughes Goodman LLP

Raleigh, North Carolina
March 11, 2020

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Shareholders and the Board of Directors
Select Bancorp, Inc.
Dunn, North Carolina

Opinion on the Consolidated Financial Statements

We have audited the accompanying consolidated balance sheets of Select Bancorp, Inc. (the "Company") as of December 31, 2019 and 2018, the related consolidated statements of operations, comprehensive income, changes in shareholders' equity and cash flows, for each of the three years in the period ended December 31, 2019, and the related notes (collectively referred to as the "financial statements"). In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2019 and 2018, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2019, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) ("PCAOB"), the Company's internal control over financial reporting as of December 31, 2019, based on criteria established in *Internal Control - Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated March 11, 2020 expressed an unqualified opinion thereon.

Basis for Opinion

These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the Company's financial statements based on our audits. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud.

Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

/s/ Dixon Hughes Goodman LLP

We have served as the Company's auditor since 2000.

Raleigh, North Carolina
March 11, 2020

SELECT BANCORP, INC.
CONSOLIDATED BALANCE SHEETS
December 31, 2019 and 2018

	2019	2018
	(In thousands, except share and per share data)	
ASSETS		
Cash and due from banks	$ 19,110	$ 17,059
Interest-earning deposits in other banks	50,920	121,303
Certificates of deposit	-	1,000
Federal funds sold	9,047	-
Investment securities available for sale, at fair value	72,367	51,533
Loans held for sale	928	580
Loans	1,029,975	986,040
Allowance for loan losses	(8,324)	(8,669)
NET LOANS	1,021,651	977,371
Accrued interest receivable	4,189	3,889
Stock in Federal Home Loan Bank of Atlanta (“FHLB”), at cost	3,045	3,283
Other non-marketable securities	719	762
Foreclosed real estate	3,533	1,088
Premises and equipment, net	17,791	17,920
Right of use lease asset	8,596	-
Bank owned life insurance	29,789	29,117
Goodwill	24,579	24,579
Core deposit intangible (“CDI”)	1,610	2,085
Assets held for sale	-	668
Other assets	7,202	6,288
TOTAL ASSETS	$ 1,275,076	$ 1,258,525
LIABILITIES AND SHAREHOLDERS’ EQUITY		
Deposits:		
Demand	$ 240,305	$ 247,007
Savings	43,128	51,811
Money market and NOW	280,145	254,482
Time	429,260	427,127
TOTAL DEPOSITS	992,838	980,427
Short-term debt	-	7,000
Long-term debt	57,372	57,372
Lease liability	8,813	-
Accrued interest payable	578	667
Accrued expenses and other liabilities	2,700	3,448
TOTAL LIABILITIES	1,062,301	1,048,914
Shareholders’ Equity		
Preferred stock, no par value, 5,000,000 shares authorized; no preferred shares were issued and outstanding	-	-
Common stock, $1 par value, 50,000,000 shares authorized; 18,330,058 and 19,311,505 shares issued and outstanding at December 31, 2019 and 2018, respectively	18,330	19,312
Additional paid-in capital	140,870	150,718
Retained earnings	52,675	39,640
Common stock issued to deferred compensation trust, at cost; 319,753 and 303,239 shares outstanding at December 31, 2019 and 2018, respectively	(2,815)	(2,615)
Directors’ Deferred Compensation Plan Rabbi Trust	2,815	2,615
Accumulated other comprehensive income (loss)	900	(59)
TOTAL SHAREHOLDERS’ EQUITY	212,775	209,611
TOTAL LIABILITIES AND SHAREHOLDERS’ EQUITY	$ 1,275,076	$ 1,258,525

See accompanying notes.

SELECT BANCORP, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS
Years Ended December 31, 2019, 2018 and 2017

	2019	2018	2017
	(In thousands, except share and per share data)		
INTEREST INCOME			
Loans	$ 54,605	$ 53,796	$ 37,849
Federal funds sold and interest-earning deposits in other banks	1,838	1,618	480
Investments	2,003	1,421	1,288
TOTAL INTEREST INCOME	58,446	56,835	39,617
INTEREST EXPENSE			
Money market, NOW and savings deposits	1,616	1,339	547
Time deposits	8,061	6,293	3,779
Short-term debt	62	328	357
Long-term debt	1,817	1,490	423
TOTAL INTEREST EXPENSE	11,556	9,450	5,106
NET INTEREST INCOME	46,890	47,385	34,511
PROVISION FOR (RECOVERY OF) LOAN LOSSES	438	(156)	1,367
NET INTEREST INCOME AFTER PROVISION FOR (RECOVERY OF) LOAN LOSSES	46,452	47,541	33,144
NON-INTEREST INCOME			
Gain on the sale of securities	48	-	1
Service charges on deposit accounts	1,161	1,124	899
Fees from the sale of mortgages	753	497	-
Other fees and income	3,457	3,080	2,172
TOTAL NON-INTEREST INCOME	5,419	4,701	3,072
NON-INTEREST EXPENSE			
Personnel	20,278	18,304	14,552
Occupancy and equipment	3,695	3,666	2,192
Deposit insurance	184	628	357
Professional fees	1,886	1,394	1,181
Core deposit intangible amortization	825	1,016	409
Merger/acquisition related expenses	406	1,826	2,166
Information systems	3,492	3,372	2,257
Foreclosure-related expenses	140	115	562
Other	4,234	4,229	3,643
TOTAL NON-INTEREST EXPENSE	35,140	34,550	27,319
INCOME BEFORE INCOME TAX	16,731	17,692	8,897
INCOME TAX	3,696	3,910	5,712
NET INCOME	13,035	13,782	3,185
Basic	$ 0.69	$ 0.87	$ 0.27
Diluted	$ 0.68	$ 0.87	$ 0.27
WEIGHTED AVERAGE COMMON SHARES OUTSTANDING			
Basic	19,016,808	15,812,585	11,763,050
Diluted	19,063,237	15,877,633	11,826,977

See accompanying notes.

SELECT BANCORP, INC.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
Years Ended December 31, 2019, 2018 and 2017

	2019	2018	2017
	(Amounts in thousands)		
Net income	$ 13,035	$ 13,782	$ 3,185
Other comprehensive income (loss):			
Unrealized gains (losses) on investment securities-available for sale	1,294	(596)	(41)
Tax effect	(298)	139	82
	996	(457)	41
Reclassification adjustment for (gains) losses included in net income	(48)	-	(1)
Tax effect	11	-	-
	(37)	-	(1)
Total	959	(457)	40
Total comprehensive income	$ 13,994	$ 13,325	$ 3,225

See accompanying notes.

SELECT BANCORP, INC.
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
Years Ended December 31, 2019, 2018 and 2017 (Amounts in thousands except share data)

	Preferred Stock		Common Stock		Additional paid-in	Retained	Deferred	Common Stock Issued to Deferred Compensation	Accumulated Other Comprehensive Income	Total Shareholders'
	Shares	Amount	Shares	Amount	Capital	Earnings	Comp Plan	Trust	(loss)	Equity
Balance at December 31, 2016	**-**	**-**	**11,645,413**	**11,645**	**69,597**	**22,673**	**2,340**	**(2,340)**	**358**	**104,273**
Net income	-	-	-	-	-	3,185	-	-	-	3,185
Other comprehensive income	-	-	-	-	-	-	-	-	40	40
Shares issued for Premara merger	-	-	2,334,999	2,335	26,001	-	-	-	-	28,336
Stock option exercises	-	-	28,725	29	137	-	-	-	-	166
Stock based compensation	-	-	-	-	115	-	-	-	-	115
Director equity incentive plan, net	-	-	-	-	-	-	178	(178)	-	-
Balance at December 31, 2017	**-**	**$ -**	**14,009,137**	**$ 14,009**	**$ 95,850**	**$ 25,858**	**$ 2,518**	**$ (2,518)**	**$ 398**	**$ 136,115**
Net income	-	-	-	-	-	13,782	-	-	-	13,782
Other comprehensive loss	-	-	-	-	-	-	-	-	(457)	(457)
Shares issued for capital raise, net	-	-	5,270,834	5,271	54,535	-	-	-	-	59,806
Stock option exercises	-	-	31,534	32	155	-	-	-	-	187
Stock based compensation	-	-	-	-	178	-	-	-	-	178
Director equity incentive plan, net	-	-	-	-	-	-	97	(97)	-	-
Balance at December 31, 2018	**-**	**$ -**	**19,311,505**	**$ 19,312**	**$ 150,718**	**$ 39,640**	**$ 2,615**	**$ (2,615)**	**$ (59)**	**$ 209,611**
Net income	-	-	-	-	-	13,035	-	-	-	13,035
Other comprehensive income	-	-	-	-	-	-	-	-	959	959
Stock repurchases	-	-	(1,008,260)	(1,008)	(10,419)	-	-	-	-	(11,427)
Stock option exercises	-	-	26,813	26	202	-	-	-	-	228
Stock based compensation	-	-	-	-	369	-	-	-	-	369
Director equity incentive plan, net	-	-	-	-	-	-	200	(200)	-	-
Balance at December 31, 2019	**-**	**$ -**	**18,330,058**	**$ 18,330**	**$ 140,870**	**$ 52,675**	**$ 2,815**	**$ (2,815)**	**$ 900**	**$ 212,775**

See accompanying notes.

SELECT BANCORP, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
Years Ended December 31, 2019, 2018 and 2017

	2019	2018	2017
	(Amounts in thousands)		
CASH FLOWS FROM OPERATING ACTIVITIES			
Net income	$ 13,035	$ 13,782	$ 3,185
Adjustments to reconcile net income to net cash provided by operating activities:			
Provision for (recovery of) loan losses	438	(156)	1,367
Depreciation and amortization of premises and equipment	1,790	1,738	1,144
Amortization and accretion of investment securities	767	560	556
Amortization of right of use asset	990	-	-
Amortization of deferred loan fees and costs	(844)	(744)	(602)
Amortization of core deposit intangible	825	1,016	409
Amortization of acquisition premium on time deposits	(14)	(178)	(292)
Amortization of acquisition premium on borrowings	-	(12)	(89)
Deferred income taxes	585	1,061	2,325
Stock-based compensation	369	178	115
Accretion on acquired loans	(904)	(3,051)	(1,061)
Proceeds from loans held for sale	34,578	22,726	-
Originations of loans held for sale	(34,173)	(22,711)	(98)
Gain on loans held for sale	(753)	(497)	-
Gain on the sale of securities	(48)	-	(1)
Increase in cash surrender value of bank owned life insurance	(672)	(686)	(575)
Loss (gain) on sale of premises and equipment	60	62	(5)
Loss on assets held for sale	8	178	-
Net loss on sale and write-downs of foreclosed real estate	49	71	442
Change in assets and liabilities:			
Net change in accrued interest receivable	(300)	108	(432)
Net change in other assets	(1,708)	2,578	526
Net change in accrued expenses and other liabilities	(719)	(11,210)	(356)
NET CASH PROVIDED BY OPERATING ACTIVITIES	13,359	4,813	6,558
CASH FLOWS FROM INVESTING ACTIVITIES			
Redemption (purchase) of FHLB stock	238	(793)	1,265
Purchase of investment securities available for sale	(38,698)	-	(1,523)
Maturities of investment securities available for sale	3,383	1,400	4,255
Mortgage-backed securities pay-downs	13,805	9,685	6,015
Proceeds from sale of investment securities available for sale	1,125	-	21,972
Net change in loans outstanding	(45,584)	(247)	(108,814)
Cash received from branch acquisitions	24,093	-	28,513
Net change in other non-marketable securities	43	257	73
Proceeds from sale of foreclosed real estate	120	717	1,442
Proceeds from sale of premises and equipment	68	104	9
Proceeds from sale of assets held for sale	660	-	-
Purchases of premises and equipment	(1,381)	(1,556)	(931)
NET CASH PROVIDED BY (USED IN) INVESTING ACTIVITIES	(42,128)	9,567	(47,724)

See accompanying notes.

SELECT BANCORP, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS (Continued)
Years Ended December 31, 2019, 2018 and 2017

	2019	2018	2017
	(Amounts in thousands)		
CASH FLOWS FROM FINANCING ACTIVITIES			
Net change in deposits	$ (12,614)	$ (14,439)	$ 89,356
Proceeds from long-term debt	-	38,000	-
Repayments of short-term debt	(7,000)	(21,267)	(26,722)
Repayments of long-term debt	-	-	(14,653)
Repayment of lease liability	(703)	-	-
Proceeds from issuance of common stock	-	63,250	-
Direct expenses related to capital transactions	-	(3,444)	-
Repurchase of common stock	(11,427)	-	-
Proceeds from stock options exercised	228	187	166
NET CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES	(31,516)	62,287	48,147
NET CHANGE IN CASH AND CASH EQUIVALENTS	(60,285)	76,667	6,981
CASH AND CASH EQUIVALENTS, BEGINNING	139,362	62,695	55,714
CASH AND CASH EQUIVALENTS, ENDING	$ 79,077	$ 139,362	$ 62,695
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION			
Cash paid during the period for:			
Interest paid	$ 11,645	$ 9,210	$ 4,900
Income taxes paid	2,553	2,277	3,471
Non-cash transactions:			
Change in fair value of investment securities available for sale, net of tax	959	(457)	(40)
Transfer from loans to foreclosed real estate	2,614	618	2,543
Acquisition:			
Assets acquired (excluding goodwill)	26,258	-	279,142
Liabilities assumed	25,776	-	256,422
Purchase price	482	-	40,693
Goodwill recorded	-	-	17,973

See accompanying notes.

NOTE A - ORGANIZATION AND OPERATIONS

Select Bancorp, Inc. ("Company") is a bank holding company whose principal business activity consists of ownership of Select Bank & Trust Company (referred to as the "Bank"). All significant intercompany transactions and balances have been eliminated in consolidation. In 2004, the Company formed New Century Statutory Trust I, which issued trust preferred securities to provide additional capital for general corporate purposes, including the current and future expansion of the Company. New Century Statutory Trust I is not a consolidated subsidiary of the Company. The Company is subject to the rules and regulations of the Board of Governors of the Federal Reserve (the "Federal Reserve") and the North Carolina Commissioner of Banks.

The Bank was originally incorporated as New Century Bank on May 19, 2000 and began banking operations on May 24, 2000. On July 25, 2014, the Company acquired Select Bank & Trust Company, Greenville, North Carolina, and changed the Bank's legal name to Select Bank & Trust Company. On December 15, 2017, the Company acquired Premara Financial, Inc. and its subsidiary Carolina Premier Bank through the merger of Premara with and into the Company, followed immediately by the merger of Carolina Premier with and into the Bank. The Bank continues as the only banking subsidiary of the Company with its headquarters and operations center located in Dunn, NC. The Bank is engaged in general commercial and retail banking in central and eastern North Carolina, as well as now in Charlotte, North Carolina, southeastern Virginia and northwest South Carolina. The Bank is subject to the supervision and regulation of the Federal Deposit Insurance Corporation and the North Carolina Commissioner of Banks.

Reclassification

Certain items for prior years have been reclassified to conform to the current year presentation. Such reclassifications had no effect on net income, total assets or shareholders' equity as previously reported.

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

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 the 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 change relate to the determination of the allowance for loan losses, business combinations, goodwill, deferred tax assets and the valuation of other real estate owned.

Business Combinations

Business combinations are accounted for under the acquisition method of accounting in accordance with Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") 805, "Business Combinations*."* Under the acquisition method, the acquiring entity in a business combination recognizes all of the acquired assets and assumed liabilities at their estimated fair values as of the date of acquisition. Any excess of the purchase price over the fair value of net assets and other identifiable intangible assets acquired is recorded as goodwill. To the extent the fair value of net assets acquired, including identified intangible assets, exceeds the purchase price, a bargain purchase gain is recognized.

Assets acquired and liabilities assumed from contingencies must also be recognized at fair value if the fair value can be determined during the measurement period. Results of operations of an acquired business are included in the Statement of Operations from the date of acquisition. Acquisition-related costs, including conversion and restructuring charges, are expensed as incurred.

The acquired assets and assumed liabilities are recorded at estimated fair values. Management makes significant estimates and exercises significant judgment in accounting for business combinations. Management uses its judgment to assign risk ratings to loans based on credit quality, appraisals and estimated collateral values, and estimated expected cash flows to measure fair values for loans. Real estate acquired in settlement of loans is valued based upon pending sales contracts and appraised values, adjusted for current market conditions. Core deposit intangibles are valued based on a weighted combination of the income and market approach where the income approach converts anticipated economic benefits to a present value and the market approach evaluates the market in which the asset is traded to find an indication of prices from actual transactions. Management uses quoted or current market prices to determine the fair value of investment securities. Fair values of deposits and borrowings are based on current market interest rates and are inclusive of any applicable prepayment penalties.

Cash and Due from Banks, Interest-Earning Deposits in Other Banks and Federal Funds Sold

For the purpose of presentation in the statements of cash flows, cash and cash equivalents are defined as those amounts included in the balance sheet captions “Cash and due from banks,” “Interest-earning deposits in other banks,” “Certificates of deposit” and “Federal funds sold.”

Certificates of Deposit

Certificates of deposit are cash instruments that management has the intent and ability to hold for the foreseeable future or until maturity and are reported at cost.

Investment Securities Available for Sale

Investment securities available for sale are reported at fair value and consist of debt instruments that are not classified as either trading securities or as held to maturity securities. Unrealized holding gains and losses, net of deferred income tax, on available for sale securities are reported as a net amount in accumulated other comprehensive income. Gains and losses on the sale of investment securities available for sale are determined using the specific-identification method.

Loans

Loans that management has the intent and ability to hold for the foreseeable future or until maturity are reported at their outstanding principal balance adjusted for any charge-offs, the allowance for loan losses, and any deferred fees or costs on originated loans and unamortized premiums or discounts on purchased loans. Loan origination fees and certain direct origination costs are capitalized and recognized as an adjustment of the yield of the related loan. The accrual of interest on impaired loans is discontinued when, in management’s opinion, the borrower may be unable to meet payment obligations as they become due. When interest accrual is discontinued, all unpaid accrued interest is reversed. Interest income is subsequently recognized only to the extent cash payments are received in excess of principal due. Loans are returned to accrual status when all of the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

The acquired loans are segregated between those considered to be performing (“acquired performing”) and those with evidence of credit deterioration based on such factors as past due status, nonaccrual status and credit risk ratings (“purchased credit-impaired loans”).

In determining the acquisition date fair value of purchased credit-impaired ("PCI") loans, and in subsequent accounting, the Company generally aggregates purchased loans into pools of loans with common risk characteristics within the following loan categories: 1-to-4 family residential loans other than junior liens, 1-to-4 family residential junior liens, construction and land development, farm land, commercial real estate (nonowner-occupied), commercial real estate (owner-occupied), commercial and industrial, and all other loan categories. Expected cash flows at the acquisition date in excess of the fair value of loans are referred to as the "accretable yield" and recorded as interest income over the life of the loans using a level yield method if the timing and amount of the future cash flows of the pool is reasonably estimable. Subsequent to the acquisition date, significant increases in cash flows over those expected at the acquisition date are recognized as interest income prospectively. Accordingly, such loans are not classified as nonaccrual and they are considered to be accruing because their interest income relates to the accretable yield recognized under accounting for PCI loans and not to contractual interest payments. The difference between the contractually required payments and the cash flows expected to be collected at acquisition, considering the impact of prepayments, is referred to as the nonaccretable difference.

The difference between the fair value of an acquired performing loan pool and the contractual amounts due at the acquisition date (the "fair value discount") is accreted into income over the estimated life of the pool. The Company's policy for determining when to discontinue accruing interest on acquired performing loans and the subsequent accounting for such loans is essentially the same as the policy for originated loans described earlier.

Loans are deemed uncollectible based on a variety of credit, collateral, documentation and other issues. In the case where a loan is unsecured and in default, it is fully charged off.

Non-accrual Loans

Loans are placed on non-accrual when it has been determined that all contractual principal and interest will not be received. Any payments received on these loans are applied to principal first and then to interest only after all principal has been collected. Impaired loans include all loans in non-accrual status, all troubled debt restructures, all substandard loans that are deemed to be collateral dependent, and other loans that management determines require impairment. In the case of an impaired loan that is still on accrual basis, payments are applied to both principal and interest.

Allowance for Loan Losses

The provision for loan losses is based upon management's estimate of the amount needed to maintain the allowance for loan losses at an adequate level in light of the risk inherent in the loan portfolio. In making the evaluation of the adequacy of the allowance for loan losses, management gives consideration to current economic conditions, statutory examinations of the loan portfolio by regulatory agencies, delinquency information and management's internal review of the loan portfolio. Loans are considered impaired when it is probable that all amounts due will not be collected in accordance with the contractual terms of the loan agreement. The measurement of impaired loans is generally based on the present value of expected future cash flows discounted at the historical effective interest rate, or upon the fair value of the collateral if the loan is collateral-dependent. If the recorded investment in the loan exceeds the measure of fair value, a valuation allowance is established as a component of the allowance for loan losses. Interest payments on impaired loans are typically applied to principal unless collectability of the principal amount is reasonably assured, in which case, interest is recognized on a cash basis. Impaired loans, or portions thereof, are charged off when deemed uncollectible. While management uses the best information available to make evaluations, future adjustments to the allowance may be necessary if conditions differ substantially from the assumptions used in making the evaluations. In addition, regulatory examiners may require the Company to recognize adjustments to the allowance for loan losses based on their judgments about information available to them at the time of their examination.

Decreases in expected cash flows of PCI loans after the acquisition date are recognized by recording an allowance for credit loss. For any significant increases in cash flows expected to be collected, the Company first adjusts any prior recorded allowance for loan and lease losses through a reversal of previously recognized allowance through provision expense, and then increases the amount of accretable yield to be recognized on a prospective basis over the pool's remaining life. Management analyzes these acquired loan pools using various assessments of risk to determine and calculate an expected loss. The expected loss is derived using an estimate of a loss given default based upon the collateral type and/or specific review by loan officers. Trends are reviewed in terms of traditional credit metrics such as accrual status, past due status, and weighted average risk grade of the loans within each of the accounting pools. In addition, the relationship between the change in the unpaid principal balance and change in the fair value mark is assessed to correlate the directional consistency of the expected loss for each pool.

Loans Held for Sale

Mortgage loans originated and intended for sale in the secondary market are classified as held for sale and are carried at the lower of cost or fair value. Upon closing, these loans are sold to mortgage loan investors under pre-arranged terms. Origination fees are recognized upon the sale and are included in non-interest income. Related to the mortgage business, the Company enters into interest rate lock commitments and commitments to sell mortgages to investors. Interest rate lock commitments are used to manage interest rate risk associated with the fixed rate loan commitments, and forward sale commitments are entered into with investors to manage the interest rate risk associated with the customer interest rate lock commitments, both of which are considered derivative financial instruments. The period of time between the issuance of a loan commitment and the closing and sale of the loan generally ranges from 10 to 60 days. Interest rate lock commitments and forward sale commitments are derivative instruments and are carried at fair value. These derivative instruments do not qualify for hedge accounting. The fair value of interest rate lock commitments is based on current secondary market pricing and has been determined to be immaterial. The fair value of the forward sale commitments is based on changes in the value of the commitment, principally because of changes in interest rates, and is included on the consolidated balance sheets in other assets or other liabilities. Changes in fair value for these instruments are reflected in non-interest income on the income statement. Gains and losses from sales of the mortgage loans are recognized when the Company ultimately sells the loans, and such gains and losses are also recorded in non-interest income. The Company does not retain servicing rights of the loans sold and has not included any servicing assets in other assets or recorded any expenses or revenue.

Stock in Federal Home Loan Bank of Atlanta

As a requirement for membership, the Bank invests in stock of the Federal Home Loan Bank of Atlanta ("FHLB"). This investment was carried at cost at December 31, 2019 and 2018. The Company continually monitors the financial strength of the FHLB and evaluates the investment for potential impairment. There can be no assurance that the impact of recent or future legislation on the Federal Home Loan Banks will not cause a decrease in the value of the Bank's investment in FHLB stock.

Other Non-Marketable Securities

Other non-marketable securities are equity instruments that are reported at cost, less any impairment, plus or minus changes resulting from observable price changes in orderly transactions for an identical or similar investment of the same issuer.

Foreclosed Real Estate

Real estate acquired through, or in lieu of, loan foreclosure is recorded at fair value, less the estimated cost to sell, at the date of foreclosure. At foreclosure, any excess of the loan balance over the fair value of the property is charged to the allowance for loan losses. After foreclosure, management periodically performs valuations of the property and adjusts the value down when the carrying value of the property exceeds the estimated net realizable value. Revenue and expenses from operations and changes in the valuation allowance are included in foreclosure-related expense.

Premises and Equipment

Premises and equipment are stated at cost less accumulated depreciation. Depreciation is calculated on the straight-line method over the estimated useful lives of the assets. Estimated useful lives are 40 years for buildings and 3 to 10 years for furniture, fixtures and equipment. Leasehold improvements are amortized over the terms of the respective leases or the estimated useful lives of the improvements, whichever is shorter.

Repairs and maintenance costs are charged to operations as incurred and additions and improvements to premises and equipment are capitalized. Upon sale or retirement, the cost and related accumulated depreciation are removed from the accounts and any gains or losses are reflected in current operations.

Income Taxes

Deferred tax assets and liabilities are recognized for the estimated future tax consequences attributable to differences between the tax basis of assets and liabilities and their carrying amounts for financial reporting purposes. Deferred tax assets are also recognized for operating loss carry-forwards. Deferred tax assets and liabilities are measured using enacted tax rates in effect for the year in which the temporary differences are expected to be recovered or settled. Deferred tax assets are reduced by a valuation allowance if it is more likely than not that the tax benefits will not be realized.

Public law No. 115-97, known as the Tax Cuts and Jobs Act (the "Act"), enacted on December 22, 2017, reduced the U.S. federal corporate tax rate from 35% to 21%. Also on December 22, 2017, the Securities and Exchange Commission issued Staff Accounting Bulletin No. 118 (SAB 118), which provides guidance on accounting for tax effects of the Act. SAB 118 provides a measurement period of up to one year from the enactment date to complete the accounting. Any adjustments during this measurement period will be included in net earnings from continuing operations as an adjustment to income tax expense in the reporting period when such adjustments are determined. Based on the information available and current interpretation of the rules, the Company has made estimates of the impact of the reduction in the corporate tax rate and re-measurement of certain deferred tax assets and liabilities. The provisional amount recorded related to the re-measurement of the Company's deferred tax balance was $2.6 million for 2017. The measurement period expired prior to December 31, 2018. No additional amount related to the re-measurement of the Company's deferred tax balance was recorded prior to the expiration of the measurement period. See **Note L** *Income Taxes* for more information.

Bank Owned Life Insurance

Bank Owned Life Insurance ("BOLI") is carried at its cash surrender value on the balance sheet and is classified as a non-interest-earning asset. Death benefit proceeds received in excess of the policy's cash surrender value are recognized to income. Returns on the BOLI assets are added to the carrying value and included as non-interest income in the consolidated statement of operations. Any receipt of benefit proceeds is recorded as a reduction to the carrying value of the BOLI asset. At December 31, 2019 and 2018, the Company held no loans against its BOLI cash surrender values.

Goodwill

Goodwill represents the cost in excess of the fair value of net assets acquired (including identifiable intangibles) in transactions accounted for as business combinations. Goodwill has an indefinite useful life and is evaluated for impairment annually, or more frequently if events and circumstances indicate that the asset might be impaired. An impairment loss is recognized to the extent that the carrying amount exceeds the asset's fair value. For the 2019 assessment, we performed a qualitative assessment to determine if it was more likely than not that the fair value of our single reporting unit is less than its carrying amount. We concluded that the fair value of our single reporting unit exceeded its carrying amount and that it was not necessary to perform the two-step test pursuant to ASC 350-20. Our qualitative assessment considered many factors including, but not limited to, our actual and projected operating performance and profitability, as well as consideration of recent bank merger and acquisition transaction metrics. No impairment was indicated in 2019, 2018 or 2017.

In January 2017, the FASB ASU 2017-04, *Intangibles - Goodwill and Other (Topic 350):Simplifying the Test for Goodwill Impairment,* was amended to simplify the accounting for goodwill impairment for public business entities and other entities that have goodwill reported in their financial statements and have not elected the private company alternative for the subsequent measurement of goodwill. The amendment removes Step 2 of the goodwill impairment test. A goodwill impairment will now be the amount by which a reporting unit's carrying value exceeds its fair value, not to exceed the carrying amount of goodwill. The effective date and transition requirements for the technical corrections will be effective for the Company for reporting periods beginning after December 15, 2019. Early adoption is permitted for interim or annual

goodwill impairment tests performed on testing dates after January 1, 2017. The Company will adopt the standard for reporting periods beginning after December 15, 2019 and does not expect these amendments to have a material effect on its financial statements.

Core Deposit Intangible

The Company considers its core deposits to be intangible assets with finite lives. Core deposit intangibles are being amortized using the effective interest method over six years.

Derivative Financial Instruments

The Company utilizes interest rate lock commitments, which are considered derivative instruments, in its mortgage banking operations. As of December 31, 2019, the amount of interest rate lock commitments is considered immaterial.

Stock-Based Compensation

The Company has certain stock-based employee compensation plans, described more fully in **Note P**. Generally accepted accounting principles ("GAAP") require recognition of the cost of employee services received in exchange for an award of equity instruments in the financial statements over the period the employee is required to perform the services in exchange for the award (usually the vesting period). GAAP also requires the compensation cost for all awards granted after the date of adoption and any unvested awards that remained outstanding as of the date of adoption to be measured based on the fair value of the award on the grant date.

Comprehensive Income

The Company reports as comprehensive income all changes in shareholders' equity during the year from sources other than shareholders. Other comprehensive income refers to all components (revenues, expenses, gains, and losses) of comprehensive income that are excluded from net income. The Company's only component of other comprehensive income is unrealized gains and losses on investment securities available for sale.

Segment Information

The Company follows the provisions of ASC 280, *Segment Reporting,* which specifies guidelines for determining an entity's operating segments and the type and level of financial information to be disclosed. Based on these guidelines, management has determined that the Bank operates as a single business segment; the providing of general commercial and retail financial services to customers located in the Company's market areas. The various products, as well as the methods used to distribute them, are those generally offered by community banks.

Net Income per Common Share and Common Shares Outstanding

Basic earnings per share represents income available to common shareholders divided by the weighted-average number of common shares outstanding during the period. Diluted earnings per share reflect additional common shares that would have been outstanding if dilutive potential common shares had been issued, as well as any adjustment to income that would result from the assumed issuance. Potential common shares that may be issued by the Company relate to outstanding stock options. Basic and diluted net income per share have been computed based upon net income as presented in the accompanying Statements of Operations divided by the weighted average number of common shares outstanding or assumed to be outstanding as summarized below:

	2019	2018	2017
Weighted average number of common shares used in computing basic net income per share	19,016,808	15,812,585	11,763,050
Effect of dilutive stock options	46,429	65,048	63,927
Weighted average number of common shares and dilutive potential common shares used in computing diluted net income per share	19,063,237	15,877,633	11,826,977

At December 31, 2019, 2018 and 2017, there were 176,600, 122,300 and 121,300 anti-dilutive options, respectively.

Recent Accounting Pronouncements

The following summarizes recent accounting pronouncements and their expected impact on the Company:

In February 2016, the FASB issued Accounting Standards Update ("ASU") 2016-02, *Leases* (Topic 842). ASU 2016-02 applies a right-of-use ("ROU") model that requires a lessee to record, for all leases with a lease term of more than 12 months, an asset representing its right to use the underlying asset and a liability to make lease payments. For leases with a term of 12 months or less, a practical expedient is available whereby a lessee may elect, by class of underlying asset, not to recognize an ROU asset or lease liability. At inception, lessees must classify all leases as either finance or operating based on five criteria. Balance sheet recognition of finance and operating leases is similar, but the pattern of expense recognition in the income statement, as well as the effect on the statement of cash flows, differs depending on the lease classification. For public business entities, the amendments in ASU 2016-02 are effective for interim and annual periods beginning after December 15, 2018. The Company adopted this standard during the first quarter of 2019. The impact was an increase to the Consolidated Balance Sheet for ROU assets and associated lease liabilities, as well as resulting depreciation expense of the ROU assets and expense of the lease liabilities in the Consolidated Statements of Income. Additionally, adding these assets to the balance sheet impacted total risk-weighted assets used to determine the regulatory capital levels.

In July 2018, the FASB amended the Leases Topic of the Accounting Standards Codification to make narrow amendments to clarify how to apply certain aspects of the new standard. The amendments are effective for reporting periods beginning after December 15, 2018.

The Company elected to apply ASU 2016-02 as of the beginning of the period of adoption (January 1, 2019) and will not restate comparative periods. Adoption of ASU 2016-02 resulted in the recognition of lease liabilities totaling $9,013,900 and the recognition of ROU assets totaling $9,013,900 as of the date of adoption. The adoption of this standard did not impact beginning retained earnings. Total risk-based capital was adversely impacted by 13 basis points due to the increase in risk-weighted assets, see Note J. Lease liabilities and ROU assets are reflected in other liabilities and other assets, respectively. The initial balance sheet gross up upon adoption was primarily related to operating leases of certain real estate properties. The Company has a finance lease and no material subleases or leasing arrangements for which it is the lessor of property or equipment. The Company has elected to apply the package of practical expedients allowed by the new standard under which the Company need not reassess whether any expired or existing contracts are leases or contain leases, the Company need not reassess the lease classification for any expired or existing lease, and the Company need not reassess initial direct costs for any existing leases.

In June 2016, the FASB issued ASU 2016-13, *Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments,* guidance to change the accounting for credit losses and modify the impairment model for certain debt securities. ASU 2016-13 requires an entity to utilize a new impairment model known as the current expected credit loss ("CECL") model to estimate its lifetime "expected credit loss" and record an allowance that, when deducted from the amortized cost basis of the financial asset, presents the net amount expected to be collected on the financial asset. The CECL model is expected to result in earlier recognition of credit losses. ASU 2016-13 also requires new disclosures for financial assets measured at amortized cost, loans and available-for-sale debt securities. The updated guidance is effective for interim and annual reporting periods beginning after December 15, 2019, including interim periods within those fiscal years. Early adoption is permitted. Entities will apply the standard's provisions as a cumulative-effect adjustment to retained earnings as of the beginning of the first reporting period in which the guidance is adopted. On October 16, 2019, the FASB voted to delay implementation of CECL until January 2023 for certain companies, including smaller reporting companies (as defined by the SEC). The Company currently qualifies as a smaller reporting company and is still assessing the impact that this new guidance will have on its consolidated financial statements.

In August 2018, the FASB amended ASU 2018-13 - *Fair Value Measurement (Topic 820): Disclosure Framework - Changes to the Disclosure Requirements for Fair Value Measurement* topic of the Accounting Standards Codification. The amendments remove, modify, and add certain fair value disclosure requirements based on the concepts in the FASB Concepts Statement, *Conceptual Framework for Financial Reporting—Chapter 8: Notes to Financial Statements*. The amendments are effective for all entities for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019. Early adoption is permitted. An entity is permitted to early adopt any removed or modified disclosures upon issuance of this ASU and delay adoption of the additional disclosures until their effective date. The Company does not expect these amendments to have a material effect on its consolidated financial statements.

From time to time, the FASB issues exposure drafts for proposed statements of financial accounting standards. Such exposure drafts are subject to comment from the public, to revisions by the FASB and to final issuance by the FASB as statements of financial accounting standards. Management considers the effect of the proposed statements on the consolidated financial statements of the Company and monitors the status of changes to and proposed effective dates of exposure drafts.

NOTE C – BUSINESS COMBINATIONS

On July 20, 2017, the Company executed a merger agreement with Premara Financial, Inc. ("Premara"), a bank holding company headquartered in Charlotte, North Carolina, whose wholly owned subsidiary, Carolina Premier Bank, was a North Carolina state-chartered commercial bank. On December 15, 2017, the Company completed its previously announced acquisition of Premara and pursuant to the terms of the merger agreement, Premara was merged with and into the Company, followed immediately by the merger of Carolina Premier Bank with and into the Bank. Carolina Premier had approximately $279.6 million in assets as of the merger date, December 15, 2017. The merger expanded the Bank's North Carolina presence with a branch in Charlotte and marked the Bank's initial entry into South Carolina with the acquisition of branches in Rock Hill, Blacksburg and Six Mile, South Carolina. During 2019 the Bank sold the Six Mile location to another financial institution.

Premara had 3,179,808 shares of common stock outstanding as of the merger closing date. Under the terms of the merger agreement, 948,080 shares of Premara common stock (equivalent to 30% of Premara's outstanding shares of common stock as of the date of the merger agreement) were converted to the $12.65 per share cash merger consideration, for aggregate cash consideration of $11,993,212 (exclusive of cash paid-in-lieu of fractional shares) which was paid out subsequent to year-end 2017. Pursuant to the merger agreement, each warrant or stock option to acquire shares of Premara common stock issued and outstanding as of the effective time of the merger was converted into the right to receive from the Company a cash payment equal to $12.65 less the exercise price of such warrant or option, as applicable and paid out prior to year-end 2017. The remaining 2,231,728 Premara common shares were converted into stock consideration at the merger exchange ratio of 1.0463 shares of Company common stock for each share of Premara common stock, resulting in the issuance of 2,334,999 new shares of Company common stock. The transaction was valued at approximately $40.6 million in the aggregate based on 3,179,808 shares of Premara common stock outstanding on December 15, 2017. The Premara common stock shares converted to Select common stock were valued at $12.14 per share, the low price of Select common stock on December 15, 2017.

The merger with Premara was accounted for under the acquisition method of accounting with the Company as the legal and accounting acquirer and Premara as the legal and accounting acquiree. The assets and liabilities of Premara, as of the effective date of the acquisition, are recorded at their respective fair values. For the acquisition of Premara, estimated fair values of assets acquired and liabilities assumed are based on the information that is available, and the Company believes this information provides a reasonable basis for determining fair values.

The following table provides the carrying value of acquired assets and assumed liabilities, as recorded by the Company, the fair value adjustments calculated at the time of the merger and the resulting fair value recorded by the Company.

	December 15, 2017		
	As recorded by Premara	Fair Value adjustments	As recorded by the Company
(Dollars in thousands)			
Assets			
Cash and cash equivalents	$ 28,513	$ -	$ 28,513
Investment securities	32,939	(106)	32,833
Loans	203,780	(5,340)	198,440
Less: allowance for loan losses	(2,341)	2,341	-
Premises and equipment	928	(233)	695
Accrued interest receivable	853	(56)	797
Bank owned life insurance	5,673	-	5,673
Goodwill	325	(325)	-
Core deposit intangible	223	2,477	2,700
Other assets	8,701	790	9,491
Total assets acquired	$ 279,594	$ (452)	$ 279,142
Liabilities			
Deposits:			
Noninterest-bearing	$ 55,617	$ -	$ 55,617
Interest-bearing	170,873	171	171,044
Total deposits	226,490	171	226,661
Borrowings	29,000	14	29,014
Other liabilities	747	-	747
Total liabilities assumed	$ 256,237	$ 185	$ 256,422
Fair value of net assets assumed			22,720
Value of common shares of Premara shareholders			40,693
Goodwill recorded for Premara			$ 17,973

Goodwill recorded for Premara represents future revenues to be derived from the existing customer base, including efficiencies that will result from combining operations.

In determining the acquisition date fair value of purchased credit-impaired ("PCI") loans, and in subsequent accounting, the Company generally aggregates loans into pools of loans with common risk characteristics. Expected cash flows at the acquisition date in excess of the fair value of loans are referred to as the "accretable yield" and recorded as interest income prospectively.

PCI loans acquired totaled $8.6 million at estimated fair value and acquired performing loans totaling $189.6 million at estimated fair value. For PCI loans acquired from Premara, the contractually required payments including principal and interest, cash flows expected to be collected and fair values as of the closing date of the merger were:

(Dollars in thousands)	December 15, 2017
Contractually required payments	$ 11,752
Nonaccretable difference	1,768
Cash flows expected to be collected	9,984
Accretable yield	1,392
Fair value at acquisition date	$ 8,592

Merger-related expense in 2019, 2018 and 2017 totaled 406,000, $ 1.8 million and $2.2 million, respectively which were recorded as noninterest expense as incurred.

NOTE D - INVESTMENT SECURITIES

The amortized cost and fair value of available for sale ("AFS") investments, with gross unrealized gains and losses, follow:

	December 31, 2019			
	Amortized cost	Gross unrealized gains	Gross unrealized losses	Fair value
	(dollars in thousands)			
Securities available for sale:				
U.S. government agencies – GSE's	$ 9,839	$ 159	$ (2)	$ 9,996
Mortgage-backed securities – GSE's	46,926	830	(13)	47,743
Corporate bonds	2,282	17	-	2,299
Municipal bonds	12,152	177	-	12,329
	$ 71,199	$ 1,183	$ (15)	$ 72,367

	December 31, 2018			
	Amortized cost	Gross unrealized gains	Gross unrealized losses	Fair value
	(dollars in thousands)			
Securities available for sale:				
U.S. government agencies – GSE's	$ 9,852	$ 36	$ (51)	$ 9,837
Mortgage-backed securities – GSE's	23,150	62	(229)	22,983
Corporate bonds	1,697	25	-	1,722
Municipal bonds	16,910	105	(24)	16,991
	$ 51,609	$ 228	$ (304)	$ 51,533

Securities with a carrying value of $18.4 million and $6.4 million at December 31, 2019 and 2018, respectively, were pledged to secure public monies on deposit as required by law, customer repurchase agreements, and access to the Federal Reserve Discount Window.

The following tables show gross unrealized losses and fair value, aggregated by investment category and length of time that the individual securities have been in a continuous unrealized loss position as of December 31, 2019 and 2018.

	2019					
	Less Than 12 Months		12 Months or More		Total	
	Fair value	Unrealized losses	Fair value	Unrealized losses	Fair value	Unrealized losses
	(dollars in thousands)					
Securities available for sale:						
U.S. government agencies – GSE's	$ 872	$ -	$ 621	$ (2)	$ 1,493	$ (2)
Mortgage-backed securities-GSE's	2,672	(3)	3,774	(10)	6,446	(13)
Corporate bonds	-	-	-	-	-	-
Municipal bonds	-	-	-	-	-	-
Total temporarily impaired securities	$ 3,544	$ (3)	$ 4,395	$ (12)	$ 7,939	$ (15)

At December 31, 2019, the Company had two AFS mortgage-backed GSE's and one U.S Government agency – GSE with an unrealized loss for twelve or more consecutive months totaling $12,000. The Company had three AFS securities with a loss for twelve months or less. One U.S. government agency GSE and two mortgage-backed GSE's had unrealized losses for less than twelve months totaling $3,000 at December 31, 2019. All unrealized losses are attributable to the general trend of interest rates

	2018					
	Less Than 12 Months		12 Months or More		Total	
	Fair value	Unrealized losses	Fair value	Unrealized losses	Fair value	Unrealized losses
	(dollars in thousands)					
Securities available for sale:						
U.S. government agencies – GSE's	$ 1,224	$ (6)	$ 4,086	$ (45)	$ 5,310	$ (51)
Mortgage-backed securities-GSE's	200	-	16,932	(229)	17,132	(229)
Corporate bonds	-	-	-	-	-	-
Municipal bonds	1,007	(2)	1,740	(22)	2,747	(24)
Total temporarily impaired securities	$ 2,431	$ (8)	$ 22,758	$ (296)	$ 25,189	$ (304)

At December 31, 2018, the Company had twenty-four AFS mortgage-backed GSE's, four municipals and six U.S Government agencies – GSE's with an unrealized loss for twelve or more consecutive months totaling $296,000. The Company had six AFS securities with a loss for twelve months or less. Three U.S. government agency GSE's, two municipals and one mortgage-backed GSE had unrealized losses for less than twelve months totaling $8,000 at December 31, 2018. All unrealized losses are attributable to the general trend of interest rates.

Since none of the unrealized losses relate to the liquidity of the securities or the issuer's ability to honor redemption obligations and the Company has the intent and ability to hold these securities to recovery, no other than temporary impairments were identified for these investments having unrealized losses for the periods ended December 31, 2019 and December 31, 2018. In 2019, the Company realized gains of $48,000 on proceeds of $1.1 million related to the disposal of two securities; in 2018, the Company did not sell any securities; and in 2017 the Company realized net gains of $1,000 on proceeds of $22.0 million related to the disposal of fifty one securities.

The following table sets forth certain information regarding the amortized costs, carrying values and contractual maturities of the Company's investment portfolio at December 31, 2019.

	Amortized Cost	Fair Value
	(dollars in thousands)	
Securities available for sale:		
U.S. government agencies – GSE's		
Due within one year	$ 122	$ 123
Due after one but within five years	7,517	7,620
Due after five but within ten years	1,855	1,909
Due after ten years	345	344
	9,839	9,996
Mortgage-backed securities – GSE's		
Due within one year	4,455	4,449
Due after one but within five years	33,217	33,802
Due after five but within ten years	710	719
Due after ten years	8,544	8,773
	46,926	47,743
Corporate bonds		
Due within one year	276	280
Due after one but within five years	-	-
Due after five but within ten years	1,256	1,269
Due after ten years	750	750
	2,282	2,299
Municipal bonds		
Due within one year	4,048	4,062
Due after one but within five years	220	220
Due after five but within ten years	747	764
Due after ten years	7,137	7,283
	12,152	12,329
Total securities available for sale		
Due within one year	8,901	8,914
Due after one but within five years	40,954	41,642
Due after five but within ten years	4,568	4,661
Due after ten years	16,776	17,150
	$ 71,199	$ 72,367

For purposes of the maturity table, mortgage-backed securities, which are not due at a single maturity date, have been allocated over maturity groupings based on the weighted-average contractual maturities of underlying collateral. The mortgage-backed securities may mature earlier than their weighted-average contractual maturities because of principal prepayments.

NOTE E - LOANS

The following is a summary of loans at December 31, 2019 and 2018:

	2019		2018	
	Amount	Percent of total	Amount	Percent of total
	(dollars in thousands)			
Real estate loans:				
1-to-4 family residential	$ 151,697	14.73%	$ 159,597	16.19%
Commercial real estate	459,115	44.58%	457,611	46.41%
Multi-family residential	69,124	6.71%	63,459	6.44%
Construction	221,878	21.55%	170,404	17.28%
Home equity lines of credit (“HELOC”)	44,514	4.32%	49,713	5.04%
Total real estate loans	946,328	91.89%	900,784	91.36%
Other loans:				
Commercial and industrial	75,748	7.35%	74,181	7.52%
Loans to individuals	9,779	0.95%	12,597	1.28%
Overdrafts	234	0.02%	217	0.02%
Total other loans	85,761	8.32%	86,995	8.82%
Gross loans	1,032,089		987,779	
Less deferred loan origination fees, net	(2,114)	(.18)%	(1,739)	(.18)%
Total loans	1,029,975	100.00%	986,040	100.00%
Allowance for loan losses	(8,324)		(8,669)	
Total loans, net	$ 1,021,651		$ 977,371	

Loans are primarily made in central and eastern North Carolina, southeast Virginia and northwest South Carolina. Real estate loans can be affected by the condition of the local real estate market and can be affected by the local economic conditions.

At December 31, 2019, the Company had pre-approved but unused lines and letters of credit totaling $234.2 million. In management’s opinion, these commitments, and undisbursed proceeds on loans reflected above, represent no more than normal lending risk to the Company and will be funded from normal sources of liquidity.

A description of the various loan products provided by the Bank is presented below.

Residential 1-to-4 Family Loans

Residential 1-to-4 family loans are mortgage loans that typically convert from construction loans into permanent financing and are secured by properties within the Bank's market areas.

Commercial Real Estate Loans

Commercial real estate loans are underwritten based on the borrower's ability to generate adequate cash flow to repay the subject debt within reasonable terms. Commercial real estate loans typically include both owner and non-owner occupied properties with higher principal loan amounts and the repayment of these loans is generally dependent on the successful management of the property. Commercial real estate loans are sensitive to market and general economic conditions. Repayment analysis must be performed and consists of an identified primary/cash flow source of repayment and a secondary/liquidation source of repayment. The primary source of repayment is cash flow from income generated from rental or lease of the property. However, the cash flow can be supplemented with the borrower's and guarantor's global cash flow position. Other credit issues such as the business fundamentals and financial strength of the borrower/guarantor can be considered in determining adequacy of repayment ability. The secondary source of repayment is liquidation of the collateral, supplemented by liquidation cushion provided by the financial assets of the borrower/guarantor. Management monitors and evaluates commercial real estate loans based on collateral, market area, and risk grade.

Multi-family Residential Loans

Multi-family residential loans are typically nonfarm properties with 5 or more dwelling units in structures which include apartment buildings used primarily to accommodate households on a more or less permanent basis. Successful performance of these types of loans is primarily dependent on occupancy rates, rental rates, and property management.

Construction Loans

Construction loans are non-revolving extensions of credit secured by real property of which the proceeds are used to acquire and develop land and to construct commercial or residential buildings. The primary source of repayment for these types of loans is the sale of the improved property or permanent financing in which case the property is expected to generate the cash flow necessary for repayment on a permanent loan basis. Property cash flow may be supplemented with financial support from the borrowers/guarantors. Proper underwriting of a construction loan consists of the initial process of obtaining, analyzing, and approving various aspects of information pertaining to: the analysis of the permanent financing source, creditworthiness of the borrower and guarantors, ability of contractor to perform under the terms of the contract, and the feasibility, marketability, and valuation of the project.

Also, consideration is given to the cost of the project and sources of funds needed to complete construction as well as identifying any sources of equity funding. Construction loans are traditionally considered to be higher risk loans involving technical and legal requirements inherently different from other types of loans; however with thorough credit underwriting, proper loan structure, and diligent loan servicing, these risks can be mitigated. Some examples of risks inherent in this type of lending include: underestimated costs, inflation of material and labor costs, site difficulties (i.e. rock, soil), project not built to plans, weather delays and natural disasters, borrower/contractor/subcontractor disputes which prompt liens, and interest rates increasing beyond budget.

Home Equity Lines of Credit

Home equity lines of credit are consumer-purpose revolving extensions of credit which are secured by first or second liens on owner-occupied residential real estate. Appropriate risk management and compliance practices are exercised to ensure that loan-to-value, lien perfection, and compliance risks are addressed and managed within the Bank's established guidelines. The degree of utilization of revolving commitments within this loan segment is reviewed periodically to identify changes in the behavior of this borrowing group.

Commercial and Industrial Loans

Commercial and industrial loans are underwritten after evaluating and understanding the borrower's ability to generate positive cash flow, operate profitably and prudently expand its business. Underwriting standards are designed to promote relationships to include a full range of loan, deposit, and cash management services. Commercial and industrial loans are primarily made based on the identified cash flows of the borrower and secondarily on the underlying collateral provided by the borrower and the guarantors. The cash flows of the borrower, however, may not be as expected and the collateral securing these loans may fluctuate in value. In the case of loans secured by accounts receivable, the availability of funds for repayment can be impacted by the borrower's ability to collect amounts due from its customers.

Loans to Individuals

Consumer loans are approved using Bank policies and procedures established to evaluate each credit request. All lending decisions and credit risks are clearly documented. Several factors are considered in making these decisions such as credit score, adjusted net worth, liquidity, debt ratio, disposable income, credit history, and loan-to-value of the collateral. This process, combined with the relatively smaller loan amounts, spreads the risk among many individual borrowers.

Overdrafts

Overdrafts on customer accounts are classified as loans for reporting purposes.

Non-Accrual and Past Due Loans

The following tables present as of December 31, 2019 and 2018 an age analysis of past due loans, segregated by class of loans:

	December 31, 2019						
	30-59 Days Past Due	60-89 Days Past Due	90+ Days Accruing	Non-Accrual Loans	Total Past Due	Current	Total Loans
	(dollars in thousands)						
Total loans							
Commercial and industrial	$ 1,108	$ 34	$ 46	$ 2,824	$ 4,012	$ 71,736	$ 75,748
Construction	-	-	-	181	181	221,697	221,878
Multi-family residential	-	-	-	-	-	69,124	69,124
Commercial real estate	393	82	321	1,832	2,628	456,487	459,115
Loans to individuals & overdrafts	5	-	-	155	160	9,853	10,013
1-to-4 family residential	859	810	864	505	3,038	148,659	151,697
HELOC	168	-	-	444	612	43,902	44,514
Deferred loan (fees) cost, net	-	-	-	-	-	-	(2,114)
	$ 2,533	$ 926	$ 1,231	$ 5,941	$ 10,631	$ 1,021,458	$ 1,029,975
Loans- PCI							
Commercial and industrial	$ -	$ -	$ 46	$ -	$ 46	$ 1,057	$ 1,103
Construction	-	-	-	-	-	677	677
Multi-family residential	-	-	-	-	-	897	897
Commercial real estate	-	-	321	-	321	5,449	5,770
Loans to individuals & overdrafts	-	-	-	-	-	-	-
1-to-4 family residential	-	-	864	-	864	6,354	7,218
HELOC	-	-	-	-	-	48	48
	$ -	$ -	$ 1,231	$ -	$ 1,231	$ 14,482	$ 15,713
Loans- excluding PCI							
Commercial and industrial	$ 1,108	$ 34	$ -	$ 2,824	$ 3,966	$ 70,679	$ 74,645
Construction	-	-	-	181	181	221,020	221,201
Multi-family residential	-	-	-	-	-	68,227	68,227
Commercial real estate	393	82	-	1,832	2,307	451,038	453,345
Loans to individuals & overdrafts	5	-	-	155	160	9,853	10,013
1-to-4 family residential	859	810	-	505	2,174	142,305	144,479
HELOC	168	-	-	444	612	43,854	44,466
Deferred loan (fees) cost, net	-	-	-	-	-	-	(2,114)
	$ 2,533	$ 926	$ -	$ 5,941	$ 9,400	$ 1,006,976	$ 1,014,262

Non-Accrual and Past Due Loans

	December 31, 2018						
	30-59 Days Past Due	60-89 Days Past Due	90+ Days Accruing	Non-Accrual Loans	Total Past Due	Current	Total Loans
	(dollars in thousands)						
Total loans							
Commercial and industrial	$ 27	$ 203	$ 1,665	$ 4,170	$ 6,065	$ 68,116	$ 74,181
Construction	-	-	69	587	656	169,748	170,404
Multi-family residential	-	-	-	-	-	63,459	63,459
Commercial real estate	103	483	-	1,074	1,660	455,951	457,611
Loans to individuals & overdrafts	1	24	-	-	25	12,789	12,814
1-to-4 family residential	502	505	1,433	386	2,826	156,771	159,597
HELOC	-	43	-	1,040	1,083	48,630	49,713
Deferred loan (fees) cost, net	-	-	-	-	-	-	(1,739)
	$ 633	$ 1,258	$ 3,167	$ 7,257	$ 12,315	$ 975,464	$ 986,040
Loans- PCI							
Commercial and industrial	$ -	$ -	$ 1,665	$ -	$ 1,665	$ 99	$ 1,764
Construction	-	-	69	-	69	682	751
Multi-family residential	-	-	-	-	-	937	937
Commercial real estate	-	-	-	-	-	7,579	7,579
Loans to individuals & overdrafts	-	-	-	-	-	-	-
1-to-4 family residential	-	-	1,433	-	1,433	6,755	8,188
HELOC	-	-	-	-	-	49	49
	$ -	$ -	$ 3,167	$ -	$ 3,167	$ 16,101	$ 19,268
Loans- excluding PCI							
Commercial and industrial	$ 27	$ 203	$ -	$ 4,170	$ 4,400	$ 68,017	$ 72,417
Construction	-	-	-	587	587	169,066	169,653
Multi-family residential	-	-	-	-	-	62,522	62,522
Commercial real estate	103	483	-	1,074	1,660	448,372	450,032
Loans to individuals & overdrafts	1	24	-	-	25	12,789	12,814
1-to-4 family residential	502	505	-	386	1,393	150,016	151,409
HELOC	-	43	-	1,040	1,083	48,581	49,664
Deferred loan (fees) cost, net	-	-	-	-	-	-	(1,739)
	$ 633	$ 1,258	$ -	$ 7,257	$ 9,148	$ 959,363	$ 966,772

There were six loans in the aggregate amount of $1.2 million greater than 90 days past due and still accruing interest at December 31, 2019 and there were seventeen loans in the aggregate amount of $3.2 million greater than 90 days past due and still accruing interest at December 31, 2018. All loans greater than 90 days past due and still accruing are acquired loans that are considered past due rather than non-accrual loans due to the accounting treatment of acquired loans. In accordance with the ASC 310-20 guidance, if the loan pays differently than contractually required, than an adjustment to the discount premium is made in order to maintain the same effective interest rate.

Impaired Loans

The following tables present information on loans, excluding PCI loans and loans evaluated collectively as a homogenous group, that were considered to be impaired as of December 31, 2019 and December 31, 2018:

				December 31, 2019 Year to Date	
	Recorded Investment	Contractual Unpaid Principal Balance	Related Allowance for Loan Losses	Average Recorded Investment	Interest Income Recognized on Impaired Loans
		(dollars in thousands)			
2019:					
With no related allowance recorded:					
Commercial and industrial	$ 2,796	$ 4,051	$ -	$ 4,186	$ 122
Construction	440	537	-	500	26
Commercial real estate	5,585	6,750	-	5,632	272
Loans to individuals & overdrafts	284	293	-	193	12
Multi-family residential	197	197	-	206	13
HELOC	543	678	-	793	36
1-to-4 family residential	395	1,816	-	1,204	86
Subtotal:	10,240	14,322	-	12,714	567
With an allowance recorded:					
Commercial and industrial	731	1,056	403	572	41
Construction	-	-	-	13	-
Commercial real estate	-	-	-	-	-
Loans to individuals & overdrafts	-	-	-	-	-
Multi-family Residential	-	-	-	-	-
HELOC	160	222	-	212	10
1-to-4 family residential	81	94	10	563	7
Subtotal:	972	1,372	413	1,360	58
Totals:					
Commercial	9,749	12,591	403	11,109	474
Consumer	284	293	-	193	12
Residential	1,179	2,810	10	2,772	139
Grand Total:	$ 11,212	$ 15,694	$ 413	$ 14,074	$ 625

Impaired loans at December 31, 2019 were approximately $11.2 million and included $5.9 million in non-accrual loans and $6.2 million in loans still in accruing status. Recorded investment represents the current principal balance for the loan. Approximately $972,000 of the $11.2 million in impaired loans at December 31, 2019 had specific allowances aggregating $413,000 while the remaining $10.2 million had no specific allowances recorded. Of the $10.2 million with no allowance recorded, partial charge-offs through December 31, 2019 amounted to $4.1 million.

				December 31, 2018 Year to Date	
	Recorded Investment	Contractual Unpaid Principal Balance	Related Allowance for Loan Losses	Average Recorded Investment	Interest Income Recognized on Impaired Loans
			(dollars in thousands)		
2018:					
With no related allowance recorded:					
Commercial and industrial	$ 4,210	$ 4,495	$ -	$ 2,899	$ 229
Construction	561	647	-	473	16
Commercial real estate	4,744	6,903	-	5,053	372
Loans to individuals & overdrafts	101	109	-	51	9
Multi-family residential	215	215	-	225	15
HELOC	1,040	1,204	-	884	50
1-to-4 family residential	572	732	-	1,169	79
Subtotal:	11,443	14,305	-	10,754	770
With an allowance recorded:					
Commercial and industrial	127	325	51	234	13
Construction	27	27	14	13	-
Commercial real estate	-	-	-	-	-
Loans to individuals & overdrafts	-	-	-	-	-
Multi-family Residential	-	-	-	-	-
HELOC	-	-	-	-	-
1-to-4 family residential	137	555	22	374	23
Subtotal:	291	907	87	621	36
Totals:					
Commercial	10,007	12,612	65	8,897	645
Consumer	101	109	-	51	9
Residential	1,626	2,491	22	2,427	152
Grand Total:	$ 11,734	$ 15,212	$ 87	$ 11,375	$ 806

Impaired loans at December 31, 2018 were approximately $11.7 million and were comprised of $7.3 million in non-accrual loans and $4.4 million in loans still in accruing status. Recorded investment represents the current principal balance for the loan. Approximately $291,000 of the $11.7 million in impaired loans at December 31, 2018 had specific allowances aggregating $87,000 while the remaining $11.4 million had no specific allowances recorded. Of the $11.4 million with no allowance recorded, partial charge-offs through December 31, 2018 amounted to $3.5 million.

Troubled Debt Restructurings

The following tables present loans that were modified as troubled debt restructurings ("TDRs") within the previous twelve months with a breakdown of the types of concessions made by loan class during the twelve months ended December 31, 2019 and 2018:

	Twelve Months Ended December 31, 2019		
	Number of loans	Pre-Modification Outstanding Recorded Investments	Post-Modification Outstanding Recorded Investments
		(dollars in thousands)	
Extended payment terms:			
Commercial and industrial	6	$ 2,535	$ 2,380
Commercial real estate	1	752	687
Construction	1	260	259
1-to-4 family residential	3	232	208
Total	11	$ 3,779	$ 3,534

As noted in the tables above, there were eleven loans that were considered TDRs during the year ended December 31, 2019, for reasons due to extended terms. These loans were renewed at terms that vary from those that the Company would enter into for new loans of this type.

	Twelve Months Ended December 31, 2018		
	Number of loans	Pre-Modification Outstanding Recorded Investments	Post-Modification Outstanding Recorded Investments
		(dollars in thousands)	
Extended payment terms:			
Commercial and industrial	6	$ 1,579	$ 1,517
Commercial real estate	3	1,283	895
1-to-4 family residential	1	409	389
Total	10	$ 3,271	$ 2,801

As noted in the tables above, there were ten loans that were considered TDRs during the year ended December 31, 2018, for reasons due to extended terms. These loans were renewed at terms that vary from those that the Company would enter into for new loans of this type.

The following tables present loans that were modified as TDRs within the previous twelve months for which there was a payment default together with a breakdown of the types of concessions made by loan class during the twelve months ended December 31, 2019 and 2018:

	Twelve months ended December 31, 2019		
	Number of loans		Recorded investment
	(dollars in thousands)		
Extended payment terms:			
Commercial and industrial	2	$	1,566
Total	2	$	1,566

	Twelve months ended December 31, 2018		
	Number of loans		Recorded investment
	(dollars in thousands)		
Extended payment terms:			
Commercial and industrial	4	$	1,036
Commercial real estate	1		334
Total	5	$	1,370

At December 31, 2019, the Company had forty-two loans with an aggregate balance of $9.4 million that were considered to be troubled debt restructurings. Of those TDRs, twenty-eight loans with a balance totaling $6.2 million were still accruing as of December 31, 2019. The remaining fourteen TDRs with a balance totaling $3.2 million were in non-accrual status. All TDRs are included in non-performing assets and impaired loans.

At December 31, 2018, the Company had thirty-six loans with an aggregate balance of $6.9 million that were considered to be troubled debt restructurings. Of those TDRs, twenty loans with a balance totaling $4.4 million were still accruing as of December 31, 2018. The remaining sixteen TDRs with a balance totaling $2.5 million were in non-accrual status. All TDRs are included in non-performing assets and impaired loans.

Credit Quality Indicators

As part of the on-going monitoring of the credit quality of the loan portfolio, management utilizes a risk grading matrix to assign a risk grade to each of the Company's loans. All non-consumer loans are graded on a scale of 1 to 9. A description of the general characteristics of these nine different risk grades is as follows:

- Risk Grade 1 (Superior) - Credits in this category are virtually risk-free and are well-collateralized by cash-equivalent instruments. The repayment program is well-defined and achievable. Repayment sources are numerous. No material documentation deficiencies or exceptions exist.

- Risk Grade 2 (Very Good) - This grade is reserved for loans secured by readily marketable collateral, or loans within guidelines to borrowers with liquid financial statements. A liquid financial statement is a financial statement with substantial liquid assets relative to debts. These loans have excellent sources of repayment, with no significant identifiable risk of collection, and conform in all respects to Bank policy, guidelines, underwriting standards, and Federal and State regulations (no exceptions of any kind).

- Risk Grade 3 (Good) - These loans have excellent sources of repayment, with no significant identifiable risk of collection. Generally, loans assigned this risk grade will demonstrate the following characteristics:
  - Conformity in all respects with Bank policy, guidelines, underwriting standards, and Federal and State regulations (no exceptions of any kind).
  - Documented historical cash flow that meets or exceeds required minimum Bank guidelines, or that can be supplemented with verifiable cash flow from other sources.
  - Adequate secondary sources to liquidate the debt, including combinations of liquidity, liquidation of collateral, or liquidation value to the net worth of the borrower or guarantor.

- Risk Grade 4 (Acceptable) - This grade is given to acceptable loans. These loans have adequate sources of repayment, with little identifiable risk of collection. Loans assigned this risk grade will demonstrate the following characteristics:
  - General conformity to the Bank's policy requirements, product guidelines and underwriting standards, with limited exceptions. Any exceptions that are identified during the underwriting and approval process have been adequately mitigated by other factors.
  - Documented historical cash flow that meets or exceeds required minimum Bank guidelines, or that can be supplemented with verifiable cash flow from other sources.
  - Adequate secondary sources to liquidate the debt, including combinations of liquidity, liquidation of collateral, or liquidation value to the net worth of the borrower or guarantor.

- Risk Grade 5 (Acceptable With Care) - This grade is given to acceptable loans that show signs of weakness in either adequate sources of repayment or collateral, but have demonstrated mitigating factors that minimize the risk of delinquency or loss. Loans assigned this grade may demonstrate some or all of the following characteristics:
  - Additional exceptions to the Bank's policy requirements, product guidelines or underwriting standards that present a higher degree of risk to the Bank. Although the combination and/or severity of identified exceptions is greater, all exceptions have been properly mitigated by other factors.
  - Unproven, insufficient or marginal primary sources of repayment that appear sufficient to service the debt at this time. Repayment weaknesses may be due to minor operational issues, financial trends, or reliance on projected (not historic) performance.
  - Marginal or unproven secondary sources to liquidate the debt, including combinations of liquidation of collateral and liquidation value to the net worth of the borrower or guarantor.

- Risk Grade 6 (Watch List or Special Mention) – Loans in this category can have the following characteristics:
  - Loans with underwriting guideline tolerances and/or exceptions and with no mitigating factors.
  - Extending loans that are currently performing satisfactorily but with potential weaknesses that may, if not corrected, weaken the asset or inadequately protect the Bank's position at some future date. Potential weaknesses are the result of deviations from prudent lending practices.
  - Loans where adverse economic conditions that develop subsequent to the loan origination that do not jeopardize liquidation of the debt but do substantially increase the level of risk may also warrant this rating.

- Risk Grade 7 (Substandard) - A Substandard loan is inadequately protected by the current sound net worth and paying capacity of the obligor or of the collateral pledged, if any. Loans classified as Substandard 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. Loans consistently not meeting the repayment schedule should be downgraded to substandard. Loans in this category are characterized by deterioration in quality exhibited by any number of well-defined weaknesses requiring corrective action.

- Risk Grade 8 (Doubtful) - Loans classified Doubtful have all the weaknesses inherent in loans classified Substandard, plus the added characteristic that the weaknesses make collection or liquidation in full on the basis of currently existing facts, conditions, and values highly questionable and improbable. However, these loans are not yet rated as loss because certain events may occur which would salvage the debt.

- Risk Grade 9 (Loss) - Loans classified as Loss are considered uncollectable and of such little value that their continuance as bankable assets is not warranted. This classification does not mean that the asset has absolutely no recovery or salvage value, but rather that it is not practical or desirable to defer writing off the loan even though partial recovery may be affected in the future.

Consumer loans are graded on a scale of 1 to 9. A description of the general characteristics of the 9 risk grades is as follows:

- Risk Grades 1 – 5 (Pass) – The loans in this category range from loans secured by cash with no risk of principal deterioration (Risk Grade 1) to loans that show signs of weakness in either adequate sources of repayment or collateral but have demonstrated mitigating factors that minimize the risk of delinquency or loss (Risk Grade 5).

- Risk Grade 6 (Watch List or Special Mention) - Watch list or Special Mention loans include the following characteristics:

    - Loans within guideline tolerances or with exceptions of any kind that have not been mitigated by other economic or credit factors.
    - Extending loans that are currently performing satisfactorily but with potential weaknesses that may, if not corrected, weaken the asset or inadequately protect the Bank's position at some future date. Potential weaknesses are the result of deviations from prudent lending practices.
    - Loans where adverse economic conditions that develop subsequent to the loan origination that don't jeopardize liquidation of the debt but do substantially increase the level of risk may also warrant this rating.

- Risk Grade 7 (Substandard) - A Substandard loan is inadequately protected by the current sound net worth and paying capacity of the obligor or of the collateral pledged, if any. Loans classified as Substandard must have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt; they are characterized by the distinct possibility that the institution will sustain some loss if the deficiencies are not corrected.

- Risk Grade 8 (Doubtful) - Loans classified Doubtful have all the weaknesses inherent in loans classified Substandard, plus the added characteristic that the weaknesses make collection or liquidation in full on the basis of currently existing facts, conditions, and values highly questionable and improbable. However, these loans are not yet rated as loss because certain events may occur which would salvage the debt.

- Risk Grade 9 (Loss) - Loans classified Loss are considered uncollectable and of such little value that their continuance as bankable assets is not warranted. This classification does not mean that the asset has absolutely no recovery or salvage value, but rather that it is not practical or desirable to defer writing off this worthless loan even though partial recovery may be affected in the future.

The following tables present information on risk ratings of the commercial and consumer loan portfolios, segregated by loan class as of December 31, 2019 and 2018:

Total Loans:

	December 31, 2019			
Commercial Credit Exposure By Internally Assigned Grade	**Commercial and industrial**	**Construction**	**Commercial real estate**	**Multi-family residential**
	(dollars in thousands)			
Superior	$ 4,014	$ -	$ 337	$ -
Very good	349	110	1,245	-
Good	5,976	8,674	62,643	4,839
Acceptable	19,197	16,249	255,751	41,113
Acceptable with care	40,579	196,228	133,190	23,172
Special mention	242	436	1,490	-
Substandard	5,391	181	4,459	-
Doubtful	-	-	-	-
Loss	-	-	-	-
	$ 75,748	$ 221,878	$ 459,115	$ 69,124

Consumer Credit Exposure By Internally Assigned Grade	**1-to-4 family residential**	**HELOC**
Pass	$ 147,958	$ 43,585
Special mention	1,246	76
Substandard	2,493	853
	$ 151,697	$ 44,514

Consumer Credit Exposure Based On Payment Activity	**Loans to individuals & overdrafts**
Pass	$ 9,727
Special mention	286
	$ 10,013

Total Loans:

	December 31, 2018			
Commercial Credit Exposure By Internally Assigned Grade	**Commercial and industrial**	**Construction**	**Commercial real estate**	**Multi-family residential**
		(dollars in thousands)		
Superior	$ 1,662	$ -	$ 21	$ -
Very good	2,266	246	1,120	-
Good	5,773	12,106	47,959	5,116
Acceptable	22,332	30,897	263,017	37,832
Acceptable with care	34,626	125,788	139,484	20,296
Special mention	879	711	1,789	-
Substandard	6,643	656	4,221	215
Doubtful	-	-	-	-
Loss	-	-	-	-
	$ 74,181	$ 170,404	$ 457,611	$ 63,459

Consumer Credit Exposure By Internally Assigned Grade	**1-to-4 family residential**	**HELOC**
Pass	$ 155,117	$ 48,143
Special mention	900	88
Substandard	3,580	1,482
	$ 159,597	$ 49,713

Consumer Credit Exposure Based On Payment Activity	**Loans to individuals & overdrafts**
Pass	$ 10,891
Special mention	1,923
	$ 12,814

The process of determining the allowance for loan losses is driven by the risk grade system and the loss experience on non-risk graded homogeneous types of loans. The Bank’s allowance for loan losses is calculated and determined, at a minimum, each fiscal quarter end. The allowance for loan losses represents management’s estimate of the appropriate level of reserve to provide for probable losses inherent in the loan portfolio. In determining the allowance for loan losses and any resulting provision to be charged against earnings, particular emphasis is placed on the results of the loan review process. Consideration is also given to a review of individual loans, historical loan loss experience, the value and adequacy of collateral and economic conditions in the Bank’s market areas. For loans determined to be impaired, the impairment is based on discounted expected cash flows using the loan’s initial effective interest rate or the fair value of the collateral (less selling costs) for certain collateral dependent loans. This evaluation is inherently subjective as it requires material estimates, including the amounts and timing of future cash flows expected to be received on impaired loans that may be susceptible to significant change. In addition, various regulatory agencies, as an integral part of their examination process, periodically review the Bank’s allowance for loan losses. Such agencies may require the Bank to recognize changes to the allowance based on their judgments about information available to them at the time of their examinations. Loans are charged off when in the opinion of management, they are deemed to be uncollectible. Recognized losses are charged against the allowance, and subsequent recoveries are added to the allowance. The Credit Management Committee of the Board of Directors has responsibility for oversight.

Management believes the allowance for loan losses of $8.3 million at December 31, 2019 is adequate to provide for inherent losses in the loan portfolio; however, assessing the adequacy of the allowance is a process that requires continuous evaluation and considerable judgment. Management's judgments are based on numerous assumptions about current events which it believes to be reasonable, but which may or may not be valid. Thus, there can be no assurance that credit losses in future periods will not exceed the current allowance or that future increases in the allowance will not be required. No assurance can be given that management's ongoing evaluation of the loan portfolio in light of changing economic conditions and other relevant circumstances will not require significant future additions to the allowance, thus adversely affecting future operating results of the Bank.

For PCI loans acquired from Legacy Select and Premara, the contractually required payments including principal and interest, cash flows expected to be collected and fair values as of the closing date of the merger and December 31, 2019 and 2018 were:

	December 31, 2019	December 31, 2018
	(dollars in thousands)	
Contractually required payments	$ 20,598	$ 24,823
Nonaccretable difference	1,694	1,962
Cash flows expected to be collected	18,904	22,861
Accretable yield	3,191	3,593
Fair value	$ 15,713	$ 19,268

The following table documents changes to the amount of the PCI accretable yield as of December 31, 2019 and 2018:

	2019	2018
	(dollars in thousands)	
Accretable yield, beginning of period	$ 3,593	$ 3,307
Additions	-	-
Accretion	(904)	(1,541)
Reclassification from nonaccretable difference	360	576
Other changes, net	142	1,251
Accretable yield, end of period	$ 3,191	$ 3,593

Allowance for Loan Losses

The allowance for loan losses is a reserve established through provisions for loan losses charged to income and represents management's best estimate of probable loan losses inherent within the existing portfolio of loans. The allowance, in the judgment of management, is necessary to reserve for estimated losses and risk inherent in the loan portfolio. The Company's allowance for loan loss methodology is based on historical loss experience by type of credit and internal risk grade, specific homogeneous risk pools and specific loss allocations, with adjustments for current events and conditions. The Company's process for determining the appropriate level of reserves is designed to account for changes in credit quality as they occur. The provision for loan losses reflects loan quality trends, including the levels of, and trends related to, past due loans and economic conditions at the local and national levels. It also considers the quality and risk characteristics of the Company's loan origination and servicing policies and practices.

Individual reserves are calculated according to ASC Section 310-10-35 against loans evaluated individually and deemed to most likely be impaired. Impaired loans include all loans in non-accrual status, all troubled debt restructures, all substandard loans that are deemed to be collateral dependent, and other loans that management determines require reserves.

The Company's allowance for loan losses model calculates historical loss rates using a loss migration analysis associating losses to the risk-graded pool to which they relate for each of the previous twelve quarters. Then, using a twelve quarter look back period, loss factors are calculated for each risk-graded pool.

The model incorporates various internal and external qualitative and environmental factors as described in the Interagency Policy Statement on the Allowance for Loan and Lease Losses, dated December 2006. Input for these factors is determined on the basis of management observation, judgment, and experience. The factors utilized by the Company are as follows:

Internal Factors

- Concentrations – Measures the increased risk derived from concentration of credit exposure in particular industry segments within the portfolio.
- Policy exceptions – Measures the risk derived from granting terms outside of underwriting guidelines.
- Compliance exceptions– Measures the risk derived from granting terms outside of regulatory guidelines.
- Document exceptions– Measures the risk exposure resulting from the inability to collect due to improperly executed documents and collateral imperfections.
- Financial information monitoring – Measures the risk associated with not having current borrower financial information.
- Nonaccrual – Reflects increased risk of loans with characteristics that merit nonaccrual status.
- Delinquency – Reflects the increased risk deriving from higher delinquency rates.
- Personnel turnover – Reflects staff competence in various types of lending.
- Portfolio growth – Measures the impact of growth and potential risk derived from new loan production.

External Factors

- GDP growth rate – Impact of general economic factors that affect the portfolio.
- North Carolina unemployment rate – Impact of local economic factors that affect the portfolio.
- South Carolina unemployment rate – Impact of local economic factors that affect the portfolio.
- Peer group delinquency rate – Measures risk associated with the credit requirements of competitors.
- Prime rate change – Measures the effect on the portfolio in the event of changes in the prime lending rate.

Each pool is assigned an adjustment to the potential loss percentage by assessing its characteristics against each of the factors listed above.

Reserves are generally divided into three allocation segments:

1. Individual reserves. These are calculated according to ASC Section 310-10-35 against loans evaluated individually and deemed to most likely be impaired. All loans in non-accrual status and all substandard loans that are deemed to be collateral dependent are assessed for impairment. Loans are deemed uncollectible based on a variety of credit, collateral, documentation and other issues. In the case of uncollectible receivables, the collateral is considered unsecured and therefore fully charged off.

2. Formula reserves. Formula reserves are held against loans evaluated collectively. Loans are grouped by type or by risk grade, or some combination of the two. Loss estimates are based on historical loss rates for each respective loan group. Formula reserves represent the Company's best estimate of losses that may be inherent, or embedded, within the group of loans, even if it is not apparent at this time which loans within any group or pool represent those embedded losses.

3. Qualitative and external reserves. If individual reserves represent estimated losses tied to specific loans, and formula reserves represent estimated losses tied to a pool of loans but not yet to any specific loan, then these reserves represent an estimate of losses that are likely to be incurred, but are not yet tied to any loan or group of loans.

All information related to the calculation of the three segments, including data analysis, assumptions, and calculations are documented. Assigning specific individual reserve amounts, formula reserve factors, or unallocated amounts based on unsupported assumptions or conclusions is not permitted.

The following tables present a roll forward of the Company's allowance for loan losses by loan segment for the twelve-month periods ended December 31, 2019, 2018 and 2017, respectively (in thousands):

2019	Commercial and industrial	Construction	Commercial real estate	1 to 4 family residential	HELOC	Loans to individuals & overdrafts	Multi-family residential	Total
Allowance for loan losses								
Loans – excluding PCI								
Balance, beginning of period 01/01/2019	$ 762	$ 1,385	$ 3,024	$ 1,663	$ 555	$ 206	$ 471	$ 8,066
Provision for loan losses	1,143	328	(371)	(259)	(169)	152	(52)	772
Loans charged-off	(790)	-	(10)	-	(150)	(206)	-	(1,156)
Recoveries	12	18	194	33	93	23	-	373
Balance, end of period 12/31/2019	$ 1,127	$ 1,731	$ 2,837	$ 1,437	$ 329	$ 175	$ 419	$ 8,055
PCI Loans								
Balance, beginning of period 01/01/2019	$ 214	$ -	$ 385	$ 4	$ -	$ -	$ -	$ 603
Provision for loan losses	(36)	6	(371)	52	-	-	15	(334)
Loans charged-off	-	-	-	-	-	-	-	-
Recoveries	-	-	-	-	-	-	-	-
Balance, end of period 12/31/2019	$ 178	$ 6	$ 14	$ 56	$ -	$ -	$ 15	$ 269
Total Loans								
Balance, beginning of period 01/01/2019	$ 976	$ 1,385	$ 3,409	$ 1,667	$ 555	$ 206	$ 471	$ 8,669
Provision for loan losses	1,107	334	(742)	(207)	(169)	152	(37)	438
Loans charged-off	(790)	-	(10)	-	(150)	(206)	-	(1,156)
Recoveries	12	18	194	33	93	23	-	373
Balance, end of period 12/31/2019	$ 1,305	$ 1,737	$ 2,851	$ 1,493	$ 329	$ 175	$ 434	$ 8,324
Ending Balance: individually evaluated for impairment	$ 403	$ -	$ -	$ 10	$ -	$ -	$ -	$ 413
Ending Balance: collectively evaluated for impairment	$ 902	$ 1,737	$ 2,851	$ 1,483	$ 329	$ 175	$ 434	$ 7,911
Loans:								
Ending Balance: collectively evaluated for impairment non PCI loans	$ 71,118	$ 220,761	$ 447,760	$ 144,003	$ 43,763	$ 9,729	$ 68,030	$ 1,005,164
Ending Balance: collectively evaluated for impairment PCI loans	$ 1,103	$ 677	$ 5,770	$ 7,218	$ 48	$ -	$ 897	$ 15,713
Ending Balance: individually evaluated for impairment	$ 3,527	$ 440	$ 5,585	$ 476	$ 703	$ 284	$ 197	$ 11,212
Ending Balance	$ 75,748	$ 221,878	$ 459,115	$ 151,697	$ 44,514	$ 10,013	$ 69,124	$ 1,032,089

2018 Allowance for loan losses	Commercial and industrial	Construction	Commercial real estate	1 to 4 family residential	HELOC	Loans to individuals & overdrafts	Multi-family residential	Total
Loans – excluding PCI								
Balance, beginning of period 01/01/2018	$ 742	$ 1,955	$ 3,304	$ 1,058	$ 549	$ 305	$ 791	$ 8,704
Provision for loan losses	(23)	(576)	(326)	585	31	1	(320)	(628)
Loans charged-off	(196)	-	(2)	(12)	(68)	(191)	-	(469)
Recoveries	239	6	48	32	43	91	-	459
Balance, end of period 12/31/2018	$ 762	$ 1,385	$ 3,024	$ 1,663	$ 555	$ 206	$ 471	$ 8,066
PCI Loans								
Balance, beginning of period 01/01/2018	$ 65	$ -	$ 66	$ -	$ -	$ -	$ -	$ 131
Provision for loan losses	149	-	319	4	-	-	-	472
Loans charged-off	-	-	-	-	-	-	-	-
Recoveries	-	-	-	-	-	-	-	-
Balance, end of period 12/31/2018	$ 214	$ -	$ 385	$ 4	$ -	$ -	$ -	$ 603
Total Loans								
Balance, beginning of period 01/01/2018	$ 807	$ 1,955	$ 3,370	$ 1,058	$ 549	$ 305	$ 791	$ 8,835
Provision for loan losses	126	(576)	(7)	589	31	1	(320)	(156)
Loans charged-off	(196)	-	(2)	(12)	(68)	(191)	-	(469)
Recoveries	239	6	48	32	43	91	-	459
Balance, end of period 12/31/2018	$ 976	$ 1,385	$ 3,409	$ 1,667	$ 555	$ 206	$ 471	$ 8,669
Ending Balance: individually evaluated for impairment	$ 51	$ 14	$ -	$ 22	$ -	$ -	$ -	$ 87
Ending Balance: collectively evaluated for impairment	$ 925	$ 1,371	$ 3,409	$ 1,645	$ 555	$ 206	$ 471	$ 8,582
Loans:								
Ending Balance: collectively evaluated for impairment non PCI loans	$ 68,891	$ 169,065	$ 444,354	$ 150,700	$ 48,747	$ 12,713	$ 62,307	$ 956,777
Ending Balance: collectively evaluated for impairment PCI loans	$ 1,764	$ 751	$ 7,579	$ 8,188	$ 49	$ -	$ 937	$ 19,268
Ending Balance: individually evaluated for impairment	$ 3,526	$ 588	$ 5,678	$ 709	$ 917	$ 101	$ 215	$ 11,734
Ending Balance	$ 74,181	$ 170,404	$ 457,611	$ 159,597	$ 49,713	$ 12,814	$ 63,459	$ 987,779

2017 Allowance for loan losses	Commercial and industrial	Construction	Commercial real estate	1 to 4 family residential	HELOC	Loans to individuals & overdrafts	Multi-family residential	Total
Loans – excluding PCI								
Balance, beginning of period 01/01/2017	$ 1,211	$ 1,301	$ 3,448	$ 846	$ 611	$ 317	$ 628	$ 8,362
Provision for loan losses	(607)	642	754	188	92	55	161	1,285
Loans charged-off	(73)	(17)	(914)	(22)	(179)	(101)	-	(1,306)
Recoveries	211	29	16	46	25	34	2	363
Balance, end of period 12/31/2017	$ 742	$ 1,955	$ 3,304	$ 1,058	$ 549	$ 305	$ 791	$ 8,704
PCI Loans								
Balance, beginning of period 01/01/2017	$ 37	$ -	$ -	$ -	$ 12	$ -	$ -	$ 49
Provision for loan losses	28	-	66	-	(12)	-	-	82
Loans charged-off	-	-	-	-	-	-	-	-
Recoveries	-	-	-	-	-	-	-	-
Balance, end of period 12/31/2017	$ 65	$ -	$ 66	$ -	$ -	$ -	$ -	$ 131
Total Loans								
Balance, beginning of period 01/01/2017	$ 1,248	$ 1,301	$ 3,448	$ 846	$ 623	$ 317	$ 628	$ 8,411
Provision for loan losses	(579)	642	820	188	80	55	161	1,367
Loans charged-off	(73)	(17)	(914)	(22)	(179)	(101)	-	(1,306)
Recoveries	211	29	16	46	25	34	2	363
Balance, end of period 12/31/2017	$ 807	$ 1,955	$ 3,370	$ 1,058	$ 549	$ 305	$ 791	$ 8,835
Ending Balance: individually evaluated for impairment	$ 50	$ -	$ -	$ 11	$ -	$ -	$ -	$ 61
Ending Balance: collectively evaluated for impairment	$ 757	$ 1,955	$ 3,370	$ 1,047	$ 549	$ 305	$ 791	$ 8,774
Loans:								
Ending Balance: collectively evaluated for impairment non PCI loans	$ 102,148	$ 176,479	$ 389,617	$ 146,504	$ 51,958	$ 10,176	$ 75,777	$ 952,659
Ending Balance: collectively evaluated for impairment PCI loans	$ 2,933	$ 1,069	$ 9,056	$ 9,119	$ 46	$ 67	$ 971	$ 23,261
Ending Balance: individually evaluated for impairment	$ 1,083	$ 385	$ 4,427	$ 1,278	$ 602	$ 1	$ 235	$ 8,011
Ending Balance	$ 106,164	$ 177,933	$ 403,100	$ 156,901	$ 52,606	$ 10,244	$ 76,983	$ 983,931

NOTE F – OTHER REAL ESTATE OWNED

The following table explains changes in other real estate owned ("OREO") during the years ended December 31, 2019 and 2018 (dollars in thousands):

	December 31, 2019	December 31, 2018
	(Dollars in thousands)	
Beginning balance January 1	$ 1,088	$ 1,258
Sales	(120)	(717)
Write-downs and loss on sales	(49)	(71)
Transfers	2,614	618
Ending balance	$ 3,533	$ 1,088

At December 31, 2019 and December 31, 2018, the Company had $3.5 million and $1.1 million, respectively, of foreclosed residential real estate property in OREO. The Company had 3 loans with recorded investment in the amount of $114,000 in consumer mortgage loans collateralized by residential real estate property in the process of foreclosure at December 31, 2019 compared to 4 loans with recorded investment in the amount of $500,000 in consumer mortgage loans collateralized by residential real estate property in the process of foreclosure at December 31, 2018.

NOTE G - PREMISES AND EQUIPMENT

The following is a summary of premises and equipment at December 31, 2019 and 2018:

	2019	2018
	(dollars in thousands)	
Land	$ 4,846	$ 4,913
Buildings	15,692	14,878
Furniture and equipment	8,077	7,455
Leasehold improvements	498	562
Construction in progress	-	136
	29,113	27,944
Less accumulated depreciation	11,322	10,024
Total	$ 17,791	$ 17,920

Depreciation amounting to approximately $2.8 million, $1.7 million, and $1.1 million for the years ended December 31, 2019, 2018, and 2017, respectively, is included in occupancy and equipment expenses.

NOTE H – GOODWILL AND OTHER INTANGIBLE ASSETS

The table below summarizes the changes in carrying amounts of goodwill and other intangibles (core deposit intangibles) for the periods presented.

		Core Deposit Intangible		
	Goodwill	Gross	Accumulated Amortization	**Net**
		(dollars in thousands)		
Balance at January 1, 2017	$ 6,931	$ 3,219	$ (2,409)	$ 810
Goodwill and core deposit intangible resulting from Premara merger	17,973	2,700	-	2,700
Amortization expense	-	-	(409)	(409)
Balance at December 31, 2017	24,904	5,919	(2,818)	3,101
Adjustment of goodwill	(325)	-	-	-
Amortization expense	-	-	(1,016)	(1,016)
Balance at December 31, 2018	24,579	5,919	(3,834)	2,085
Core deposit intangible resulting from branch acquisition	-	350	-	350
Amortization expense	-	-	(825)	(825)
Balance at December 31, 2019	$ 24,579	$ 6,269	$ (4,659)	$ 1,610

Goodwill represents the excess of the purchase price over the fair value of acquired net assets under the acquisition method of accounting. An adjustment to goodwill was made during 2018 as a result of a revision to the purchase accounting entry during the measurement period.

The value of acquired core deposit relationships was determined using the present value of the difference between a market participant's cost of obtaining alternative funds and the cost to maintain the acquired deposit base.

The table below summarizes the remaining core deposit intangible amortization (dollars in thousands):

2020	$ 628
2021	435
2022	288
2023	147
2024	41
Thereafter	71
	$ 1,610

NOTE I – DEPOSITS

The scheduled maturities of time deposits at December 31, 2019 are as follows:

	Total Time Deposits
	(dollars in thousands)
2020	$ 332,254
2021	81,002
2022	10,764
2023	4,599
2024	641
Thereafter	-
	$ 429,260

Time deposits with balances of more than $250,000 were $150.4 million and $120.8 million at December 31, 2019 and 2018, respectively.

NOTE J – REVENUE RECOGNITION

On January 1, 2018, the Company adopted ASU No. 2014-09, *Revenue from Contracts with Customers (Topic 606),* and all subsequent ASUs that modified Topic 606. As stated in Note B, *Recent Accounting Pronouncements*, the implementation of the new standard did not have a material impact on the measurement or recognition of revenue; as such, a cumulative effect adjustment to opening retained earnings was not deemed necessary. Results for reporting periods beginning after January 1, 2018 are presented under Topic 606, while prior period amounts were not adjusted and continue to be reported in accordance with accounting policies employed under Topic 605.

Topic 606 does not apply to revenue associated with financial instruments, including revenue from loans and securities. In addition, certain noninterest income streams such as fees associated with mortgage servicing rights, financial guarantees, derivatives, and certain credit card fees are also not in scope of the new guidance. Topic 606 is applicable to noninterest revenue streams such as trust and asset management income, deposit related fees, interchange fees, merchant income, and annuity and insurance commissions. However, the recognition of these revenue streams did not change significantly upon adoption of Topic 606. Substantially all of the Company's revenue is generated from contracts with customers. Noninterest revenue streams in-scope of Topic 606 are discussed below.

Service Charges on Deposit Accounts

Service charges on deposit accounts consist of insufficient funds fees, account analysis fees (i.e., net fees earned on analyzed business and public checking accounts), monthly service fees, check orders, and other deposit account related fees. The Company's performance obligation for account analysis fees and monthly service fees is generally satisfied, and the related revenue recognized, over the period in which the service is provided. Check orders and other deposit account related fees are largely transactional based, and therefore, the Company's performance obligation is satisfied, and related revenue recognized, at a point in time. Payment for service charges on deposit accounts is primarily received immediately or in the following month through a direct charge to customers' accounts.

Other Fees and Income

Other fees and income primarily consist of debit and credit card income, ATM fees, merchant services income, and other service charges. Debit and credit card income primarily consists of interchange fees earned whenever the Company's debit and credit cards are processed through card payment networks such as Visa. ATM fees are primarily generated when a Company cardholder uses a non-Company ATM or a non-Company cardholder uses a Company ATM. Merchant services income mainly represents fees charged to merchants to process their debit and credit card transactions, in addition to account management fees. Other service charges include revenue from processing wire transfers, bill pay services, cashier's checks, and other services. The Company's performance obligation for fees, exchange, and other service charges are largely satisfied, and related revenue recognized, when the services are rendered or upon completion. Payment is typically received immediately or in the following month. Other fees and income also includes other recurring revenue streams such as safety deposit box rental fees and other miscellaneous revenue streams. Safe deposit box rental fees are charged to the customer on an annual basis and recognized upon receipt of payment. The Company determined that since rentals and renewals occur fairly consistently over time, revenue is recognized on a basis consistent with the duration of the performance obligation.

The following presents noninterest income, segregated by revenue streams in-scope and out-of-scope of Topic 606, for the year ended December 31, 2019, 2018 and 2017.

	December 31, 2019	December 31, 2018	December 31, 2017
		(dollars in thousands)	
Service Charges on Deposit Accounts	$ 1,161	$ 1,124	$ 899
Other	2,050	1,657	960
Noninterest Income (in-scope of Topic 606)	3,211	2,781	1,859
Noninterest Income (out-of-scope of Topic 606)	2,208	1,920	1,213
Total Non-interest Income	$ 5,419	$ 4,701	$ 3,072

Contract Balances

A contract asset balance occurs when an entity performs a service for a customer before the customer pays consideration (resulting in a contract receivable) or before payment is due (resulting in a contract asset). A contract liability balance is an entity's obligation to transfer a service to a customer for which the entity has already received payment (or payment is due) from the customer. The Company's noninterest revenue streams are largely based on transactional activity. Consideration is often received immediately or shortly after the Company satisfies its performance obligation and revenue is recognized. The Company does not typically enter into long-term revenue contracts with customers, and therefore, does not experience significant contract balances. As of December 31, 2019 and December 31, 2018, the Company did not have any significant contract balances.

Contract Acquisition Costs

In connection with the adoption of Topic 606, an entity is required to capitalize, and subsequently amortize into expense, certain incremental costs of obtaining a contract with a customer if these costs are expected to be recovered. The incremental costs of obtaining a contract are those costs that an entity incurs to obtain a contract with a customer that it would not have incurred if the contract had not been obtained (for example, sales commission). The Company utilizes the practical expedient which allows entities to immediately expense contract acquisition costs when the asset that would have resulted from capitalizing these costs would have been amortized in one year or less. Upon adoption of Topic 606, the Company did not capitalize any contract acquisition costs.

NOTE K – SHORT-TERM AND LONG-TERM DEBT

At December 31, 2019, the Company had no short-term debt and $57.4 million in long-term debt. Long-term debt consisted of $12.4 million in junior subordinated debentures and $45.0 million in Federal Home Loan Bank advances. The Federal Home Loan Bank advances are collateralized by $108.3 million of loans as of December 31, 2019.

At December 31, 2018, the Company had $7.0 million in short-term debt and $57.4 million in long-term debt. Short-term debt consisted of $7.0 million in Federal Home Loan Bank advances. Long-term debt consisted of $12.4 million in junior subordinated debentures and $45.0 million in Federal Home Loan Bank advances. The Federal Home Loan Bank advances are collateralized by $142.3 million of loans as of December 31, 2018.

At December 31, 2019, the Company had $45.0 million in advances from the Federal Home Loan Bank of Atlanta and no borrowings from the Federal Reserve Bank discount window. Advances consisted of the following at December 31, 2019:

	Amount	Rate	Maturity
	(dollars in thousands)		
Advance type:			
Fixed rate hybrid	20,000	2.53%	2/2/2021
Fixed rate hybrid	10,000	2.89%	4/12/2023
Fixed rate hybrid	5,000	2.94%	5/30/2023
Fixed rate hybrid	10,000	2.97%	6/28/2023

On September 20, 2004, $12.4 million of junior subordinated debentures were issued to New Century Statutory Trust I ("the Trust") in exchange for the proceeds of trust preferred securities issued by the Trust. All of the Trust's common equity is owned by the Company. The junior subordinated debentures are included in long-term debt and the Company's equity interest in the Trust is included in other assets.

The Company pays interest on the junior subordinated debentures at an annual rate, reset quarterly, equal to 3 month LIBOR plus 2.15%. The debentures are redeemable on September 20, 2009 or afterwards in whole or in part, on any March 20, June 20, September 20 or December 20. Redemption is mandatory at September 20, 2034. The Company has fully and unconditionally guaranteed repayment of the trust-preferred securities. The Company's obligation under the guarantee is unsecured and subordinate to senior and subordinated indebtedness of the Company. The trust preferred securities qualify as Tier 1 capital for regulatory capital purposes subject to certain limitations, none of which were applicable at December 31, 2019.

Lines of credit amounted to $238.9 million with various correspondent banks with $45.0 million outstanding and $173.9 million available as of December 31, 2019. Some of the lines of credit are secured and others unsecured with a variety of rates and terms.

NOTE L - INCOME TAXES

The significant components of the provision for income taxes for the years ended December 31, 2019, 2018 and 2017 are as follows:

	2019	2018	2017
		(dollars in thousands)	
Current tax provision:			
Federal	$ 2,699	$ 2,366	$ 3,059
State	412	483	328
Total current tax provision	3,111	2,849	3,387
Deferred tax provision:			
Federal	575	943	2,328
State	10	118	(3)
Total deferred tax provision	585	1,061	2,325
Net income tax provision	$ 3,696	$ 3,910	$ 5,712

The difference between the provision for income taxes and the amounts computed by applying the statutory federal income tax rate of 21% for 2019 and 2018 and 34% for 2017 to income before income taxes is summarized below:

	2019	2018	2017
		(dollars in thousands)	
Income tax at federal statutory rate	$ 3,513	$ 3,715	$ 3,025
Increase (decrease) resulting from:			
State income taxes, net of federal tax effect	333	475	214
Tax-exempt interest income	(95)	(99)	(128)
Income from life insurance	(141)	(144)	(195)
Incentive stock option expense	41	(2)	39
Merger expenses	-	20	209
Impact of changes in tax rates	-	-	2,591
Other permanent differences	45	(55)	(43)
Provision for income taxes	$ 3,696	$ 3,910	$ 5,712

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Significant components of deferred taxes at December 31, 2019 and 2018 are as follows:

	2019	2019
	(dollars in thousands)	
Deferred tax assets relating to:		
Allowance for loan losses	$ 1,913	$ 1,992
Deferred compensation	116	132
Unrealized losses on available-for-sale securities	-	(17)
Net operating loss carryforwards	541	999
Acquisition accounting	1,024	1,107
Write-downs on foreclosed real estate	120	108
Other	229	269
Total deferred tax assets	3,943	4,590
Deferred tax liabilities relating to:		
Premises and equipment	(796)	(721)
Deferred loan fees/costs	(73)	(67)
Unrealized gains on available-for-sale securities	(268)	-
Core deposit intangible	(8)	(140)
Total deferred tax liabilities	(1,145)	(928)
Net recorded deferred tax asset, included in other assets	$ 2,798	$ 3,662

Deferred income taxes are measured at the enacted tax rate for the period in which they are expected to reverse. In December 2017 the U.S. Congress passed and the President signed legislation which reduced the statutory federal corporate tax rate to 21% effective January 1, 2018 and for all taxable years ending after that date. North Carolina also enacted legislation to reduce its corporate tax rate from 3.0% to 2.5% effective January 1, 2019. The impact of this change in tax rate was an additional income tax expense of $2.6 million for 2017.

The Company had $2.6 million of net operating losses which can be carried forward and applied against future taxable income. If unused, these net operating losses will expire in 2027 through 2036. The Company's policy is to report interest and penalties, if any, related to uncertain tax positions in income tax expense in the Consolidated Statements of Operations. With few exceptions, the Company is no longer subject to U.S. federal, state and local, or non-U.S. income tax examinations by tax authorities for years before 2014. As of December 31, 2019 and 2018, the Company has no uncertain tax positions.

The Company's net deferred tax asset was $2.8 million and $3.7 million at December 31, 2019 and 2018. In evaluating whether the Company will realize the full benefit of the net deferred tax asset, both positive and negative evidence are considered, including among other things recent earnings trends, projected earnings, and asset quality. As of December 31, 2019, management concluded that the Company's net deferred tax assets were fully realizable. The Company will continue to monitor deferred tax assets closely to evaluate whether we will be able to realize the full benefit of our net deferred tax asset or whether there is any need for a valuation allowance. Significant negative trends in credit quality, losses from operations or other factors could impact the realization of the deferred tax asset in the future.

NOTE M - REGULATORY MATTERS

The Company is subject to various regulatory capital requirements administered by federal and state banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory, and possibly additional discretionary actions by regulators that, if undertaken, could have a material adverse effect on the Company's consolidated financial statements. Quantitative measures established by regulation to ensure capital adequacy require the Company to maintain minimum amounts and ratios, as set forth in the table below. Management believes, as of December 31, 2019, that the Company meets all capital adequacy requirements to which it is subject. The Company's significant assets are its investments in Select Bank & Trust Company and New Century Statutory Trust I.

Regulatory authorities may limit payment of dividends by any bank when it is determined that such a limitation is in the public interest and is necessary to ensure financial soundness of the bank. The North Carolina Commissioner of Banks and the FDIC are also authorized to prohibit the payment of dividends under certain other circumstances.

A significant measure of the strength of a financial institution is its capital base. Federal regulations have classified and defined capital into the following components: (1) Tier 1 capital, which includes common shareholders' equity and qualifying preferred equity, and (2) Tier 2 capital, which includes a portion of the allowance for loan losses, certain qualifying long-term debt and preferred stock which does not qualify as Tier 1 capital. Financial institutions and holding companies became subject to the Basel III capital requirements beginning on January 1, 2015. A new part of the capital ratios profile is the Common Equity Tier 1 risk-based ratio which does not include limited life components such as trust preferred securities and Small Business Lending Fund ("SBLF") preferred stock. Minimum capital levels are regulated by risk-based capital adequacy guidelines, which require a financial institution to maintain capital as a percentage of its assets, and certain off-balance sheet items adjusted for predefined credit risk factors (risk-adjusted assets).

As the following tables indicate, at December 31, 2019 and 2018, the Company and its Bank subsidiary both exceeded minimum regulatory capital requirements as specified below.

	Actual		Minimum for capital adequacy purposes	
The Company:	Amount	Ratio	Amount	Ratio
	(dollars in thousands)			
December 31, 2019:				
Total Capital (to Risk-Weighted Assets)	$ 205,462	18.26%	$ 90,003	8.00%
Tier 1 Capital (to Risk-Weighted Assets)	197,138	17.52%	67,502	6.00%
Common Equity Tier 1 (to Risk-Weighted Assets)	185,138	16.46%	50,627	4.50%
Tier 1 Capital (to Average Assets)	197,138	15.84%	49,777	4.00%

	Actual		Minimum for capital adequacy purposes	
The Company:	Amount	Ratio	Amount	Ratio
	(dollars in thousands)			
December 31, 2018:				
Total Capital (to Risk-Weighted Assets)	$ 202,675	19.26%	$ 84,179	8.00%
Tier 1 Capital (to Risk-Weighted Assets)	194,006	18.44%	63,135	6.00%
Common Equity Tier 1 (to Risk-Weighted Assets)	182,006	17.30%	47,351	4.50%
Tier 1 Capital (to Average Assets)	194,006	15.65%	49,576	4.00%

Select Bank & Trust Company's actual capital amounts and ratios are presented in the table below as of December 31, 2019 and 2018:

The Bank:	Actual		Minimum for capital adequacy purposes		Minimum to be well capitalized under prompt corrective action provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
			(dollars in thousands)			
December 31, 2019:						
Total Capital (to Risk-Weighted Assets)	$ 177,223	15.69%	$ 90,366	8.00%	112,958	10.00%
Tier 1 Capital (to Risk-Weighted Assets)	168,899	14.95%	67,775	6.00%	90,366	8.00%
Common equity Tier 1 (to Risk-Weight Assets)	168,899	14.95%	50,831	4.50%	73,422	6.50%
Tier 1 Capital (to Average Assets)	168,899	13.59%	49,730	4.00%	62,162	5.00%

The Bank:	Actual		Minimum for capital adequacy purposes		Minimum to be well capitalized under prompt corrective action provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
			(dollars in thousands)			
December 31, 2018:						
Total Capital (to Risk-Weighted Assets)	$ 162,507	15.45%	$ 84,124	8.00%	105,156	10.00%
Tier 1 Capital (to Risk-Weighted Assets)	153,838	14.63%	63,093	6.00%	84,124	8.00%
Common equity Tier 1 (to Risk-Weight Assets)	153,838	14.63%	47,320	4.50%	68,351	6.50%
Tier 1 Capital (to Average Assets)	153,838	12.42%	49,557	4.00%	61,947	5.00%

During 2004, the Company issued $12.4 million of junior subordinated debentures to a newly formed subsidiary, New Century Statutory Trust I, which in turn issued $12.0 million of trust preferred securities. The proceeds from the sale of the trust preferred securities provided additional capital for the growth and expansion of the Bank. Under the current applicable regulatory guidelines, all of the proceeds from the issuance of these trust preferred securities qualify as Tier 1 capital as of December 31, 2019.

Management expects that the Bank will remain "well capitalized" for regulatory purposes, although there can be no assurance that additional capital will not be required in the future.

NOTE N - OFF-BALANCE SHEET RISK

The Company is a party to financial instruments with off-balance sheet credit risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit and letters of credit. Those instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the balance sheet. The contract or notional amounts of those instruments reflect the extent of involvement the Company has in particular classes of financial instruments. The Company uses the same credit policies in making commitments and conditional obligations as it does for on-balance-sheet instruments.

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of conditions established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since some of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Company evaluates each customer's creditworthiness on a case-by-case basis.

The amount of collateral obtained, if deemed necessary by the Company, upon extension of credit is based on management's credit evaluation of the borrower. Collateral obtained varies but may include real estate, stocks, bonds, and certificates of deposit.

A summary of the contract amount of the Company’s exposure to off-balance sheet credit risk as of December 31, 2019 is as follows:

		(In thousands)
Financial instruments whose contract amounts represent credit risk:		
Undisbursed commitments	$	234,191
Letters of credit		2,367

The Company has legally binding delayed equity commitments to private investment funds. These commitments are not expected to be called, and therefore, are not reflected in the financial statements. The amount of these commitments at December 31, 2019 and 2018 was $425,000 and $425,000, respectively.

NOTE O – FAIR VALUE MEASUREMENTS

ASC 820 defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. ASC 820 does not require any new fair value measurements, but clarifies and standardizes some divergent practices that have emerged since prior guidance was issued. ASC 820 creates a three-level hierarchy under which individual fair value estimates are to be ranked based on the relative reliability of the inputs used in the valuation.

Fair value estimates are made at a specific moment in time, based on relevant market information and information about the financial instrument. These estimates do not reflect any premium or discount that could result from offering for sale at one time the Company’s entire holdings of a particular financial instrument.

The following methods and assumptions were used to estimate the fair value of each class of financial instruments for which it is practicable to estimate that value:

Fair Value Hierarchy
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 fair value. These levels are:

- Level 1 – Valuation is based upon quoted prices for identical instruments traded in active markets.
- Level 2 – Valuation is based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active and model-based valuation techniques for which all significant assumptions are observable in the market.
- Level 3 – Valuation is generated from model-based techniques that use at least one significant assumption not observable in the market. These unobservable assumptions reflect estimates of assumptions that market participants would use in pricing the asset or liability. Valuation techniques include use of option pricing models, discounted cash flows models and similar techniques.

The following is a description of valuation methodologies used for assets and liabilities recorded at fair value on a recurring basis.

Investment Securities Available-for-Sale
Investment securities available-for-sale are recorded at fair value on a recurring basis. Fair value measurement is based upon quoted prices, if available. If quoted prices are not available, fair values are measured using independent pricing models or other model-based valuation techniques such as the present value of future cash flows, adjusted for the security's credit rating, prepayment assumptions and other factors such as credit loss assumptions. Level 1 securities include those traded on an active exchange, such as the New York Stock Exchange, U.S. Treasury securities that are traded by dealers or brokers in active over-the-counter markets and money market funds. Level 2 securities include U.S. government agencies – GSE's, mortgage-backed securities issued by GSE's, corporate bonds and municipal bonds. Valuation techniques are consistent with methodologies used in prior periods.

The following tables summarize quantitative disclosures about the fair value measurement for each category of assets carried at fair value on a recurring basis as of December 31, 2019 and December 31, 2018 (dollars in thousands):

Investment securities available for sale December 31, 2019	Fair value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
U.S. government agencies – GSE's	$ 9,996	$ -	$ 9,996	$ -
Mortgage-backed securities –GSE's	47,743	-	47,743	-
Corporate Bonds	2,299	-	2,299	-
Municipal bonds	12,329	-	12,329	-
Total investment available for sale	$ 72,367	$ -	$ 72,367	$ -

Investment securities available for sale December 31, 2018	Fair value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
U.S. government agencies – GSE's	$ 9,837	$ -	$ 9,837	$ -
Mortgage-backed securities –GSE's	22,983	-	22,983	-
Corporate Bonds	1,722		1,722	-
Municipal bonds	16,991	-	16,991	-
Total investment available for sale	$ 51,533	$ -	$ 51,533	$ -

The following are descriptions of valuation methodologies used for assets and liabilities recorded at fair value on a non-recurring basis.

Loans
The Company does not record loans at fair value on a recurring basis. However, from time to time, a loan is considered impaired and a specific reserve in the allowance for loan losses is established. Loans for which it is probable that payment of interest and principal will not be made in accordance with the contractual terms of the loan agreement are considered impaired. Once a loan is identified as individually impaired, management measures impairment in accordance with ASC 310, "Receivables". The fair value of impaired loans is estimated using one of several methods, including collateral value, market value of similar debt, enterprise value, or liquidation value and discounted cash flows. Those impaired loans not requiring an allowance represent loans for which the fair value of the expected repayments or collateral exceed the recorded investments in such loans. At December 31, 2019, and 2018, substantially all of the total impaired loans were evaluated based on the fair value of the collateral. Impaired loans where a specific reserve is established based on the fair value of collateral require classification in the fair value hierarchy. When the fair value of the collateral is based on an observable market price or a current appraised value, the Company records the impaired loan as nonrecurring Level 2. When an appraised value is not available or management determines the fair value of the collateral is further impaired below the appraised value and there is no observable market price, the Company records the impaired loan as nonrecurring Level 3. There were no transfers between levels from prior reporting periods. Valuation techniques are consistent with prior periods.

The significant unobservable inputs used in the fair value measurement of the Company's impaired loans range between 1 – 50% and 5 – 50% discount from appraisals for expected liquidation and sales costs at December 31, 2019 and 2018.

Foreclosed Real Estate
Foreclosed real estate are properties recorded at estimated fair value, less the estimated costs to sell, at the date of foreclosure. Inputs include appraised values on the properties or recent sales activity for similar assets in the property's market adjusted by discounts as determined by the Company. Therefore, foreclosed real estate is classified within Level 3 of the hierarchy. Valuation techniques are consistent with prior periods.

The significant unobservable input used in the fair value measurement of the Company's foreclosed real estate range between 6% – 10% discount from appraisals for expected liquidation and sales costs at both December 31, 2019 and 2018, respectively.

Assets held for sale
During 2015, a branch facility was taken out of service as part of the Company's branch restructuring plan and reclassified as held for sale. The property is recorded at the remaining book balance of the asset or an estimated fair value less estimated selling costs, whichever is less. Inputs include appraised values on the properties or recent sales activity for similar assets in the property's market. The significant unobservable input used is the discount applied to appraised values to account for expected liquidation and selling costs ranged between 1% and 25 % at December 31, 2018. The branch was sold in 2019.

The following tables summarize quantitative disclosures about the fair value measurement for each category of assets carried at fair value on a nonrecurring basis as of December 31, 2019 and December 31, 2018 (dollars in thousands):

Asset Category December 31, 2019	Fair value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Impaired loans	$ 5,941	$ -	$ -	$ 5,941
Foreclosed real estate	3,533	-	-	3,533
Total	$ 9,474	$ -	$ -	$ 9,474

Asset Category December 31, 2018	Fair value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Impaired loans	$ 7,257	$ -	$ -	$ 7,257
Assets held for sale	668	-	-	668
Foreclosed real estate	1,088	-	-	1,088
Total	$ 9,013	$ -	$ -	$ 9,013

As of December 31, 2019, the Bank identified $11.2 million in impaired loans, of which $5.9 million were carried at fair value on a non-recurring basis which included $972,000 in loans that required a specific reserve of $413,000, and an additional $438,000 in other loans without specific reserves that had partial charge-offs. As of December 31, 2018, the Bank identified $11.7 million in impaired loans, of which $7.3 million were carried at fair value on a non-recurring basis which included $291,000 in loans that required a specific reserve of $87,000, and an additional $595,000 in other loans without specific reserves that had partial charge-offs.

Financial instruments include cash and due from banks, interest-earning deposits with banks, investments, loans, deposit accounts and borrowings. Due to the nature of the Company’s business, a significant portion of its assets and liabilities consist of financial instruments, the estimated values of which are disclosed. These estimates do not reflect any premium or discount that could result from offering for sale at one time the Company’s entire holdings of a particular financial instrument. Because no active market readily exists for a portion of the Company’s financial instruments, fair value estimates are based on judgments regarding future expected loss experience, current economic conditions, risk characteristics of various financial instruments, and other factors. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and, therefore, cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

The following table presents the carrying values and estimated fair values of the Company's financial instruments at December 31, 2019 and 2018:

	December 31, 2019				
	Carrying Amount	Estimated Fair Value	Level 1	Level 2	Level 3
	(dollars in thousands)				
Financial assets:					
Cash and due from banks	$ 19,110	$ 19,110	$ 19,110	$ -	$ -
Interest-earning deposits in other banks	50,920	50,920	50,920	-	-
Federal funds sold	9,047	9,047	9,047	-	-
Investment securities available for sale	72,367	72,367	-	72,367	-
Loans held for sale	928	928	-	928	-
Loans, net	1,021,651	1,016,239	-	-	1,016,239
Accrued interest receivable	4,189	4,189	-	4,189	-
Stock in the FHLB	3,045	3,045	-	-	3,045
Other non-marketable securities	719	719	-	-	719
Financial liabilities:					
Deposits	$ 992,838	$ 995,056	$ -	$ 995,056	$ -
Long-term debt	57,372	55,429	-	55,429	-
Accrued interest payable	578	578	-	578	-

	December 31, 2018				
	Carrying Amount	Estimated Fair Value	Level 1	Level 2	Level 3
	(dollars in thousands)				
Financial assets:					
Cash and due from banks	$ 17,059	$ 17,059	$ 17,059	$ -	$ -
Certificates of deposits	1,000	1,000	1,000	-	-
Interest-earning deposits in other banks	121,303	121,303	121,303	-	-
Investment securities available for sale	51,533	51,533	-	51,533	-
Loans held for sale	580	580	-	580	-
Loans, net	977,371	970,330	-	-	970,330
Accrued interest receivable	3,889	3,889	-	3,889	-
Stock in the FHLB	3,283	3,283	-	-	3,283
Other non-marketable securities	762	762	-	-	762
Assets held for sale	668	668	-	-	668
Financial liabilities:					
Deposits	$ 980,427	$ 979,570	$ -	$ 979,570	$ -
Short-term debt	7,000	7,000	-	7,000	-
Long-term debt	57,372	55,504	-	55,504	-
Accrued interest payable	667	667	-	667	-

NOTE P - EMPLOYEE AND DIRECTOR BENEFIT PLANS

401(k) Plan

The Company has a 401(k) Plan and substantially all employees participate in the plan. The Company matches 100% of the first 6% of an employee's compensation contributed to the plan. Expenses attributable to the plan amounted to $698,000, $639,000, and $465,000 for the years ended December 31, 2019, 2018 and 2017, respectively.

Employment Agreements

The Company has entered into employment agreements with five executive officers to promote a stable and competent management base. These agreements provide for benefits as specified in the contracts and cannot be terminated by the Board of Directors, except for cause, without prejudicing the officer's right to receive certain vested rights, including compensation. In the event of a change in control of the Company, as outlined in the agreements, the acquirer will generally be bound by the terms of those contracts.

Supplemental Executive Retirement Plans

The Company implemented a nonqualified supplemental executive retirement plan for the former Chief Executive Officer during 2003. Benefits accrue and vest during the period of employment, and will be paid in monthly benefit payments over the officer's life after retirement. Provisions of $81,000, $36,000, and $53,000 were expensed for future benefits to be provided under this plan during 2019, 2018 and 2017, respectively. In conjunction with the implementation of this plan, the Company has purchased life insurance on certain key officers to help offset plan accruals. The life insurance policies provide the payment of a death benefit in the event an insured officer dies prior to attainment of retirement age. The total liability under this plan at December 31, 2019 and 2018 was $24,000 and $85,000, respectively.

As part of the acquisition of Progressive State Bank ("Progressive"), the Company assumed a liability for the supplemental early retirement plan for Progressive's Chief Executive Officer. Provisions of $81,000, $(35,000), and $36,000 and were expensed in 2019, 2018 and 2017, resulting in a total liability of $265,000 and $286,000 as of December 31, 2019 and 2018, respectively. Due to the plan having a tax gross up feature that was impacted by lower tax rates under the Tax Act, the Company recorded a negative provision for 2018. Corresponding to this liability, Progressive had purchased a life insurance policy on a key officer to help offset the expense associated with future benefit payments. This policy was acquired by the Company upon its acquisition of Progressive.

The Company approved a supplemental executive retirement plan for two of its executives in 2019. Provisions of $64,000 were expensed during 2019 resulting in a total liability of $64,000. Proceeds from purchased life insurance on certain key officers were used to offset plan accruals.

Directors Deferred Compensation

The Company has instituted a Directors' Deferral Plan ("Deferral Plan") whereby individual directors may elect annually to defer receipt of all or a designated portion of their directors' fees for the coming year. Amounts so deferred are used to purchase shares of the Company's common stock on the open market by the administrator of the Deferral Plan or to issue shares from the Company's authorized but unissued shares, with such deferred compensation disbursed in the future as specified by the director at the time of his or her deferral election. All deferral amounts and matching contributions, if any, are paid into a rabbi trust with a separate account for each participant under the plan. Net compensation and other expenses attributable to this plan for the years ended December 31, 2019, 2018 and 2017 were $200,000, $97,000, and $178,000, respectively. The Directors' Deferral Plan was amended and restated on September 22, 2015 to ensure compliance with applicable regulations and to provide that the eventual payment of compensation deferred under the plan may be made only in the form of the Registrant's common stock. A liability of $2.8 million and $2.6 million related to this plan is included in shareholders' equity for December 31, 2019 and 2018, respectively.

Equity-Based Compensation Plans

The Company utilizes equity-based awards as a component of its compensation of employees and directors. These equity-based awards may be in the form of incentive stock options, nonstatutory stock options, stock appreciation rights, restricted stock awards, or restricted stock unit awards. Awards are granted pursuant to the Company's equity-based compensation plans. The Company's shareholders approved all equity-based compensation plans. At December 31, 2019, the Company had awards outstanding under its 2004 Incentive Stock Option Plan, 2008 Omnibus Stock Ownership and Long Term Incentive Plan (the "2008 Omnibus Plan"), 2010 Omnibus Stock Ownership and Long Term Incentive Plan (the "2010 Omnibus Plan"), and 2018 Omnibus Stock Incentive Plan (the "2018 Omnibus Plan").

As of December 31, 2019, the Company had awards covering 13,000 shares outstanding under the 2004 Incentive Stock Option Plan, awards covering 33,200 shares outstanding under the 2008 Omnibus Plan, awards covering 163,700 shares outstanding under the 2010 Omnibus Plan, and awards covering 58,500 shares outstanding under the 2018 Omnibus Plan.

The 2018 Omnibus Plan became effective upon the approval of shareholders on May 22, 2018. As of December 31, 2019, the 2018 Omnibus Plan was the only plan that had shares available for future grants, and there were 568,900 shares remaining available for grant. All other plans have been frozen as to new grants.

In 2019, the Company awarded fully vested stock grants under the 2018 Omnibus Plan of 10,569 common shares to its independent directors. The value of the stock grant totaled $130,000 with each director receiving 813 shares.

For years when stock options were granted the estimated weighted average fair market value of each option awarded, using the Black-Scholes option pricing model, together with the assumptions used in estimating those weighted average fair values, are displayed below:

	2019	2018	2017
Estimated fair value of options granted	$ 5.99	$ 6.07	$ 5.47
Assumptions in estimating average option values:			
Risk-free interest rate	2.59%	2.94%	2.07%
Dividend yield	-%	-%	-%
Volatility	42.18%	36.67%	42.42%
Expected life (in years)	8.00	8.00	8.00

A summary of the Company's option plans as of and for the year ended December 31, 2019 is as follows:

	Outstanding Options			Exercisable Options	
	Shares Available for Future Grants	Number Outstanding	Weighted Average Exercise Price	Number Outstanding	Weighted Average Exercise Price
At December 31, 2018	597,500	239,955	$ 8.63	113,013	$ 6.71
Options granted/vested	(58,500)	58,500	-	35,660	-
Stock grants	(10,569)	-	12.30	-	-
Options exercised	26,813	(26,813)	8.50	(26,813)	8.50
Options expired	-	-	-	-	-
Options forfeited	3,100	(3,100)	10.92	(200)	$ 5.25
At December 31, 2019	568,913	268,542	$ 9.55	121,660	$ 7.80

The aggregate intrinsic value of options outstanding as of December 31, 2019 and 2018 was $740,000 and $900,000, respectively. The aggregate intrinsic value of options exercisable as of December 31, 2019 and 2018 was $548,000 and $641,000, respectively. The unrecognized compensation expense for outstanding options at December 31, 2019, 2018, and 2017 was $460,000, $642,000, and $768,000, respectively. As of December 31, 2019, this cost is expected to be recognized over a weighted average period of 1.62 years.

The weighted average remaining life of options outstanding and options exercisable as of December 31, 2019 was 6.57 years and 4.85 years, respectively. The weighted average remaining life of options outstanding and options exercisable as of December 31, 2018 was 6.57 years and 4.75 years, respectively. Information regarding the stock options outstanding at December 31, 2019 is summarized below:

Range of Exercise Prices	Number of options outstanding	Number of options exercisable
\$2.25 - \$7.07	67,922	62,920
\$7.08 - \$10.69	41,620	18,040
\$10.70 - \$12.99	159,000	40,700
Outstanding at end of year	268,542	121,660

A summary of the status of the Company's non-vested options as of December 31, 2019 and changes during the year ended December 31, 2019, is presented below:

Non-vested Options	Options	Weighted-Average Grant Date Fair Value
Non-vested at December 31, 2018	126,942	\$ 5.16
Granted	58,500	5.99
Vested	(35,660)	5.02
Expired	-	-
Forfeited	(3,100)	5.55
Non-vested at December 31, 2019	146,882	5.51

For the years ended December 31, 2019, 2018 and 2017, the intrinsic value of options exercised was \$148,000, \$213,000 and \$197,000, respectively. For the years ended December 31, 2019, 2018 and 2017, the grant-date fair value of options vested was \$179,000, \$181,000, and \$66,000, respectively. In addition, there were no stock options acquired in the Premara merger. For the years ended December 31, 2019 and 2018, respectively, \$68,000 and \$79,000 in tax benefits were recognized from non-qualified stock option exercises.

NOTE Q - PARENT COMPANY FINANCIAL DATA

Following are the condensed balance sheets of Select Bancorp as of and for the years ended December 31, 2019 and 2018 and the related condensed statements of operations and cash flows for each of the years in the three-year period ended December 31, 2019:

Condensed Balance Sheets
December 31, 2019 and 2018
(dollars in thousands)

	2019	2018
Assets		
Cash balances with Select Bank & Trust	$ 22,556	$ 34,949
Investment in Select Bank & Trust	196,536	181,442
Investment in New Century Statutory Trust I	598	580
Other assets	5,711	5,255
Total Assets	$ 225,401	$ 222,226
Liabilities and Shareholders' Equity		
Junior subordinated debentures	$ 12,372	$ 12,372
Accrued interest and other liabilities	254	243
Total Liabilities	12,626	12,615
Shareholders' equity:		
Preferred stock	-	-
Common stock	18,330	19,312
Additional paid-in capital	140,870	150,718
Retained earnings	52,675	39,640
Common stock issued to deferred compensation trust	(2,815)	(2,615)
Directors' Deferred Compensation Plan Rabbi Trust	2,815	2,615
Accumulated other comprehensive income (loss)	900	(59)
Total Shareholders' Equity	212,775	209,611
Total Liabilities and Shareholders' Equity	$ 225,401	$ 222,226

Condensed Statements of Operations
Years Ended December 31, 2019, 2018 and 2017
(dollars in thousands)

	2019	2018	2017
Equity in earnings of subsidiaries	$ 14,153	$ 39,153	$ (9,236)
Dividends received for subsidiary	-	(25,000)	-
Dividends in excess of earnings	434	642	13,291
Operating expense	(1,862)	(1,275)	(1,175)
Income tax benefit	310	262	305
Net income	$ 13,035	$ 13,782	$ 3,185

Condensed Statements of Cash Flows
Years Ended December 31, 2019, 2018 and 2017
(dollars in thousands)

	2019	2018	2017
CASH FLOWS FROM OPERATING ACTIVITIES			
Net income	$ 13,035	$ 13,782	$ 3,185
Equity in undistributed income of subsidiaries	(14,153)	(39,153)	9,236
Stock based compensation	369	178	115
Net change in other assets	(456)	(283)	(315)
Net change in other liabilities	11	(12,185)	12,066
Net cash provided by (used in) operating activities	(1,194)	(37,661)	24,287
CASH FLOWS FROM INVESTING ACTIVITIES			
Cash received from acquisition	-	-	257
Investment in subsidiary	-	-	(12,407)
Net cash used in investing activities	-	-	(12,150)
CASH FLOWS FROM FINANCING ACTIVITIES			
Proceeds from stock option exercises	228	187	166
Repurchase of common stock	(11,427)	-	-
Proceeds from the issuance of common stock	-	63,250	-
Direct expenses related to capital transaction	-	(3,444)	-
Net cash provided by (used in) financing activities	(11,199)	59,993	166
Net (decrease) increase in cash and cash equivalents	(12,393)	22,332	12,303
Cash and cash equivalents at beginning of year	34,949	12,617	314
Cash and cash equivalents, end of year	$ 22,556	$ 34,949	$ 12,617

NOTE R - RELATED PARTY TRANSACTIONS

The Bank has had, and expects to have in the future, banking and other transactions in the ordinary course of business with certain of its current directors, nominees for director, executive officers and associates. All such transactions are made on substantially the same terms, including interest rates, repayment terms and collateral, as those prevailing for comparable transactions with persons not related to the lender, and do not involve more than the normal risk of collection or present other unfavorable features.

The Bank has loan transactions with its directors and executive officers in the regular course of business. Such loans were made in the ordinary course of business and on substantially the same terms and collateral as those for comparable transactions prevailing at the time and did not involve more than the normal risk of collectability or present other unfavorable features. The following table represents loan transactions for directors and executive officers who held that position as of December 31, 2019 and 2018. A summary of related party loan transactions, is as follows:

	2019	2018
	(dollars in thousands)	
Balance at January 1	$ 12,658	$ 13,520
Exposure of directors/executive officers added	-	-
Borrowings	5,110	1,312
Directors/executive officers resigned or retired from board	(647)	-
Loan repayments	(9,894)	(2,174)
Balance at December 31	$ 7,227	$ 12,658

At December 31, 2019, there was $2.8 million of unused lines of credit outstanding to directors and executive officers of the Company and its subsidiaries. Directors and executive officers had $35.5 million deposited with the Company at December 31, 2019.

NOTE S – CAPITAL TRANSACTIONS

Common Stock

On August 27, 2018, the Company and the Bank entered into an underwriting agreement (the "Underwriting Agreement") with FIG Partners, LLC, as the underwriter named therein (the "Underwriter"), pursuant to which the Company agreed to issue and sell to the Underwriter and the Underwriter agreed to purchase, subject to and upon the terms and conditions of the Underwriting Agreement, an aggregate of 4,583,334 shares of the Company's common stock, par value $1.00 per share, at a public offering price of $12.00 per share less underwriting discounts and commissions in an underwritten public offering (the "Offering"). The Company granted the Underwriter an option for a period of 30 days after the date of the Underwriting Agreement to purchase up to an additional 687,500 shares of common stock at the public offering price. The Underwriter exercised its option in full resulting in a total of 5,270,834 shares of common stock being issued and sold in the Offering. The Offering closed on August 30, 2018. The net proceeds to the Company, after deducting underwriting discounts and commissions and offering expenses, were approximately $59.8 million.

In addition to the Offering, during 2017 the capital of the Company also increased due to the acquisition of Premara and its subsidiary bank, Carolina Premier Bank, on December 15, 2017. Premara had 3,179,808 shares of common stock outstanding as of the merger closing date. Under the terms of the merger agreement, 948,080 shares of Premara common stock (equivalent to 30% of Premara's outstanding shares of common stock as of the date of the merger agreement) were converted to the $12.65 per share cash merger consideration, for aggregate cash consideration of $11,993,212 (exclusive of cash paid-in-lieu of fractional shares). The remaining 2,231,728 Premara common shares were converted into stock consideration at the merger exchange ratio of 1.0463 shares of Company common stock for each share of Premara common stock, resulting in the issuance of 2,334,999 new shares of Company common stock in the merger.

In August of 2016 the Board of Directors approved a common stock repurchase plan in which 581,518 shares were authorized for repurchase at management's discretion. During the second quarter of 2019 the Company began repurchasing shares and by September 10, 2019 had repurchased all authorized shares. On September 17, 2019 the Board of Directors approved Plan 2 which authorized the repurchase of 937,248 shares of common stock. In the third and fourth quarters of 2019 the Company repurchased 426,742 shares and has 510,506 shares remaining in Plan 2.

NOTE T – LEASES

The Company has operating leases for branches and certain equipment. The Company's leases have remaining lease terms of 1 year to 15 years which may include options to extend the leases for up to 5 years per option period. The Company has some leases that are month to month or expire within 1 year that are not included below.

At December 31, 2019, the Company did not have any leases that had not yet commenced for which the Company had created a ROU asset and a lease liability. For the operating leases the Company has elected the practical expedient of not separating lease components from non-lease components and instead to account for each separate lease component and the non-lease components associated with that lease as a single lease component. The Company's lease agreements do not contain any material residual value guarantees or material restrictive covenants. Most of the lease agreements include periodic rate adjustments for inflation.

Most leases include one or more options to renew, with renewal terms that can extend the lease term from 1 to 25 years. The exercise of lease renewal options is at our sole discretion. When it is reasonably certain that the Company will exercise the option to renew or extend the lease term, that option is included in determining the value of the ROU asset and lease liability.

The Company has operating leases for its corporate offices and branches that expire at various times through 2034. Future minimum lease payments under the leases for years subsequent to December 31, 2019 are as follows:

	Total Lease Payments
	(dollars in thousands)
2020	$ 1,071
2021	1,097
2022	1,128
2023	1,063
2024	996
Years thereafter	6,400
	$ 11,755

During 2019, 2018, and 2017, payments under operating leases were approximately $1.1 million, $1.2 million, and $408,000, respectively. Lease expense was accounted for on a straight line basis. Rental income earned on office space leased to third parties was $449,000, $426,000 and $148,000 for 2019, 2018 and 2017, respectively.

The components of lease expense were as follows (dollars in thousands):

	December 31, 2019
Operating lease cost	$ 1,054

Supplemental cash flow information related to leases was as follows:

	December 31, 2019
Cash paid for amounts included in the measurement of lease liabilities:	
Operating cash flows from operating leases	$ 1,054
Right-of-use assets obtained in exchange for lease obligations:	
Operating leases	8,596
The following table presents the remaining weighted average lease terms and discount rates as of December 31, 2019:	
Weighted Average Remaining Lease Term	
Operating leases	6.8 years
Weighted Average Discount Rate	
Operating leases	6.0%

Maturities of lease liabilities were as follows:
(In thousands)

	Operating Leases
Year Ending December 31,	
2020	$ 580
2021	642
2022	714
2023	693
2024	665
Thereafter	5,150
Lease payments	8,444
Amounts representing interest	(269)
Present Value of Net Future Minimum Lease Payments	8,175

NOTE U – SUBSEQUENT EVENTS

The Company has evaluated for subsequent events through the date and time the financial statements were issued and has determined there are no reportable subsequent events.

ITEM 9 – CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

ITEM 9A – CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

At the end of the period covered by this report, the Company carried out an evaluation, under the supervision and with the participation of the Company's management, including the Company's Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures pursuant to Securities Exchange Act Rule 13a-15.

Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that the Company's disclosure controls and procedures were effective (1) to provide reasonable assurance that information required to be disclosed by the Company in the reports filed or submitted by it under the Securities Exchange Act was recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and (2) to provide reasonable assurance that information required to be disclosed by the Company in such reports is accumulated and communicated to the Company's management, including its Chief Executive Officer and Chief Financial Officer, as appropriate to allow for timely decisions regarding required disclosure.

Management's Annual Report on Internal Control over Financial Reporting

Management is responsible for preparing the Company's annual consolidated financial statements and for establishing and maintaining adequate internal control over financial reporting for the Company. The Company's internal control over financial reporting is a process designed under the supervision of the Company's Chief Executive Officer and Chief Financial Officer to provide reasonable assurance regarding the reliability of financial reporting and the preparation of the Company's financial statements for external reporting purposes in accordance with U.S. generally accepted accounting principles.

All internal control systems, no matter how well designed, have inherent limitations. Therefore, even systems that are deemed to be effective can provide only reasonable assurance with respect to financial statement preparation and presentation. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate due to changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Management has made a comprehensive review, evaluation and assessment of the Company's internal control over financial reporting as of December 31, 2019. In making its assessment of internal control over financial reporting as of December 31, 2019, Management used the criteria issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO") in *Internal Control−Integrated Framework (2013)* (the "2013 Framework").

Based on this assessment, Management has concluded that that the Company's internal control over financial reporting as of December 31, 2019 was effective based on those criteria.

The effectiveness of the Company's internal control over financial reporting as of December 31, 2019 has been audited by Dixon Hughes Goodman LLP, an independent registered public accounting firm, as stated in their report which appears under Item 8 of Part II of this annual report.

Date: March 11, 2020	/s/ William L. Hedgepeth II William L. Hedgepeth II President and Chief Executive Officer
Date: March 11, 2020	/s/ Mark A. Jeffries Mark A. Jeffries Executive Vice President, Chief Financial Officer

Changes in Internal Control over Financial Reporting

Management of the Company has evaluated, with the participation of the Company's Chief Executive Officer and Chief Financial Officer, changes in the Company's internal controls over financial reporting (as defined in Rule 13a−15(f) and 15d−15(f) of the Exchange Act) during the fourth quarter of 2019. Management has concluded that there have been no changes to the Company’s internal controls over financial reporting that occurred since the beginning of the Company’s fourth quarter of 2019 that have materially affected, or are likely to materially affect, the Company’s internal control over financial reporting.

ITEM 9B – OTHER INFORMATION

None.

PART III

ITEM 10 – DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

Incorporated by reference to the Registrant’s Proxy Statement for the 2020 Annual Meeting of Shareholders.

The Registrant has adopted a code of ethics for its directors as well as a code of ethics specifically for its senior financial officers. Each of these policies is posted in the “Investor Overview - Governance Documents” section of the “Investor Relations” page of the Registrant’s website: www.selectbank.com.

ITEM 11 - EXECUTIVE COMPENSATION

Incorporated by reference to the Registrant’s Proxy Statement for the 2020 Annual Meeting of Shareholders.

ITEM 12 - SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

The information required by Item 403 of Regulation S-K is incorporated by reference to the Registrant's Proxy Statement for the 2020 Annual Meeting of Shareholders.

Equity Compensation Plan Information. At December 31, 2019, the Registrant had awards outstanding under the following equity compensation plans:

- 2004 Incentive Stock Option Plan;
- 2008 Omnibus Stock Ownership and Long Term Incentive Plan, which plan was assumed in connection with Registrant's 2014 acquisition of Select Bancorp, Inc., Greenville, NC;
- 2010 Omnibus Stock Ownership and Long Term Incentive Plan; and
- 2018 Omnibus Stock Incentive Plan (the "2018 Omnibus Plan").

The Registrant's shareholders have approved all equity-based compensation plans. As of December 31, 2019, the 2018 Omnibus Plan was the only plan that had shares of the Registrant's common stock available for future grants. All other plans have been frozen as to new grants.

The following table contains aggregated plan information as of December 31, 2019, with respect to the Registrant's equity compensation plans under which equity securities are authorized for issuance:

Plan Category	Number of securities to be issued upon exercise of outstanding options	Weighted- average exercise price of outstanding options, warrants and rights	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))
	(a)	(b)	(c)
Equity compensation plans approved by security holders	268,542	$ 9.55	568,913
Equity compensation plans not approved by security holders	none	n/a	none
Total	268,542	$ 9.55	568,913

ITEM 13 – CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

Incorporated by reference to the Registrant's Proxy Statement for the 2020 Annual Meeting of Shareholders.

ITEM 14 – PRINCIPAL ACCOUNTING FEES AND SERVICES

Incorporated by reference to the Registrant's Proxy Statement for the 2020 Annual Meeting of Shareholders.

PART IV

ITEM 15 – EXHIBITS, FINANCIAL STATEMENT SCHEDULES

(a) The following documents are filed as part of this report:

1. Financial statements required to be filed by Item 8 of this Form:

Report of Independent Registered Public Accounting Firm

Consolidated Balance Sheets as of December 31, 2019 and 2018

Consolidated Statements of Operations for the years ended December 31, 2019, 2018 and 2017

Consolidated Statements of Comprehensive Income for the years ended December 31, 2019, 2018 and 2017

Consolidated Statements of Changes in Shareholders' Equity for the years ended December 31, 2019, 2018 and 2017

Consolidated Statements of Cash Flows for the years ended December 31, 2019, 2018 and 2017

Notes to Consolidated Financial Statements.

2. Financial statement schedules required to be filed by Item 8 of this Form:

   None

3. Exhibits: See below exhibit index.

Exhibit No.	Description of Exhibit	Incorporated by Reference (Unless Otherwise Indicated)			
		Form	Exhibit	Filing Date	SEC File No.
2.1	Agreement and Plan of Merger and Reorganization by and among Registrant, Select Bank & Trust Company, Premara Financial, Inc., and Carolina Premier Bank dated as of July 20, 2017	8-K	2.1	07/26/17	000-50400
2.2	Branch Purchase and Assumption Agreement by and between Select Bank & Trust Company and Entegra Bank dated as of December 20, 2019	8-K	2.1	12/27/19	000-50400
3.1	Articles of Incorporation	10-KSB	3.1	03/30/04	000-50400
3.2	Articles of Amendment	8-K	3.1	08/26/11	000-50400
3.3	Articles of Amendment	8-K	3.1	07/29/14	000-50400
3.4	Amendment to Articles (contained within plan of merger)	8-K	3.2	07/29/14	000-50400
3.5	Articles of Amendment	10-Q	3.1	08/09/19	000-50400
3.6	Bylaws	8-K	3.1	05/24/19	000-50400
4.1	Form of Stock Certificate	S-8	4.1	10/01/14	333-199090
4.2	Description of Securities Registered pursuant to Section 12 of the Securities Exchange Act of 1934	-	-	Filed herewith	-
10.1	2004 Incentive Stock Option Plan (compensatory plan)	S-8	99.1	07/19/04	333-117476
10.2	2010 Omnibus Stock Ownership and Long-Term Incentive Plan (compensatory plan)	8-K	99.1	08/02/10	000-50400
10.3	2018 Omnibus Stock Incentive Plan (compensatory plan)	8-K	10.1	05/24/18	000-50400
10.4	Directors' Deferral Plan, as amended and restated (compensatory plan)	10-K	10.10	03/16/18	000-50400
10.5	Employment Agreement with William L. Hedgepeth II (management contract)	10-K	10.7	03/31/08	000-50400
10.6	Employment Agreement of W. Keith Betts (management contract)	8-K	10.1	01/12/17	000-50400

Exhibit No.	Description of Exhibit	Incorporated by Reference (Unless Otherwise Indicated) Form	Exhibit	Filing Date	SEC File No.
10.7	First Amendment to Employment Agreement of W. Keith Betts (management contract)	8-K	10.2	01/28/19	000-50400
10.7	Employment Agreement of Mark A. Jeffries (management contract)	10-K	10.12	03/31/15	000-50400
10.8	First Amendment to Employment Agreement of Mark A. Jeffries (management contract)	8-K	10.1	01/28/19	000-50400
10.9	Employment Agreement of Lynn H. Johnson (management contract)	10-K	10.11	03/31/15	000-50400
10.10	First Amendment to Employment Agreement of Lynn H. Johnson (management contract)	8-K	10.1	02/26/18	000-50400
10.11	Employment Agreement of D. Richard Tobin, Jr. (management contract)	10-K	10.8	03/28/13	000-50400
10.12	2019 Supplemental Executive Retirement Plan Agreement with William L. Hedgepeth II (compensatory plan)	8-K	10.1	09/24/19	000-50400
10.13	2019 Supplemental Executive Retirement Plan Agreement with Lynn H. Johnson (compensatory plan)	8-K	10.2	09/24/19	000-50400
21.1	Subsidiaries	-	-	Filed herewith	-
23.1	Consent of Dixon Hughes Goodman LLP	-	-	Filed herewith	-
31.1	Certification of Principal Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act	-	-	Filed herewith	-
31.2	Certification of Principal Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act	-	-	Filed herewith	-
32.1	Certification of Principal Executive Officer Pursuant to Section 906 of the Sarbanes-Oxley Act	-	-	Furnished herewith	-

Exhibit No.	Description of Exhibit	Incorporated by Reference (Unless Otherwise Indicated) Form	Exhibit	Filing Date	SEC File No.
32.2	Certification of Principal Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act	-	-	Furnished herewith	-
101	The following financial information formatted in XBRL (eXtensible Business Reporting Language) includes: (i) the Consolidated Balance Sheets as of December 31, 2019 and 2018; (ii) the Consolidated Statements of Operations for the years ended December 31, 2019, 2018 and 2017; (ii) the Consolidated Statements of Comprehensive Income for the years ended December 31, 2019, 2018 and 2017; (iv) the Consolidated Statements of Changes in Shareholders' Equity for the years ended December 31, 2019, 2018 and 2017; (v) the Consolidated Statements of Cash Flows for the years ended December 31, 2019, 2018 and 2017; and (vi) Notes to Consolidated Financial Statements, tagged as blocks of text	-	-	Filed herewith	-

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) 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.

SELECT BANCORP, INC.
Registrant

By: /s/ William L. Hedgepeth II
William L. Hedgepeth, II
President and Chief Executive Officer

Date: March 11, 2020

Pursuant to the Securities Exchange Act of 1934, this Report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates indicated.

/s/ William L. Hedgepeth, II William L. Hedgepeth, II., President, Chief Executive Officer and Director	March 11, 2020
/s/ Mark A. Jeffries Mark A. Jeffries, Executive Vice President and Chief Financial Officer (Principal Financial Officer and Principal Accounting Officer)	March 11, 2020
/s/ J. Gary Ciccone J. Gary Ciccone, Director	March 11, 2020
/s/ James H. Glen, Jr. James H. Glen, Jr. Director	March 11, 2020
/s/ Alicia S. Hawk Alicia S. Hawk, Director	March 11, 2020
/s/ Gerald W. Hayes, Jr. Gerald W. Hayes, Jr., Director	March 11, 2020
/s/ Ronald V. Jackson Ronald V. Jackson, Director	March 11, 2020
/s/ John W. McCauley John W. McCauley, Director	March 11, 2020
/s/ Carlie C. McLamb, Jr. Carlie C. McLamb Jr., Director	March 11, 2020
/s/ V. Parker Overton V. Parker Overton, Director	March 11, 2020
/s/ Anthony E. Rand Anthony E. Rand, Director	March 11, 2020
/s/ Sharon L. Raynor Sharon L. Raynor, Director	March 11, 2020
/s/ K. Clark Stallings K. Clark Stallings, Director	March 11, 2020
/s/ W. Lyndo Tippett W. Lyndo Tippett, Director	March 11, 2020

Section 2: EX-4.2 (EXHIBIT 4.2)

Exhibit 4.2

DESCRIPTION OF THE REGISTRANT'S SECURITIES REGISTERED PURSUANT TO SECTION 12 OF THE SECURITIES EXCHANGE ACT OF 1934

The following description sets forth certain material terms and provisions of the securities of Select Bancorp, Inc. (the "Company," "we," "us," or "our"), that are registered under Section 12 of the Securities Exchange Act of 1934. The following summary does not purport to be complete and is subject to, and is qualified in its entirety by reference to, the applicable provisions of our articles of incorporation, as amended, and our bylaws, copies of which are incorporated by reference as an exhibit to the Annual Report on Form 10-K of which this Exhibit 4.2 is a part. We encourage you to read our articles of incorporation, as amended, and our bylaws for additional information.

Description of Common Stock, $1.00 Par Value Per Share

General. Outstanding shares of our common stock are validly issued, fully paid and non-assessable. Each share of our common stock has the same relative rights and is identical in all respects to each other share of our common stock.

Voting Rights. Each share of our common stock entitles the holder thereof to one vote on all matters upon which shareholders have the right to vote. Our shareholders are not entitled to cumulate their votes for the election of directors. Directors are elected by a plurality of votes cast. In addition, if our board of directors consists of nine or more directors, the board members will be classified into three groups so that approximately one-third of the directors will be elected each year. One of the effects of these "staggered" director terms is that it makes it more difficult to affect a change in majority control of our board of directors.

Liquidation. In the event of any liquidation, dissolution, or winding up of our affairs, the holders of shares of our common stock are entitled to receive, after payment of all debts and liabilities and the liquidation preference of any then-outstanding preferred stock, all of our remaining assets available for distribution in cash or in kind.

Dividends. Subject to preferences to which holders of any shares of our preferred stock may be entitled, holders of our common stock are entitled to receive ratably any dividends that may be declared from time to time by the board of directors out of funds legally available for that purpose. Under North Carolina law, cash dividends may not be paid if a corporation will not be able to pay its debts as they become due in the usual course of business after making such cash dividend distribution or the corporation's total assets would be less than the sum of its total liabilities plus the amount that would be needed to satisfy certain preferential liquidation rights. It is the current policy of the Board of Governors of the Federal Reserve System (the "Federal Reserve") that bank holding companies should pay cash dividends on capital stock only out of net income available over the past year and only if prospective earnings retention is consistent with the organization's expected future needs and financial condition.

Our ability to pay cash dividends to the holders of shares of our common stock is, at the present time and for the foreseeable future, largely dependent upon the amount of cash dividends that our wholly owned subsidiary, Select Bank & Trust Company ("Select Bank"), may pay to us. North Carolina commercial banks, such as Select Bank, are subject to legal limitations on the amounts of dividends they are permitted to pay. Also, an insured depository institution, such as Select Bank, is prohibited from making capital distributions, including the payment of dividends, if, after making such distribution, the institution would become "undercapitalized," as such term is defined in applicable law and regulations. The declaration and payment of future dividends to holders of our common stock will also depend upon our earnings and financial condition, the capital requirements of Select Bank, regulatory conditions, and other factors as our board of directors may deem relevant.

No Preemptive Rights, Conversion Rights, Redemption Rights, or Sinking Fund. Holders of our common stock do not have preemptive, conversion, or redemption rights; our common stock does not have any sinking fund provisions.

Restrictions on Ownership. The Bank Holding Company Act of 1956 (the "BHCA") requires any "bank holding company," as defined in the BHCA, to obtain the approval of the Federal Reserve before acquiring 5% or more of our voting common stock. Any person, other than a bank holding company, is required to obtain the approval of the Federal Reserve before acquiring 10% or more of our common stock under the Change in Bank Control Act. Any holder of 25% or more of our common stock, or a holder of 5% or more if such holder otherwise exercises a "controlling influence" over us, is subject to regulation as a bank holding company under the BHCA.

Preferred Stock. Under our articles of incorporation, as amended, our board of directors, without further action by our shareholders, is authorized to issue shares of preferred stock in one or more series. Our board of directors may fix the rights, preferences and privileges of the preferred stock, along with any limitations or restrictions, including voting rights, dividend rights, conversion rights, redemption privileges and liquidation preferences of each series of preferred stock. The shares of preferred stock could have voting or conversion rights that could adversely affect the voting power or other rights of holders of shares of our common stock.

Charter and Bylaw Provisions Having Potential Anti-Takeover Effects

The following paragraphs summarize certain provisions of our articles of incorporation and bylaws that may have the effect, or be used as a means, of delaying or preventing attempts to acquire or take control of the Company, or to remove or replace incumbent directors, that are not first approved by our board of directors, even if those proposed actions are favored by our shareholders. All references to our articles of incorporation reference such articles as amended to date.

Authorized Shares. Our board of directors is authorized to approve the issuance of shares of our common stock or preferred stock from time to time and, in the case of preferred stock, to create separate series of preferred stock within the class, and to determine the number of shares, designations, terms, relative rights, preferences and limitations of the preferred stock, or of shares within each series of preferred stock, at the time of issuance, all by its resolution. Those provisions give our board of directors considerable flexibility to effect, among other transactions, financings, acquisitions, stock dividends, stock splits, and grants of stock options. However, the board's authority also could be used, consistent with the board's fiduciary duty, to deter future attempts to gain control of the Company by issuing additional common stock, or by issuing a series of preferred stock, to persons friendly to management in order to attempt to block a tender offer, merger, or other transaction by which a third party seeks to gain control.

Super-majority Vote Requirement for Certain Business Combinations. Our articles of incorporation require the affirmative vote of 66 2⁄3% of the outstanding shares of all classes of our common stock entitled to vote to approve any agreement, plan, or arrangement providing for the merger, consolidation or exchange of our shares with any other corporation or the sale, lease, or exchange of all or substantially all of our assets, unless the proposed transaction is approved by the vote of at least a majority of the members of our board of directors who are unaffiliated with any other party to the proposed transaction. This provision could tend to make the acquisition of the Company more difficult to accomplish without the cooperation or favorable recommendation of our board of directors.

Other Constituency Considerations. When evaluating business combinations or transactions and determining what is in the best interests of the Company and our shareholders, our articles of incorporation provide that our board of directors (or any individual member) may, but is not required, to consider: (i) the social and economic effects of the transaction or the matter to be considered on the Company and its subsidiaries, its and their employees, depositors, customers, and creditors, and the communities in which the Company and its subsidiaries operate or are located; (ii) the business and financial condition and earnings prospects of the acquiring person(s) or entity, including, but not limited to, debt service and other existing financial obligations, financial obligations to be incurred in connection with the acquisition, and other likely financial obligations of the acquiring person or entity, and the possible effect of such conditions upon the Company and its subsidiaries and the communities in which the Company and its subsidiaries operate or are located; (iii) the competence, experience, and integrity of the acquiring person(s) or entity and its or their management; and (iv) the prospects for successful conclusion of the business combination, offer or proposal.

Advance Notice of Director Nominations. Our bylaws provide that in order to be eligible for consideration at a meeting of shareholders, all nominations for election to the board of directors, other than those made by our nominating committee, must be in writing and submitted to our corporate secretary no later than September 30th of the year preceding the meeting of shareholders at which the nominee would stand for election and must be accompanied by the nominee's written consent to serve, if elected, and a certification that the nominee has owned at least 1,000 shares of our common stock for the twelve months preceding the nomination and has business, economic, and residential ties to our market area. Only shareholders entitled to vote at the meeting at which directors are elected may make recommendations for nominations to our board of directors.

Special Meetings of Shareholders. Our bylaws provide that special meetings of our shareholders may be called only by or at the direction of (a) the chairman of our board of directors, (b) the president of the Company, or (c) the corporate secretary of the Company at the request of the board of directors of the Company.

Amendment of Bylaws. Subject to certain limitations under North Carolina law, our bylaws may be amended or repealed by either our board of directors or our shareholders. Therefore, our board of directors is authorized to amend or repeal bylaws without the approval of our shareholders. However, a bylaw adopted, amended or repealed by our shareholders may not be readopted, amended or repealed by the board alone unless our articles of incorporation or a bylaw adopted by our shareholders authorizes the board to adopt, amend or repeal that particular bylaw or the bylaws generally.

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Section 3: EX-21.1 (EXHIBIT 21.1)

Exhibit 21.1

Subsidiaries of Select Bancorp, Inc.

Select Bank & Trust Company, Dunn, North Carolina
(a North Carolina chartered banking corporation)

New Century Statutory Trust I *
(a Delaware Statutory Trust)

* Unconsolidated subsidiary

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Section 4: EX-23 (EXHIBIT 23)

Exhibit 23

CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors
Select Bancorp, Inc.

We consent to the incorporation by reference in the registration statements on Form S-8 (File Nos. 333-225204, 333-199090, 333-168937, 333-127194, 333-117816 and 333-117476) and Form S-3 (File No. 333-225805) of Select Bancorp, Inc. of our reports dated March 11, 2020, with respect to the consolidated financial statements of Select Bancorp, Inc. and the effectiveness of internal control over financial reporting as of December 31, 2019, which reports appear in Select Bancorp, Inc.'s 2019 Annual Report on Form 10-K.

/s/ Dixon Hughes Goodman LLP

Raleigh, North Carolina
March 11, 2020

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Section 5: EX-31.1 (EXHIBIT 31.1)

Exhibit 31.1

CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER

Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, William L. Hedgepeth II, certify that:

1. I have reviewed this annual report on Form 10-K of Select Bancorp, Inc. (the "registrant");

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f) for the registrant and have:

   a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   c. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   d. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 11, 2020

/s/ William L. Hedgepeth II
William L. Hedgepeth II
President and Chief Executive Officer
(Principal Executive Officer)

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Section 6: EX-31.2 (EXHIBIT 31.2)

Exhibit 31.2

CERTIFICATION OF PRINCIPAL FINANCIAL OFFICER

Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, Mark A. Jeffries, certify that:

1. I have reviewed this annual report on Form 10-K of Select Bancorp, Inc. (the "registrant");

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f) for the registrant and have:

   a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that all material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   c. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   d. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 11, 2020

/s/ Mark A. Jeffries
Mark A. Jeffries
Executive Vice President and Chief Financial Officer
(Principal Financial Officer)

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Section 7: EX-32.1 (EXHIBIT 32.1)

Exhibit 32.1

Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

The undersigned hereby certifies that, to his knowledge, **(i)** the Form 10-K filed by Select Bancorp, Inc. (the "Issuer") for the year ended December 31, 2019, fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, and **(ii)** the information contained in that report fairly presents, in all material respects, the financial condition and results of operations of the Issuer on the dates and for the periods presented therein.

Date: March 11, 2020

/s/ William L. Hedgepeth II
William L. Hedgepeth II
President and Chief Executive Officer
(Principal Executive Officer)

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Section 8: EX-32.2 (EXHIBIT 32.2)

Exhibit 32.2

Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

The undersigned hereby certifies that, to her knowledge, **(i)** the Form 10-K filed by Select Bancorp, Inc. (the "Issuer") for the year ended December 31, 2019, fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, and **(ii)** the information contained in that report fairly presents, in all material respects, the financial condition and results of operations of the Issuer on the dates and for the periods presented therein.

Date: March 11, 2020

/s/ Mark A. Jeffries
Mark A. Jeffries
Chief Financial Officer

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