

1st Colonial Bancorp, Inc.

2019 ANNUAL REPORT



1st Colonial Bancorp, Inc.

April 30, 2020

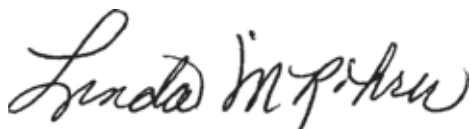
Dear Fellow Shareholders,

As we find ourselves deeply entrenched in dealing with the effects of the COVID-19 pandemic, we want to assure you that we remain very focused on the execution of our strategic initiatives. The health and welfare of our team members and customers are of paramount concern, as we continue to take all precautions to limit the potential spread of the coronavirus during these unprecedented times. As a result of our strong risk management culture, we launched our business continuity and pandemic plans before the stay-at-home orders were issued. Our ability to operate remotely, as well as balance the need for social distancing while in our offices, has proven to be effective and beneficial. The experience and commitment of our team members proved invaluable at our greatest time of need. Challenges like these will make us stronger, better, and more unified than ever before.

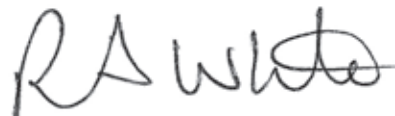
As we look back on our 2019 financial results, key priorities include improving our operating metrics and financial performance. We have realigned our commercial lending teams, as well as updated our credit policy to ensure that we are originating high quality loans, with a more focused approach towards full relationship banking. The costs associated with managing the increased level of non-performing loans negatively impacted our 2019 performance. We believe that this trend will improve, as we deal with these previously identified troubled credits. We have taken steps during the first quarter of 2020 to increase our reserves based on qualitative factor adjustments related to the pandemic. Additionally, the inverted yield curve in 2019 created additional pricing pressure on loans and deposits and accounted for the lack of growth in net interest income, our primary source of revenue.

For 2020, we remain firmly determined to execute our strategic priorities. We are investing in highly qualified, high-performing team members with experience, depth, and strong customer following, and bringing people onboard with the same values and cultural aspirations. We continue to focus on originating high quality loans, with more emphasis on building relationships, while diversifying our loan and deposit mix. Organizational changes made during the quarter will position us well as we execute upon our strategy. Investments in technology and expansion of our digital and online presence will expand our ability to deliver the bank to our customers and prospects. Although economic headwinds in 2020 are apparent, we believe that we have realigned the Company and are well positioned for the future.

Sincerely,



Linda M. Rohrer
Chairman of the Board



Robert B. White
President & Chief Executive Officer

1ST COLONIAL BANCORP, INC. AND SUBSIDIARY

Consolidated Financial Statements

December 31, 2019 and 2018

(With Independent Auditors' Report Thereon)



KPMG LLP
1601 Market Street
Philadelphia, PA 19103-2499

Independent Auditors' Report

The Board of Directors
1st Colonial Bancorp, Inc.:

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of 1st Colonial Bancorp, Inc. and its subsidiary, which comprise the consolidated statement of financial position as of December 31, 2019 and 2018, and the related consolidated statements of income, comprehensive income, changes in stockholders' equity, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of *consolidated* financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of 1st Colonial Bancorp, Inc. and its subsidiary as of December 31, 2019 and 2018, and the results of their operations and their cash flows for the years then ended in accordance with U.S. generally accepted accounting principles.

KPMG LLP

Philadelphia, Pennsylvania
April 30, 2020

1ST COLONIAL BANCORP, INC. AND SUBSIDIARY

Consolidated Statements of Financial Condition

	December 31, 2019	December 31, 2018
	(Dollars in thousands, except share data)	
Assets		
Cash and due from banks	\$ 46,348	\$ 12,105
Federal funds sold	9	9
Total cash and cash equivalents	<u>46,357</u>	<u>12,114</u>
Investments held to maturity (fair value of \$42,767 at December 31, 2019 and \$59,126 at December 31, 2018)	42,767	59,126
Securities available for sale ("AFS") (amortized cost of \$50,865 at December 31, 2019 and \$56,351 at December 31, 2018)	51,224	55,967
Bank stock, at cost	2,138	1,964
Mortgage loans held for sale	4,449	2,989
Loans	419,798	404,535
Less allowance for loan losses	<u>(6,671)</u>	<u>(5,627)</u>
Net loans	<u>413,127</u>	<u>398,908</u>
Premises and equipment, net	691	798
Accrued interest receivable	1,697	1,737
Deferred tax assets	1,454	1,023
Bank-owned life insurance	9,807	8,368
Other assets	1,492	944
Total assets	<u>\$ 575,203</u>	<u>\$ 543,938</u>
Liabilities and Shareholders' Equity		
Liabilities:		
Deposits	\$ 522,252	\$ 490,096
Other borrowings	2,290	8,157
Accrued interest payable	130	128
Other liabilities	2,625	1,861
Total liabilities	<u>527,297</u>	<u>500,242</u>
Shareholders' equity:		
Common stock, \$0 par value. Authorized 10,000,000 shares; issued 4,837,610 and 4,747,148 shares as of December 31, 2019 and 2018, respectively, and outstanding of 4,699,734 and 4,609,272 shares at December 31, 2019 and 2018, respectively	-	-
Preferred stock. Authorized 1,000,000 shares, no shares issued	-	-
Additional paid-in capital	36,776	33,719
Retained earnings	11,720	11,101
Accumulated other comprehensive income (loss)	258	(276)
Treasury stock at cost, 137,876 shares	<u>(848)</u>	<u>(848)</u>
Total shareholders' equity	<u>47,906</u>	<u>43,696</u>
Total liabilities and shareholders' equity	<u>\$ 575,203</u>	<u>\$ 543,938</u>

See accompanying notes to consolidated financial statements.

1ST COLONIAL BANCORP, INC. AND SUBSIDIARY

**Consolidated Statements of Operations
For the years ended December 31,**

(Dollars in thousands, except share data)

	<u>2019</u>	<u>2018</u>
Interest income:		
Loans	\$ 21,461	\$ 20,044
Federal funds sold and interest-bearing deposits	338	338
Investments:		
Taxable	1,259	1,409
Nontaxable	933	707
Total interest income	<u>23,991</u>	<u>22,498</u>
Interest expense:		
Deposits	5,369	4,033
Other borrowings	67	21
Total interest expense	<u>5,436</u>	<u>4,054</u>
Net interest income	18,555	18,444
Provision for loan losses	3,184	1,477
Net interest income after provision for loan losses	<u>15,371</u>	<u>16,967</u>
Other income:		
Gain on sales of mortgage loans held for sale	2,111	1,852
Mortgage fee income	242	220
Bank-owned life insurance income	239	577
Service charges on deposit accounts	128	129
Gain on sale of securities	4	-
Gain on sale of guaranteed portion of SBA loans	-	183
Loss on real estate owned	(163)	(39)
Other income and fees	424	442
Total other income	<u>2,985</u>	<u>3,364</u>
Other expenses:		
Compensation and employee benefits	7,786	7,632
Data processing expense	1,481	1,343
Occupancy and equipment expenses	926	927
Professional services	799	843
Impaired loans and other real estate owned expenses	480	62
Advertising expense	308	421
FDIC and state assessments	221	411
Other operating expenses	2,278	1,787
Total other expenses	<u>14,279</u>	<u>13,426</u>
Income before income tax expense	4,077	6,905
Income tax expense	853	1,690
Net income	<u>\$ 3,224</u>	<u>\$ 5,215</u>
Earnings per share:		
Basic earnings per share	\$ 0.69	\$ 1.13
Diluted earnings per share	\$ 0.67	\$ 1.09
Weighted average number of shares outstanding:		
Basic earnings per share	4,670,285	4,604,131
Diluted earnings per share	4,794,168	4,799,385

See accompanying notes to consolidated financial statements.

1ST COLONIAL BANCORP, INC. AND SUBSIDIARY

Consolidated Statements of Comprehensive Income

	For the years ended December 31,					
	2019			2018		
	Before tax amount	Tax expense (benefit)	Net of tax amount	Before tax amount	Tax expense (benefit)	Net of tax amount
(In thousands)						
Net income	\$ 4,077	\$ 853	\$ 3,224	\$ 6,905	\$ 1,690	\$ 5,215
Other comprehensive income (loss):						
Net unrealized gains (losses) on AFS investment securities:						
Net unrealized holding gains (losses) arising during the period	742	205	537	(380)	(105)	(275)
Less reclassification adjustment for net gains on sales realized in net income	4	1	3	-	-	-
Total net unrealized gains (losses) on AFS investment securities	738	204	534	(380)	(105)	(275)
Other comprehensive income (loss)	738	204	534	(380)	(105)	(275)
Total comprehensive income	\$ 4,815	\$ 1,057	\$ 3,758	\$ 6,525	\$ 1,585	\$ 4,940

See accompanying notes to consolidated financial statements.

1ST COLONIAL BANCORP, INC. AND SUBSIDIARY

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

	Common stock	Preferred stock	Additional paid-in capital	Retained earnings	Accumulated other comprehensive income (loss)	Treasury stock	Total shareholders' equity
(In thousands)							
Balance at January 1, 2018	\$ -	\$ -	\$ 30,898	\$ 8,361	\$ (1)	\$ (848)	\$ 38,410
Stock dividend							-
Stock issued			2,475	(2,475)			245
Stock issuance expenses			245				(5)
Net unrealized loss on securities available for sale, net of tax			(5)				
Stock-based compensation			106		(275)		(275)
Net income				5,215			106
Balance at December 31, 2018	-	-	33,719	11,101	(276)	(848)	5,215
Stock dividend			2,605	(2,605)			-
Stock issued			373				373
Stock issuance expenses			(3)				(3)
Net unrealized gain on securities available for sale, net of tax							
Stock-based compensation			82		534		534
Net income				3,224			82
Balance at December 31, 2019	\$ -	\$ -	\$ 36,776	\$ 11,720	\$ 258	\$ (848)	\$ 47,906

See accompanying notes to consolidated financial statements.

1ST COLONIAL BANCORP, INC. AND SUBSIDIARY

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

(In thousands)	2019	2018
Cash flows from operating activities:		
Net income	\$ 3,224	\$ 5,215
Adjustments to reconcile net income to net cash (used in) provided by operating activities:		
Depreciation and amortization	238	226
Net amortization of premium on securities	219	315
Net accretion of deferred fees and costs on loans	(387)	(276)
Stock-based compensation expense	82	106
Gain on sale of investment securities	(4)	-
Gain on sales of mortgage loans held for sale	(2,111)	(1,852)
Gain on sales of guaranteed portion of SBA loans	-	(183)
Provision for loan losses	3,184	1,477
Cash disbursed for mortgage banking activities	(81,450)	(73,696)
Cash received for mortgage banking activities	82,101	79,728
Net losses on sales of OREO	163	39
(Increase) decrease in cash value of bank-owned life insurance, net	(239)	66
Increase in deferred income tax benefit	(638)	(226)
Changes in assets and liabilities:		
Decrease (increase) in accrued interest receivable	40	(232)
Increase in other assets	(548)	(255)
Increase in accrued interest payable	2	28
Increase in other liabilities	764	253
Total adjustments	1,416	5,518
Net cash provided by operating activities	4,640	10,733
Cash flows from investing activities:		
Proceeds from maturities and calls of AFS investment securities	2,250	250
Proceeds from sales of AFS investment securities	5,000	-
Proceeds from principal repayment of AFS investment securities	13,246	14,981
Proceeds from maturities of securities held to maturity	63,071	47,529
Purchases of securities available for sale	(15,227)	-
Purchases of securities held to maturity	(46,712)	(60,001)
(Purchase) of Federal Home Loan Bank stock	(174)	(28)
Proceeds from sale of real estate owned	663	488
Increase in loans receivable, net	(17,842)	(28,553)
Capital expenditures	(131)	(160)
Purchase of life insurance policies	(1,200)	-
Net cash provided by (used in) investing activities	2,944	(25,494)
Cash flows from financing activities:		
Net increase (decrease) in deposits	32,156	(6,751)
Net (decrease) increase in short-term borrowings	(5,867)	4,991
Proceeds from exercise of stock options	373	245
Stock issuance costs	(3)	(5)
Net cash provided by (used in) financing activities	26,659	(1,520)
Net increase (decrease) in cash and cash equivalents	34,243	(16,281)
Cash and cash equivalents at beginning of year	12,114	28,395
Cash and cash equivalents at end of year	\$ 46,357	\$ 12,114
Supplemental disclosures:		
Cash paid during the year for:		
Interest	\$ 5,434	\$ 4,026
Income taxes paid	1,021	2,271
Noncash items:		
Net change in unrealized gain (loss) on securities available for sale, net of taxes of \$204 and \$(105) for 2019 and 2018, respectively	\$ 534	\$ (275)
Transfer to real estate owned	826	283

See accompanying notes to the consolidated financial statements.

1ST COLONIAL BANCORP, INC. AND SUBSIDIARY

Notes to Consolidated Financial Statements

Note 1. Nature of Operations

1st Colonial Bancorp, Inc. (the “Company”, “We” or “Our”) is a Pennsylvania corporation headquartered in Collingswood, New Jersey, and the parent company of 1st Colonial Community Bank (the “Bank”). The Bank opened for business on June 30, 2000 and provides a wide range of business and consumer financial services through its two New Jersey branch offices located in Collingswood and Westville.

The Company was organized as the holding company for the Bank, in connection with the reorganization approved by the Bank’s shareholders at the annual meeting on June 12, 2002. As a bank holding company registered under the Bank Holding Company Act of 1956, the Company is subject to the supervision and regulation of the Board of Governors of the Federal Reserve System (the “FRB”). The Bank was a national bank until November 1, 2012 when it was granted a state charter by the New Jersey Department of Banking and Insurance. The Bank’s deposits are insured by the Federal Deposit Insurance Corporation (“FDIC”). The Company’s operations and those of the Bank are subject to supervision and regulation by FRB, the FDIC, and the New Jersey Department of Banking and Insurance. The principal activity of the Bank is to provide its local communities with general commercial and retail banking services. The Bank is managed as one business segment.

Note 2. Summary of Significant Accounting Policies

Basis of Presentation

The accompanying consolidated financial statements include the accounts of the parent company, 1st Colonial Bancorp, Inc. and its wholly owned subsidiary, 1st Colonial Community Bank. Prior period amounts have been reclassified, where necessary, to conform to current year classification.

Use of Estimates

The preparation of consolidated financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of income and expenses during the reporting period. Actual results could differ from those estimates.

Cash and Cash Equivalents

For purposes of reporting cash flows, cash and cash equivalents include cash and amounts due from banks and federal funds sold. Generally, federal funds sold are repurchased the following day.

Investments Held to Maturity

Debt securities that management has the positive intent and ability to hold until maturity are classified as held to maturity and are carried at their remaining unpaid principal balance, net of unamortized premiums or unaccreted discounts. Premiums are amortized and discounts are accreted using a method that produces results that approximate level yield over the estimated remaining term of the underlying security.

Securities Available for Sale

Securities not classified as held to maturity are classified as available-for-sale and are stated at fair value. Unrealized gains and losses are excluded from earnings and are reported as accumulated other comprehensive income (loss), net of tax, as a separate component of shareholders’ equity, until realized. Gains and losses are determined using the specific-identification method and are accounted for on a trade-date basis.

Bank Stock

The Bank carries its investments in Atlantic Community Bankers Bank (“ACBB”) stock and Federal Home Loan Bank (“FHLB”) stock at their amortized cost because they do not have a readily determinable fair value. These investments are included in bank stock in the consolidated statements of financial condition.

1ST COLONIAL BANCORP, INC. AND SUBSIDIARY

Notes to Consolidated Financial Statements

The Bank is required to maintain an investment in ACBB stock. The Bank had \$40 thousand in ACBB stock at December 31, 2019 and 2018, respectively.

The Bank is required to acquire and hold shares of capital stock in the FHLB based upon a percentage of the Bank's FHLB borrowings, unused borrowing capacity, and the amount of residential first mortgage loans sold to the FHLB. The Bank had \$2.1 million and \$1.9 million in FHLB stock at December 31, 2019 and 2018. The Bank carries its investment in FHLB stock at cost, or par value, and evaluates FHLB stock for impairment based on the ultimate recoverability of par value rather than by recognizing temporary declines in value. As part of the impairment assessment of FHLB stock, management considers, among other things, (i) the significance and length of time any declines in net assets of the FHLB compared to its capital stock, (ii) commitments by the FHLB to make payments required by law or regulations and the level of such payments in relation to its operating performance; (iii) the impact of legislative and regulatory changes on financial institutions and, accordingly, the customer base of the FHLB; and (iv) the liquidity position of the FHLB. The FHLB has access to the U.S. government-Sponsored Enterprise Credit Facility, a secured lending facility that serves as a liquidity backstop, substantially reducing the likelihood that the FHLB would need to sell securities to raise liquidity and, thereby, cause the realization of large economic losses. The FHLB is rated AAA and is likely to remain unchanged based on expectations that the FHLB has a very high degree of government support and was in compliance with all regulatory capital requirements as of December 31, 2019. Based on the above, we have determined there was no other-than-temporary impairment related to our FHLB stock investment as of December 31, 2019 and 2018.

Mortgage Loans Held for Sale

The Bank originates and sells residential mortgage loans servicing released to the secondary market. This activity enables the Bank to fulfill the credit needs of the community while reducing its overall exposure to interest rate and credit risk. These loans are reported at the lower of their cost or fair market value.

Loans

Loans are stated at the principal amount outstanding, net of deferred loan fees and costs. Interest income is accrued on the principal amount outstanding. Loan origination fees and related direct costs are deferred and amortized to interest income over the term of the respective loan as a yield adjustment.

Loans are reported as non-accrual if they are past due as to principal or interest payments for a period of 90 days or more. Exceptions may be made if a loan is deemed by management to be well collateralized and in the process of collection. Loans that are on a current payment status may also be classified as non-accrual if there is serious doubt as to the borrower's ability to continue interest or principal payments. When a loan is placed on non-accrual all unpaid interest is reversed from interest income. Interest payments received on impaired nonaccrual loans are normally applied against principal. Excess proceeds received over the principal amounts due on impaired non-accrual loans are recognized as income on a cash basis. We recognize income under the accrual basis when the principal payments on the loans become current and the collateral on the loan is sufficient to cover the outstanding obligation to the Company. If these factors do not exist, we do not recognize income. Generally, loans are restored to accrual status when the loan is brought current, has performed in accordance with the contractual terms for a reasonable period of time (generally six months) and the ultimate collectability of the total contractual principal and interest is no longer in doubt. The past due status of all classes of loans receivable is determined based on contractual due dates for loan payments.

Impaired loans are measured based on the present value of expected future discounted cash flows, the market price of the loan, or the fair value of the underlying collateral if the loan is collateral dependent. The recognition of interest income on impaired loans is the same as for non-accrual loans discussed above.

A loan modification is deemed a troubled debt restructuring ("TDR") when two conditions are met: 1) the borrower is experiencing financial difficulty and 2) a concession is made by us that would not otherwise be considered for a borrower with similar credit risk characteristics. All loans classified as TDRs are considered to be impaired. TDRs are returned to an accrual status when the loan is brought current, has performed in accordance with the contractual restructured terms for a reasonable period of time (generally six months) and the ultimate collectability of the total

1ST COLONIAL BANCORP, INC. AND SUBSIDIARY

Notes to Consolidated Financial Statements

contractual restructured principal and interest is no longer in doubt. Our policy for TDRs is to recognize interest income on currently performing restructured loans under the accrual method.

Allowance for Loan Losses

Our loan portfolio is subject to varying degrees of credit risk. The allowance for loan losses (“allowance”) reflects management’s best estimate of losses, both known and inherent, in the existing loan portfolio. Management uses significant estimates to determine the allowance. Management’s estimates consider such factors as changes in the nature and volume of the portfolio, overall portfolio quality, and review of specific problem loans, and current economic conditions that may affect the borrowers’ ability to pay. The provision for loan losses charged to operating expenses represents the amount necessary to maintain an appropriate allowance. Loan losses are charged directly against the allowance when loans are determined to be uncollectable. Recoveries on previously charged-off loans are credited to the allowance when received.

Based on management’s comprehensive analysis of the loan portfolio, management believes the current level of the allowance is adequate at December 31, 2019. However, its determination requires significant judgment, and estimates of probable losses inherent in the credit portfolio can vary significantly from the amounts observed. While management uses the best information available to make allowance evaluations, adjustments to the allowance may be necessary based on changes in economic and other conditions or changes in accounting guidance. In addition, the FDIC, as an integral part of its examination processes, periodically reviews our allowance for loan losses. The FDIC may require the recognition of adjustments to the allowance for loan losses based on their judgment of information available to them at the time of their examinations. To the extent that actual outcomes differ from management’s estimates, additional provisions to the allowance for loan losses may be required that would adversely impact earnings in future periods.

Premises and Equipment

Premises and equipment are recorded at cost less accumulated depreciation and amortization. Depreciation is computed using the straight-line method over the expected useful lives of the assets. Amortization of leasehold improvements is computed using the straight-line method over the shorter of the useful lives or the remaining lease term. Software costs, furniture, and equipment have depreciable lives of 3 to 10 years. Building and improvements have estimated useful lives of 5 to 35 years. The costs of maintenance and repairs are expensed as they are incurred, and renewals and betterments are capitalized.

Leases

On January 1, 2019, the Company adopted Accounting Standards Update (“ASU”) No. 2016-02, Leases (Topic 842) (“ASU 2016-02”) using the required modified retrospective transition approach. 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. Our leases are operating leases and are predominantly related to real estate. The ROU asset is included in other assets and the lease liability is included in other liabilities on the balance sheet. The amortization of operating lease ROU assets and the accretion of operating lease liabilities are reported together as fixed lease expense and are included in occupancy and equipment expense within other expense. The fixed lease expense is recognized on a straight-line basis over the life of the lease. The Company has elected to exclude leases with original terms of less than one year from the operating lease ROU assets and lease liabilities.

Other Real Estate Owned

Other real estate owned (“OREO”) is comprised of properties acquired through foreclosure proceedings or acceptance of a deed in lieu of foreclosure. Real estate owned is recorded at the lower of the carrying value of the loan or the fair value of the property, net of estimated selling costs. Costs relating to the development or improvement of properties are capitalized, while expenses related to the operation and maintenance of properties are expensed as incurred. Gains or losses upon dispositions are reflected in earnings as realized. The Bank had no OREO at December 31, 2019 and 2018.

1ST COLONIAL BANCORP, INC. AND SUBSIDIARY

Notes to Consolidated Financial Statements

Bank-Owned Life Insurance

We have bank-owned life insurance (“BOLI”) policies on certain officers and key employees. These policies are reflected on the consolidated statements of financial condition at their cash surrender value, or the amount that can be realized. Income from these policies and changes in the cash surrender value are recorded in non-interest income. During 2019 we purchased an additional \$1.2 million BOLI policy and mainly covered new key employees. BOLI was valued at \$9.8 million and \$8.4 million at December 31, 2019 and 2018, respectively. The total income recognized on the BOLI policies was \$239 thousand and \$577 thousand in 2019 and 2018, respectively. During the fourth quarter of 2018, we accrued \$336 thousand in insurance income related to a former employee covered by a BOLI policy. The maximum amount that will be paid to all employees is \$1.0 million.

Earnings Per Share

Basic earnings per share is calculated as net income divided by the weighted average number of shares outstanding during the period. Dilutive earnings per share include dilutive common stock equivalents as computed under the treasury stock method using average common stock prices.

Income Taxes

The Company and the Bank file a consolidated federal income tax return and a consolidated New Jersey income tax return. The Company and the Bank file separate Pennsylvania tax returns. Income taxes are allocated to the Company and the Bank based on the contribution of their income or use of their loss in the consolidated return. As of December 31, 2019, tax years 2016 through 2018 are subject to federal examination by the IRS and years 2015 through 2018 are subject to state examination by various state taxing authorities. Tax regulations are subject to interpretation of the related tax laws and regulations and require significant judgment to apply.

Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases, as well as operating loss carry forwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. A valuation allowance is established against deferred tax assets when, in the judgment of management, it is more likely than not that such deferred tax assets will not become available.

We account for income taxes in accordance with FASB ASC Topic 740-10, “Accounting for Uncertainty in Income Taxes”, (“ASC 740”) which includes guidance related to accounting for uncertainty in income taxes, which sets out a consistent framework to determine the appropriate level of tax reserves to maintain for uncertain tax positions. We had no unrecognized tax benefits or accrued interest and penalties as of December 31, 2019 and 2018. We classify interest and penalties as an element of tax expense.

Stock Options

As of December 31, 2019, the Company had four stock-based compensation plans, which are described more fully in “Note 18 - Stock Option Plans” to the Consolidated Financial Statements. The Company accounts for all share-based payments to be recognized as compensation expense in the consolidated financial statements based on their fair values at the grant date. That expense will be recognized on a straight-line basis over the period during which services are provided in exchange for the award, known as the requisite service period (usually, the vesting period).

Recent Accounting Pronouncements

In February 2016, the FASB issued Accounting Standards Update No. 2016-02, “Leases” (“ASU 2016-02”). From the lessee's perspective, the new standard establishes a right-of-use (ROU) model that requires a lessee to record a ROU asset and a lease liability on the balance sheet for all leases with terms longer than 12 months. Our leases are operating leases and are predominantly related to real estate. The new standard is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. The adoption of ASU 2016-02 on

1ST COLONIAL BANCORP, INC. AND SUBSIDIARY

Notes to Consolidated Financial Statements

January 1, 2019, using the required modified retrospective transition approach did not have material effect on our financial statements.

In June 2016, FASB issued Accounting Standards Update No. 2016-13, “Financial Instruments–Credit Losses (Topic 326) Measurement of Credit Losses on Financial Instruments” (“ASU 2016-13”). The amendments in ASU 2016-13 replace the incurred loss impairment methodology in current GAAP with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to inform credit loss estimates. The amendments affect loans, debt securities, trade receivables, net investments in leases, off-balance-sheet credit exposures, reinsurance receivables, and any other financial assets not excluded from the scope that have the contractual right to receive cash.

The amendments in ASU 2016-13 require a financial asset (or a group of financial assets) measured at amortized cost basis to be presented at the net amount expected to be collected. The allowance for credit losses is a valuation account that is deducted from the amortized cost basis of the financial asset(s) to present the net carrying value at the amount expected to be collected on the financial asset. The income statement reflects the measurement of credit losses for newly recognized financial assets, as well as the expected increases or decreases of expected credit losses that have taken place during the period. The measurement of expected credit losses is based on relevant information about past events, including historical experience, current conditions, and reasonable and supportable forecasts that affect the collectability of the reported amount. An entity must use judgment in determining the relevant information and estimation methods that are appropriate in its circumstances.

Credit losses relating to available-for-sale debt securities should be recorded through an allowance for credit losses. Available-for-sale accounting recognizes that value may be realized either through collection of contractual cash flows or through sale of the security. Therefore, the amendments limit the amount of the allowance for credit losses to the amount by which fair value is below amortized cost because the classification as available for sale is premised on an investment strategy that recognizes that the investment could be sold at fair value, if cash collection would result in the realization of an amount less than fair value. The amendments in ASU 2016-13 require that credit losses be presented as an allowance rather than a writedown.

The amendments in ASU 2016-13 will become effective for the Company for financial statements issued for fiscal years beginning after December 15, 2022, and interim periods within those fiscal years. An entity will apply the amendments in ASU 2016-13 through a cumulative-effect adjustment to retained earnings as of the beginning of the first reporting period in which the guidance is effective (that is, modified-retrospective approach).

We are reviewing our systems and data collection to determine the necessary changes to our current process. We are completing due diligence on vendors to assist in developing a methodology that is in compliance with this ASU. We are currently evaluating the impact of the amendments in ASU 2016-13 on our consolidated financial statements. We believe that expected credit losses under ASU 2016-13 will generally result in earlier loss recognition on our loan portfolio.

In August 2016, FASB issued Accounting Standards Update No. 2016-15, “Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments” (“ASU 2016-15”). Stakeholders indicated that there is diversity in practice in how certain cash receipts and cash payments are presented and classified in the statement of cash flows under Topic 230, Statement of Cash Flows, and other Topics. The following eight specific cash flow issues are addressed in ASU 2016-15: Debt prepayment or debt extinguishment costs; settlement of zero-coupon debt instruments or other debt instruments with coupon interest rates that are insignificant in relation to the effective interest rate of the borrowing; contingent consideration payments made after a business combination; proceeds from the settlement of insurance claims; proceeds from the settlement of corporate-owned life insurance policies (“COLI”s) (including bank-owned life insurance policies (“BOLI”s)); distributions received from equity method investees; beneficial interests in securitization transactions; and separately identifiable cash flows and application of the predominance principle. For all non-public business entities, the amendments in this ASU 2016-15 are effective for financial statements issued for fiscal years beginning after December 15, 2018, and interim periods within those fiscal

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years beginning after December 15, 2019. The amendments in ASU 2016-15 should be applied using a retrospective transition method to each period presented. If it is impracticable to apply the amendments retrospectively for some of the issues, the amendments for those issues would be applied prospectively as of the earliest date practicable. Early adoption is permitted, including adoption in an interim period. If an entity early adopts the amendments in an interim period, any adjustments should be reflected as of the beginning of the fiscal year that includes that interim period. An entity that elects early adoption must adopt all of the amendments in the same period. We adopted ASU 2016-15 during the first quarter of 2019 and it had no effect on our results of operations because it only impacted the presentation of certain information on the statement of cash flows.

In March 2017, FASB issued Accounting Standards Update No. 2017-08, "Receivables-Nonrefundable Fees and Other Costs (Subtopic 310-20)" ("ASU 2017-08"). Stakeholders raised concerns that current GAAP excludes certain callable debt securities from consideration of early repayment of principal even if the holder is certain that the call will be exercised. As a result, upon the exercise of a call on a callable debt security held at a premium, the unamortized premium is recorded as a loss in earnings. Stakeholders noted that generally, in the United States, callable debt securities are quoted, priced, and traded assuming a model that incorporates consideration of calls (also referred to as "yield-to-worst" pricing). The amendments in ASU 2017-08 shorten the amortization period for certain callable debt securities held at a premium. Specifically, the amendments require the premium to be amortized to the earliest call date. The amendments do not require an accounting change for securities held at a discount; the discount continues to be amortized to maturity. The amendments in this Update more closely align the amortization period of premiums and discounts to expectations incorporated in market pricing on the underlying securities. For public business entities, the amendments in this Update are effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018. For all other entities, the amendments are effective for fiscal years beginning after December 15, 2019, and interim periods within fiscal years beginning after December 15, 2020. An entity should apply the amendments in ASU 2017-08 on a modified retrospective basis through a cumulative-effect adjustment directly to retained earnings as of the beginning of the period of adoption. We adopted ASU 2017-08 during the first quarter of 2020 and it had no effect on our financial statements.

In August 2018, FASB issued Accounting Standards Update No. 2018-13, "Fair Value Measurement (Topic 820)" ("ASU 2018-13"). ASU 2018-13 removes, modifies and adds certain disclosures to improve the usefulness of the information. This Update is effective in annual and interim periods in fiscal years beginning after December 15, 2019. Early adoption is permitted. Adoption is required on both a prospective and retrospective basis depending on the amendment. We do not expect the adoption of ASU 2018-13 to have a material impact on our Consolidated Financial Statements and related disclosures.

Note 3. Common Stock Dividends

On January 30, 2019, the Company declared a 5% stock dividend to all shareholders of record as of April 1, 2019 payable on April 15, 2019. On January 30, 2018, the Company declared a 5% stock dividend to all shareholders of record as of April 2, 2018 payable on April 16, 2018.

Note 4. Cash and Due from Banks

The Bank is required to maintain certain daily average reserve balances in accordance with FRB requirements. At December 31, 2019 and 2018, the FRB reserve requirement was \$634 thousand and \$412 thousand, respectively. In addition, the Bank was required to maintain \$50 thousand in cash reserves at its correspondent banks at December 31, 2019 and 2018.

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Note 5. Investment Securities

A comparison of amortized cost and approximate fair value of investment securities held to maturity and securities available for sale at December 31, 2019 and 2018 is as follows:

As of December 31, 2019

(In thousands)	<u>Amortized Cost</u>	<u>Gross unrealized gains</u>	<u>Gross unrealized losses</u>	<u>Fair value</u>
Investments held to maturity:				
Municipal securities	\$ 42,767	\$ -	\$ -	\$ 42,767
Total	<u>\$ 42,767</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 42,767</u>
Securities available for sale:				
U.S. government securities	\$ 3,000	\$ -	\$ (1)	\$ 2,999
Mortgage-backed securities	47,865	423	(63)	48,225
Total	<u>\$ 50,865</u>	<u>\$ 423</u>	<u>\$ (64)</u>	<u>\$ 51,224</u>

As of December 31, 2018

(In thousands)	<u>Amortized Cost</u>	<u>Gross unrealized gains</u>	<u>Gross unrealized losses</u>	<u>Fair value</u>
Investments held to maturity:				
Municipal securities	\$ 59,126	\$ -	\$ -	\$ 59,126
Total	<u>\$ 59,126</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 59,126</u>
Securities available for sale:				
U.S. government securities	\$ 9,996	\$ -	\$ (127)	\$ 9,869
Mortgage-backed securities	46,104	258	(517)	45,845
Municipal bonds	251	2	-	253
Total	<u>\$ 56,351</u>	<u>\$ 260</u>	<u>\$ (644)</u>	<u>\$ 55,967</u>

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The scheduled maturities of investment securities held to maturity and securities available for sale at December 31, 2019 are as follows:

(In thousands)	HTM Investments		AFS Investments	
	Amortized Cost	Fair value	Amortized Cost	Fair value
Due in one year or less	\$ 40,399	\$ 40,399	\$ 15	\$ 16
Due after one year up to five years	1,835	1,835	8,369	8,445
Due after five years up to ten years	533	533	21,829	21,931
Due after ten years	-	-	20,652	20,832

Proceeds from sales and maturities of securities available for sale totaled \$2.3 million and \$250 thousand during 2019 and 2018, respectively. Gains realized from the sale of securities were \$4 thousand and \$0 in 2019 and 2018, respectively.

As of December 31, 2019 and 2018, investment securities with a market value of \$78.6 million and \$74.7 million, respectively, were pledged as collateral for uninsured municipal deposits, uninsured deposits underlying retail repurchase agreements, and the FHLB for potential borrowings.

Gross unrealized losses and fair value, aggregated by investment category and length of time that individual securities have been in continuous unrealized loss positions at December 31, 2019 and 2018 are as follows:

As of December 31, 2019

(In thousands)	Less than 12 months			12 months or longer			Total		
	Fair value	Gross unrealized losses	Number of positions	Fair value	Gross unrealized losses	Number of positions	Fair value	Gross unrealized losses	Number of positions
Investments held to maturity:									
Municipal securities	\$ -	\$ -	-	\$ -	\$ -	-	\$ -	\$ -	-
Total	\$ -	\$ -	-	\$ -	\$ -	-	\$ -	\$ -	-
Securities available for sale:									
U.S. government securities	\$ 2,999	\$ (1)	1	\$ -	\$ -	-	\$ 2,999	\$ (1)	1
Mortgage-backed securities	13,430	(44)	7	1,143	(19)	1	14,573	(63)	8
Total	\$ 16,429	\$ (45)	8	\$ 1,143	\$ (19)	1	\$ 17,572	\$ (64)	9

As of December 31, 2018

(In thousands)	Less than 12 months			12 months or longer			Total		
	Fair value	Gross unrealized losses	Number of positions	Fair value	Gross unrealized losses	Number of positions	Fair value	Gross unrealized losses	Number of positions
Investments held to maturity:									
Municipal securities	\$ -	\$ -	-	\$ -	\$ -	-	\$ -	\$ -	-
Total	\$ -	\$ -	-	\$ -	\$ -	-	\$ -	\$ -	-
Securities available for sale:									
U.S. government securities	\$ -	\$ -	-	\$ 9,869	\$ (127)	3	\$ 9,869	\$ (127)	3
Mortgage-backed securities	2,489	(15)	5	28,734	(502)	18	31,223	(517)	23
Total	\$ 2,489	\$ (15)	5	\$ 38,603	\$ (629)	21	\$ 41,092	\$ (644)	26

For all of the above investment securities, the unrealized losses are generally due to changes in interest rates and, as such, are considered to be temporary by the Company. The temporary impairment of fixed rate investments is likely to continue in a rising interest rate environment. The contractual terms of these investments do not permit the issuer to settle the securities at a price less than the amortized cost of the investment. Because we have the ability and intent

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to hold these investments until a market price recovery or maturity, these investments are not considered other than temporarily impaired.

All temporarily impaired investments are bank-qualified investments. There has been no significant change in the credit quality of issuers since the securities were purchased.

Note 6. Loans Receivable

Loans receivable consist of the following at December 31, 2019 and 2018:

(In thousands)	December 31, 2019	December 31, 2018
Commercial real estate	\$ 187,099	\$ 168,934
Construction	33,448	36,723
Commercial	28,898	30,235
Residential real estate	166,438	164,238
Consumer	3,914	4,405
	<u>419,797</u>	<u>404,535</u>
Less allowance for loan losses	<u>(6,671)</u>	<u>(5,627)</u>
	<u>\$ 413,126</u>	<u>\$ 398,908</u>

The Bank is subject to a loans-to-one-borrower limitation of 15% of capital funds. At December 31, 2019, the loans-to-one-borrower limitation was \$8.1 million compared to \$7.4 million at December 31, 2018. At December 31, 2019 and 2018, there are no loans outstanding or committed to any one borrower that individually or in the aggregate exceed those limits.

The Bank lends primarily to customers in its local market area. Most loans are mortgage loans. Mortgage loans include loans secured by commercial and residential real estate and construction loans. Accordingly, lending activities could be affected by changes in the general economy, the regional economy, or real estate values. At December 31, 2019 and 2018, mortgage loans totaled \$387.0 million and \$369.9 million, respectively. Mortgage loans represent 92.8% and 91.4% of total gross loans at December 31, 2019 and 2018, respectively.

As part of the process of determining the allowance for loan losses (“allowance”) management segments the loan portfolio by product type. For the commercial real estate, construction, and commercial loan segments, periodic reviews of the individual loans are performed by both in-house staff as well as external loan reviewers. The results of these reviews are reflected in the risk grade assigned to each loan. These internally assigned grades are as follows:

Pass – Loans considered to be satisfactory with no indications of deterioration.

Special Mention – Loans classified as special mention have a potential weakness that deserves management’s close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or of the bank’s credit position at some future date.

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

Doubtful – Loans classified as doubtful have all weaknesses inherent in those classified as substandard, with 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.

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Non-accrual (substandard non-accrual, doubtful): includes credits that demonstrate serious problems to the point that it is probable that interest and principal will not be collected according to the contractual terms of the loan agreement.

In addition, the remaining segments of the loan portfolio, which include residential real estate and consumer loans are allocated portions of the allowance based on their performance status.

The following tables present risk ratings for each loan portfolio classification at December 31, 2019 and December 31, 2018.

December 31, 2019

(In thousands)	Pass	Special Mention	Substandard	Doubtful	Nonaccrual	Total
Commercial real estate	\$ 176,860	\$ 4,024	\$ 4,267	\$ -	\$ 1,948	\$ 187,099
Construction	32,741	-	312	-	395	33,448
Commercial	24,088	1,386	1,015	-	2,409	28,898
Residential real estate	164,545	358	395	-	1,140	166,438
Consumer	3,914	-	-	-	-	3,914
Total loans, net of unearned income	<u>\$ 402,148</u>	<u>\$ 5,768</u>	<u>\$ 5,989</u>	<u>\$ -</u>	<u>\$ 5,892</u>	<u>\$ 419,797</u>

December 31, 2018

(In thousands)	Pass	Special Mention	Substandard	Doubtful	Non-accrual	Total
Commercial real estate	\$ 158,065	\$ 7,322	\$ 2,717	\$ -	\$ 830	\$ 168,934
Construction	35,429	877	-	-	417	36,723
Commercial	25,927	1,532	2,353	-	423	30,235
Residential real estate	162,038	794	330	-	1,076	164,238
Consumer	4,146	-	259	-	-	4,405
Total loans, net of unearned income	<u>\$ 385,605</u>	<u>\$ 10,525</u>	<u>\$ 5,659</u>	<u>\$ -</u>	<u>\$ 2,746</u>	<u>\$ 404,535</u>

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The following tables present an aging analysis of past due payments for each loan portfolio classification at December 31, 2019 and December 31, 2018.

December 31, 2019	30-59 Days	60-89 Days	90+ Days			
(In thousands)	Past Due	Past Due	Past Due	Non-accrual	Current	Total
Commercial real estate	\$ 1,498	\$ 33	\$ -	\$ 1,948	\$ 183,620	\$ 187,099
Construction	-	-	-	395	33,053	33,448
Commercial	93	-	-	2,409	26,396	28,898
Residential real estate	198	-	-	1,140	165,100	166,438
Consumer	-	9	-	-	3,905	3,914
Total loans, net of unearned income	<u>\$ 1,789</u>	<u>\$ 42</u>	<u>\$ -</u>	<u>\$ 5,892</u>	<u>\$ 412,074</u>	<u>\$ 419,797</u>

December 31, 2018	30-59 Days	60-89 Days	90+ Days			
(In thousands)	Past Due	Past Due	Past Due	Non-accrual	Current	Total
Commercial real estate	\$ 465	\$ -	\$ -	\$ 830	\$ 167,639	\$ 168,934
Construction	-	-	-	417	36,306	36,723
Commercial	43	-	-	423	29,769	30,235
Residential real estate	199	-	-	1,076	162,963	164,238
Consumer	-	-	-	-	4,405	4,405
Total loans, net of unearned income	<u>\$ 707</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 2,746</u>	<u>\$ 401,082</u>	<u>\$ 404,535</u>

The Bank had 28 non-accrual loans at December 31, 2019 in the amount of \$5.9 million compared to 24 non-accrual loans in the amount of \$2.7 million at December 31, 2018. During 2019 we transferred \$8.1 million to non-accrual; recorded \$2.7 million in principal reductions and charged-off \$2.4 million. All of the non-accrual loans were impaired. If interest had accrued on these loans, such income would have been approximately \$432 thousand and \$174 thousand for the years ended December 31, 2019 and 2018, respectively. The specific reserves associated with the non-accrual loans were \$1.6 million and \$954 thousand at December 31, 2019 and 2018, respectively.

Troubled Debt Restructuring

The following table details our TDRs that are on an accrual status and non-accrual status at December 31, 2019 and December 31, 2018.

	As of December 31, 2019			
	Number of loans	Accrual Status	Non-Accrual Status	Total TDRs
(In thousands)				
Commercial real estate	3	\$ 831	\$ -	\$ 831
Construction	1	-	395	395
Commercial	3	250	298	548
Residential real estate	4	284	-	284
Total	<u>11</u>	<u>\$ 1,365</u>	<u>\$ 693</u>	<u>\$ 2,058</u>

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As of December 31, 2018

(In thousands)	Number of loans	Accrual Status	Non- Accrual Status	Total TDRs
Commercial real estate	4	\$ 1,004	\$ 200	\$ 1,204
Commercial	1	-	417	417
Residential real estate	6	656	-	656
Consumer	1	259	-	259
Total	12	\$ 1,919	\$ 617	\$ 2,536

During the year ended December 31, 2019, one commercial loan with a principal balance of \$128 thousand, which had been previously modified to troubled debt restructuring, defaulted.

The following table presents the new TDRs that occurred during the year ended December 31, 2019.

Modifications by type for the year ended December 31, 2019

(In thousands)	Number of loans	Rate	Term	Payment	Combination of types	Total	Pre- Modification Outstanding Recorded Investment	Post- Modification Outstanding Recorded Investment
Commercial	3	\$ -	\$ -	\$ -	\$ 548	\$ 548	\$ 632	\$ 632
Total	3	\$ -	\$ -	\$ -	\$ 548	\$ 548	\$ 632	\$ 632

Allowance for Loan Losses

The following table details the rollforward of the allowance and the loan portfolio disaggregated by loan portfolio classification for the twelve-months ended December 31, 2019 and 2018:

December 31, 2019	Commercial real estate	Construction and land development	Commercial and industrial	Residential real estate	Consumer	Total
(In thousands)						
Beginning balance	\$ 2,341	\$ 672	\$ 927	\$ 1,626	\$ 61	\$ 5,627
Charge-offs	(753)	(38)	(1,492)	(192)	(16)	(2,491)
Recoveries	102	-	181	56	12	351
Provision (credit)	1,483	55	1,756	(104)	(6)	3,184
Ending balance	\$ 3,173	\$ 689	\$ 1,372	\$ 1,386	\$ 51	\$ 6,671
Ending balance: related to loans individually evaluated for impairment	\$ 876	\$ 395	\$ 536	\$ 97	\$ -	\$ 1,904
Ending balance: related to loans collectively evaluated for impairment	\$ 2,297	\$ 294	\$ 836	\$ 1,289	\$ 51	\$ 4,767
Loan Balances						
Ending balance	\$ 187,099	\$ 33,448	\$ 28,898	\$ 166,438	\$ 3,914	\$ 419,797
Ending balance: individually evaluated for impairment	\$ 2,779	\$ 395	\$ 2,659	\$ 1,425	\$ -	\$ 7,258
Ending balance: collectively evaluated for impairment	\$ 184,320	\$ 33,053	\$ 26,239	\$ 165,013	\$ 3,914	\$ 412,539

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December 31, 2018	Construction					
(In thousands)	Commercial real estate	and land development	Commercial and industrial	Residential real estate	Consumer	Total
Beginning balance	\$ 2,129	\$ 686	\$ 677	\$ 1,310	\$ 56	\$ 4,858
Charge-offs	(176)	-	(438)	(179)	(33)	(826)
Recoveries	75	-	14	12	17	118
Provision (credit)	313	(14)	674	483	21	1,477
Ending balance	<u>\$ 2,341</u>	<u>\$ 672</u>	<u>\$ 927</u>	<u>\$ 1,626</u>	<u>\$ 61</u>	<u>\$ 5,627</u>
Ending balance: related to loans individually evaluated for impairment	<u>\$ 527</u>	<u>\$ 326</u>	<u>\$ 175</u>	<u>\$ 302</u>	<u>\$ 8</u>	<u>\$ 1,338</u>
Ending balance: related to loans collectively evaluated for impairment	<u>\$ 1,814</u>	<u>\$ 346</u>	<u>\$ 752</u>	<u>\$ 1,324</u>	<u>\$ 53</u>	<u>\$ 4,289</u>
Loan Balances						
Ending balance	<u>\$ 168,934</u>	<u>\$ 36,723</u>	<u>\$ 30,235</u>	<u>\$ 164,238</u>	<u>\$ 4,405</u>	<u>\$ 404,535</u>
Ending balance: individually evaluated for impairment	<u>\$ 1,833</u>	<u>\$ 417</u>	<u>\$ 423</u>	<u>\$ 1,733</u>	<u>\$ 259</u>	<u>\$ 4,665</u>
Ending balance: collectively evaluated for impairment	<u>\$ 167,101</u>	<u>\$ 36,306</u>	<u>\$ 29,812</u>	<u>\$ 162,505</u>	<u>\$ 4,146</u>	<u>\$ 399,870</u>

The following tables details the impaired loans by loan classification at December 31, 2019 and December 31, 2018.

	As of and for the year ended December 31, 2019					
(In thousands)	Unpaid principal balance	Recorded investment	Related allowance	Average recorded investment	Interest income recognized	Interest income recognized cash basis
With no related allowance recorded:						
Commercial real estate	\$ 918	\$ 652	\$ -	\$ 637	\$ -	\$ 34
Commercial	793	476	-	255	-	1
Residential real estate	869	725	-	775	-	-
Total:	<u>\$ 2,580</u>	<u>\$ 1,853</u>	<u>\$ -</u>	<u>\$ 1,667</u>	<u>\$ -</u>	<u>\$ 35</u>
With an allowance recorded:						
Commercial real estate	\$ 2,056	\$ 2,051	\$ 876	\$ 1,782	\$ 42	\$ -
Construction	435	645	395	450	-	-
Commercial	2,183	1,933	536	1,235	20	-
Residential real estate	904	776	97	661	17	-
Total:	<u>\$ 5,578</u>	<u>\$ 5,405</u>	<u>\$ 1,904</u>	<u>\$ 4,128</u>	<u>\$ 79</u>	<u>\$ -</u>

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As of and for the year ended December 31, 2018						
(In thousands)	Unpaid principal balance	Recorded investment	Related allowance	Average recorded investment	Interest income recognized	Interest income recognized cash basis
With no related allowance recorded:						
Commercial real estate	\$ 749	\$ 530	\$ -	\$ 716	\$ -	\$ -
Commercial	74	74	-	78	-	-
Residential real estate	940	932	-	891	12	-
Consumer	-	-	-	41	-	-
Total:	<u>\$ 1,763</u>	<u>\$ 1,536</u>	<u>\$ -</u>	<u>\$ 1,726</u>	<u>\$ 12</u>	<u>\$ -</u>
With an allowance recorded:						
Commercial real estate	\$ 1,306	\$ 1,303	\$ 527	\$ 1,283	\$ 52	\$ -
Construction	435	417	326	427	-	-
Commercial	350	349	175	157	-	-
Residential real estate	886	801	302	548	13	-
Consumer	259	259	8	61	7	-
Total:	<u>\$ 3,236</u>	<u>\$ 3,129</u>	<u>\$ 1,338</u>	<u>\$ 2,476</u>	<u>\$ 72</u>	<u>\$ -</u>

Note 7. Premises and Equipment, Net

Premises and equipment at December 31, 2019 and 2018 are summarized as follows (dollars in thousands):

(In thousands)	Estimated Useful Lives	As of December 31,	
		2019	2018
Land		\$ 122	\$ 122
Buildings and leasehold improvements	5 - 35 years	959	929
Furniture, fixtures and equipment	3 - 10 years	1,380	1,279
Premises and equipment, gross		2,461	2,330
Less accumulated depreciation and amortization		(1,770)	(1,532)
Premises and equipment, net		<u>\$ 691</u>	<u>\$ 798</u>

Depreciation expense was \$238 thousand and \$226 thousand for the years ended December 31, 2019 and 2018, respectively, and is recorded in occupancy and equipment expenses. During 2018, we retired \$1.8 million in fully depreciated and out of service furniture and equipment.

We lease our Collingswood branch location and operations center. We own the building for our Westville, New Jersey branch.

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Note 8. Deposits

Deposits consist of the following major classifications at December 31, 2019 and 2018:

(Dollars in thousand)	As of December 31,			
	2019		2018	
	Balance	Weighted Average Rate	Balance	Weighted Average Rate
Non-interest checking	\$ 61,457	-	\$ 54,298	-
Interest checking	244,170	0.76%	215,838	0.51%
Money market deposits	11,777	0.48%	15,928	0.48%
Savings deposits	46,065	0.43%	49,208	0.44%
Certificates of deposit (\$250 and over)	70,751	2.03%	54,055	2.17%
Certificates of deposit (less than \$250)	67,032	2.07%	69,035	1.99%
Brokered deposits	21,000	2.04%	31,734	2.37%
Total deposits	\$ 522,252		\$ 490,096	

The Bank has a concentration of deposits from local municipalities. Municipal deposits, which are mostly interest-checking accounts, were \$223.3 million or 42.8% of total deposits at December 31, 2019, and \$199.0 million or 40.6% of total deposits at December 31, 2018. Municipal deposit accounts in excess of \$250 thousand are collateralized by investment securities with a carrying value of \$75.2 million at December 31, 2019 and \$107.0 million secured by a FHLB Municipal Line of Credit.

Interest expense on deposits consisted of the following for the years ended December 31, 2019 and 2018:

(In thousands)	2019	2018
Interest checking	\$ 1,697	\$ 1,135
Money market deposits	62	75
Savings deposits	217	247
Certificates of deposit	3,393	2,576
Total interest expense on deposits	\$ 5,369	\$ 4,033

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Notes to Consolidated Financial Statements

The following is a schedule of certificates of deposit, which includes the brokered deposits, by maturities as of December 31, 2019:

(In thousands)	As of
	<u>December 31, 2019</u>
2020	\$ 120,626
2021	31,393
2022	3,311
2023	2,250
2024	<u>1,203</u>
Total certificates of deposits	<u>\$ 158,783</u>

Note 9. Borrowing Availability

Federal Home Loan Bank

As of December 31, 2019, we had \$14.6 million in borrowing capacity at the FHLB. The FHLB line of credit is secured with residential and commercial mortgage loans with an aggregate market value of \$18.3 million and securities with an aggregate market value of \$21 thousand. At December 31, 2018 the FHLB borrowing capacity was \$12.2 million and was secured with residential and commercial mortgage loans with an aggregate market value of \$15.2 million and securities with an aggregate market value of \$61 thousand. At December 31, 2019 and 2018, the Bank had no outstanding borrowings against its lines of credit. The average balance of FHLB advances was \$972 thousand and \$39 thousand for 2019 and 2018, respectively.

Repurchase Agreements

Historically, the Bank has sold securities under agreements to repurchase as a funding source. At December 31, 2019 and 2018, the Bank had \$2.3 million and \$3.2 million, respectively, of securities sold under agreements to repurchase. As of December 31, 2019, these repurchase agreements had a weighted average fixed rate of 1.21% with maturity dates not exceeding one year. The underlying securities for the repurchase agreements had an aggregate market value of \$3.2 million and \$3.5 million as of December 31, 2019 and 2018, respectively, and were predominantly U.S. government-sponsored mortgage-backed securities.

Other Lines of Credit

At December 31, 2019 and 2018, the Bank had an unsecured line of credit with Atlantic Community Bankers Bank (“ACBB”) in the aggregate amount of \$8.0 million. There was no outstanding balance at December 31, 2019. At December 31, 2018 the outstanding balance was \$5.0 million. The average balance of the ACBB line was \$278 thousand and \$95 thousand for 2019 and 2018, respectively.

At December 31, 2019 and 2018, 1st Colonial Bancorp, Inc. had a secured line of credit with ACBB in the aggregate amount of \$5,000,000. The ACBB line is secured with 100% of the voting stock of 1st Colonial Community Bank. At December 31, 2019 and 2018, there were no outstanding balances against this line. There were no amounts outstanding in 2019 and 2018 under this line.

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Notes to Consolidated Financial Statements

Note 10. Earnings Per Share

The following is a reconciliation of the numerators and denominators of the basic and diluted earnings per share calculation for the years ended December 31, 2019 and 2018:

(In thousands, except for per share data)	Net Income	Average shares	Per share Amount
2019:			
Basic earnings per share	\$ 3,224	4,670,285	\$ 0.69
Effect of dilutive stock equivalents	-	123,883	0.02
Diluted earnings per share	<u>\$ 3,224</u>	<u>4,794,168</u>	<u>\$ 0.67</u>
2018:			
Basic earnings per share	\$ 5,215	4,604,131	\$ 1.13
Effect of dilutive stock equivalents	-	195,254	0.04
Diluted earnings per share	<u>\$ 5,215</u>	<u>4,799,385</u>	<u>\$ 1.09</u>

Earnings per share is calculated on the basis of weighted average number of shares outstanding. Options to purchase 313,479 and 412,474 shares of common stock were outstanding at December 31, 2019 and 2018, respectively. Options, to the extent dilutive, were included in the denominator in the computation of earnings per diluted share. There were no antidilutive options at December 31, 2019 and 2018.

Note 11. Fair Value of Financial Instruments

Under FASB ASC Topic 820 “Fair Value Measurements and Disclosures” (“ASC Topic 820”), fair values are based on the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. When available, management uses quoted market prices to determine fair value. If quoted prices are not available, fair value is based upon valuation techniques such as matrix pricing or other models that use, where possible, current market-based or independently sourced market parameters, such as interest rates. If observable market-based inputs are not available, we use unobservable inputs to determine appropriate valuation adjustments using discounted cash flow methodologies.

Management uses its best judgment in estimating the fair value of our financial instruments; however, there are inherent weaknesses in any estimation technique. Therefore, for substantially all financial instruments, the fair value estimates herein are not necessarily indicative of the amounts we could have realized in a sales transaction on the dates indicated. The estimated fair value amounts have been measured as of their respective period end and have not been re-evaluated or updated for purposes of these financial statements subsequent to those respective dates. As such, the estimated fair values of these financial instruments subsequent to the respective reporting dates may be different than the amounts reported at each period-end.

ASC Topic 820 provides guidance for estimating fair value when the volume and level of activity for an asset or liability has significantly declined and for identifying circumstances when a transaction is not orderly. ASC Topic 820 establishes a fair value hierarchy that prioritizes the inputs to valuation methods used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy under ASC Topic 820 are as follows:

- Level 1:* Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities.

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Notes to Consolidated Financial Statements

- Level 2:* Quoted prices in markets that are not active, or inputs that are observable either directly or indirectly, for substantially the full term of the asset or liability. Level 2 includes debt securities with quoted prices that are traded less frequently than exchange-traded instruments. Valuation techniques include matrix pricing which is a mathematical technique used widely in the industry to value debt securities without relying exclusively on quoted market prices for the specific securities but rather by relying on the securities' relationship to other benchmark quoted prices.
- Level 3:* Prices or valuation techniques that require inputs that are both significant to the fair value measurement and unobservable (i.e., supported with little or no market activity).

A financial instrument's level within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement. We did not have transfers of financial instruments within the fair value hierarchy during the years ended December 31, 2019 and 2018.

Items Measured on a Recurring Basis

Our available for sale investment securities are recorded at fair value on a recurring basis.

Fair value for Level 1 securities are determined by obtaining quoted market prices on nationally recognized securities exchanges. We do not have any level 1 securities.

Level 2 securities include obligations of U.S. government-sponsored agencies and debt securities with quoted prices, which are traded less frequently than exchange-traded instruments, whose value is determined using matrix pricing with inputs that are observable in the market or can be derived principally from or corroborated by observable market data. The prices were obtained from third party vendors. This category generally includes our mortgage-backed securities and CMOs issued by U.S. government and government-sponsored agencies, and municipal bonds.

Items Measured on a Nonrecurring Basis

Non-accrual loans and TDRs are evaluated for impairment on an individual basis under FASB ASC Topic 310 "Receivables". The impairment analysis includes current collateral values, known relevant factors that may affect loan collectability, and risks inherent in different kinds of lending. When the collateral value or discounted cash flows less costs to sell is less than the carrying value of the loan a specific reserve (valuation allowance) is established. OREO is carried at the lower of cost or fair value. Fair value is based upon independent market prices, appraised values of the collateral or management's estimation of the value of the real estate. These assets are included as Level 3 fair values, based upon the lowest level of input that is significant to the fair value measurements.

For financial assets measured at fair value on a recurring and nonrecurring basis, the fair value measurements by level within the fair value hierarchy used at December 31, 2019 and December 31, 2018 are as follows:

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Notes to Consolidated Financial Statements

	Fair Value Measurements Using:			
	Quoted Prices			
	in Active	Significant		
	Markets for	Other	Significant	
	Identical	Observable	Unobservable	
	Assets	Inputs	Inputs	
	Level 1	Level 2	Level 3	Total
<u>At December 31, 2019</u>				
(In thousands)				
Assets measured at fair value on a recurring basis				
Investment securities:				
U.S. government agencies	\$ -	\$ 2,999	\$ -	\$ 2,999
Mortgage-backed securities-residential	-	48,225	-	48,225
Total assets measured at fair value on a recurring basis	<u>\$ -</u>	<u>\$ 51,224</u>	<u>\$ -</u>	<u>\$ 51,224</u>
Assets measured at fair value on a non-recurring basis				
Impaired loans	\$ -	\$ -	\$ 7,258	\$ 7,258
Total assets measured at fair value on a non-recurring basis	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 7,258</u>	<u>\$ 7,258</u>

	Fair Value Measurements Using:			
	Quoted Prices			
	in Active	Significant		
	Markets for	Other	Significant	
	Identical	Observable	Unobservable	
	Assets	Inputs	Inputs	
	Level 1	Level 2	Level 3	Total
<u>At December 31, 2018</u>				
(In thousands)				
Assets measured at fair value on a recurring basis				
Investment securities:				
U.S. government agencies	\$ -	\$ 9,869	\$ -	\$ 9,869
Mortgage-backed securities-residential	-	45,845	-	45,845
Municipal bonds	-	253	-	253
Total assets measured at fair value on a recurring basis	<u>\$ -</u>	<u>\$ 55,967</u>	<u>\$ -</u>	<u>\$ 55,967</u>
Assets measured at fair value on a non-recurring basis				
Impaired loans	\$ -	\$ -	\$ 4,665	\$ 4,665
Total assets measured at fair value on a non-recurring basis	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 4,665</u>	<u>\$ 4,665</u>

The following methods and assumptions were used to estimate the fair values of our financial instruments at December 31, 2019 and December 31, 2018. The following information should not be interpreted as an estimate of the fair value of the entire Company since a fair value calculation is only provided for a limited portion of our assets and liabilities. Due to a wide range of valuation techniques and the degree of subjectivity used in making the estimates, comparisons between our disclosures and those of other companies may not be meaningful.

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Notes to Consolidated Financial Statements

Cash and Cash Equivalents

The carrying amounts reported in the consolidated statements of financial condition for cash and cash equivalents are reasonable approximations of their fair values.

HTM Investment Securities

The items are generally short term in nature, and accordingly, the carrying amounts reported in the consolidated statements of financial condition are reasonable approximations of their fair values.

Accrued Interest Receivable and Accrued Interest Payable

The carrying amount of accrued interest receivable and accrued interest payable approximates its fair value.

AFS Investment Securities

Fair values for investment securities are based on quoted market prices, if available (level 1). If quoted market prices are not available, then fair values are based on quoted market prices of comparable instruments (level 2).

Bank Stock

The fair value of bank stock is estimated at its carrying value and redemption price of \$100 per share.

Mortgage Loans Held for Sale

Mortgage loans held for sale are generally sold within of few months of origination. Therefore, the fair value of mortgage loans held for sale are equal to their carrying amounts.

Loans

For variable rate loans that reprice frequently and with no significant change in credit risk, fair value is based on carrying value. The fair value for other loans receivable was estimated using a discounted cash flow analysis, which uses interest rates currently being offered for loans with similar terms to borrowers of similar credit quality. Consideration was given to prepayment speeds, economic conditions, risk characteristics, and other factors considered appropriate.

Deposits

The fair values of deposits subject to immediate withdrawal, such as interest and noninterest checking, statement savings, and money market demand deposit accounts, are equal to their carrying amounts in the accompanying consolidated statements of financial condition. Fair values for certificates of deposit are estimated by discounting future cash flows using interest rates currently offered on certificates of deposit with similar remaining maturities.

Repurchase Agreements

Repurchase agreements are included in other borrowings on the consolidated statements of financial condition. The fair value of repurchase agreements is established using a discounted cash flow calculation that applies interest rates currently being offered on repurchase agreements with similar terms.

Short-Term Borrowings

Short-term borrowings are included in other borrowings on the consolidated statements of financial condition. The carrying amount of short-term borrowings approximates their fair value.

Off-Balance-Sheet Instruments

Off-balance-sheet instruments are primarily comprised of loan commitments and unfunded lines of credit that are generally priced at market rate at the time of funding. Therefore, these instruments have nominal value prior to funding and are not shown in the table.

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Notes to Consolidated Financial Statements

The estimated fair value of the Company's financial instruments at December 31, 2019 and 2018 was as follows:

	Fair Value Measurements				
	At December 31, 2019				
			Quoted Prices in Active Markets for Identical Assets Level 1	Significant Other Observable Inputs Level 2	Significant Unobservable Inputs Level 3
(In thousands)	Carrying value	Estimated fair value			
Financial Assets:					
Cash and cash equivalents	\$ 46,357	\$ 46,357	\$ 46,357	\$ -	\$ -
Investments held to maturity	42,767	42,767	-	42,767	-
Investments available for sale	51,224	51,224	-	51,224	-
Bank stock, at cost	2,138	2,138	-	-	2,138
Mortgage loans held for sale	4,449	4,449	-	4,449	-
Loans receivable, net	413,127	411,884	-	-	411,884
Accrued interest receivable	1,697	1,697	-	-	1,697
Financial liabilities:					
Demand deposits	305,627	305,627	-	305,627	-
Money market deposits	11,777	11,777	-	11,777	-
Savings deposits	46,065	46,065	-	46,065	-
Certificates of deposit	158,783	160,404	-	160,404	-
Other borrowings	2,290	2,274	-	2,274	-
Accrued interest payable	130	130	-	130	-

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Notes to Consolidated Financial Statements

Fair Value Measurements
At December 31, 2018

(In thousands)	Carrying value	Estimated fair value	Quoted Prices in Active Markets for Identical Assets Level 1			Significant Other Observable Inputs Level 2	Significant Unobservable Inputs Level 3
			Level 1	Level 2	Level 3		
Financial Assets:							
Cash and cash equivalents	\$ 12,114	\$ 12,114	\$ 12,114	\$ -	\$ -		
Investments held to maturity	59,126	59,126	-	59,126	-		
Investments available for sale	55,967	55,967	-	55,967	-		
Bank stock, at cost	1,964	1,964	-	-	1,964		
Mortgage loans held for sale	2,989	2,989	-	2,989	-		
Loans receivable, net	398,908	390,187	-	-	390,187		
Accrued interest receivable	1,737	1,737	-	-	1,737		
Financial liabilities:							
Demand deposits	270,136	270,136	-	270,136	-		
Money market deposits	15,928	15,928	-	15,928	-		
Savings deposits	49,208	49,208	-	49,208	-		
Certificates of deposit	154,824	156,016	-	156,016	-		
Other borrowings	8,157	8,052	4,983	3,069	-		
Accrued interest payable	128	128	-	128	-		

Note 12. Income Taxes

The components of income tax expense (benefit) are stated below:

(In thousands)	For the years ended December 31,	
	2019	2018
Income tax expense (benefit)		
Federal		
Current	\$ 843	\$ 1,128
Deferred	(435)	(148)
	<u>408</u>	<u>980</u>
State		
Current	648	788
Deferred	(203)	(78)
	<u>445</u>	<u>710</u>
Total income tax expense	<u>\$ 853</u>	<u>\$ 1,690</u>

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Notes to Consolidated Financial Statements

The following is a reconciliation between expected tax expense at the statutory rate of 21% for 2019 and 2018 and actual tax expense:

(In thousands)	For the years ended December 31,	
	2019	2018
Computed tax expense at statutory rate	\$ 856	\$ 1,450
Adjustments resulting from:		
State tax, net of federal benefit	309	545
Tax-exempt interest income	(206)	(167)
Bank owned life insurance	(50)	(121)
Stock-based compensation	(76)	(31)
Other	20	14
Income tax expense	<u>\$ 853</u>	<u>\$ 1,690</u>

Significant deferred tax assets and liabilities of the Bank at December 31, 2019 and 2018 are as follows:

(In thousands)	As of December 31,	
	2019	2018
Deferred tax assets:		
Allowance for loan losses	\$ 1,695	\$ 1,175
Deferred rent	35	35
Unrealized losses on AFS debt securities	-	106
Share-based compensation cost	139	146
Non-accrual interest	8	13
Other	77	12
Deferred tax assets	<u>1,954</u>	<u>1,487</u>
Deferred tax liabilities:		
Depreciation	(36)	(135)
Unrealized gains on AFS debt securities	(101)	-
Prepaid expenses	(24)	(7)
Deferred loan costs	(339)	(322)
Total deferred tax liabilities	<u>(500)</u>	<u>(464)</u>
Net deferred tax asset, included in other assets	<u>\$ 1,454</u>	<u>\$ 1,023</u>

The realizability of deferred tax assets is dependent upon various factors, including the generation of future taxable income, the existence of taxes paid and recoverable, the reversal of deferred tax liabilities, and tax planning strategies. In assessing the realizability of 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 the net operating loss carryforwards are available and the temporary differences representing net future deductibles reverse. Based upon these and other factors management has determined that it is more likely than not that the Company will realize the benefits of the deferred tax assets that exist at December 31, 2019.

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As of December 31, 2019 and 2018, the Company had no material unrecognized tax benefits or accrued interest and penalties. The Company's policy is to account for interest as a component of interest expense and penalties as a component of other expense.

As of December 31, 2019, the years 2016 – 2018 are open for federal examination and years 2015-2018 are open for state examinations.

Note 13. Leases

The Company has operating leases for a retail branch, our operation and administration center (main office) and certain equipment. The ROU assets obtained in exchange for operating lease obligations totaled \$1.1 million at January 1, 2019, the adoption date for ASU No. 2016-02. The Company's leases have remaining lease terms of 20 months to four years, some of which include options to extend the leases for up to five years. The main office lease expires on November 30, 2022, with an option to renew for two additional five-year terms. Because we may need to expand our office space, the extension options were excluded from the calculations of the ROU asset and lease liability.

The following table presents operating lease costs for the year ended December 31, 2019.

(In thousands)	For the year ended
	December 31, 2019
Operating lease cost	\$ 278
	<u>\$ 278</u>

A maturity analysis of operating lease liabilities and reconciliation of the undiscounted cash flows to the total of operating lease liabilities is as follows:

(In thousands)	As of
	December 31, 2019
2020	\$ 293
2021	300
2022	278
2023	-
2024	-
Thereafter	-
Total lease payments	<u>871</u>
Less imputed interest	<u>(45)</u>
Total	<u>\$ 826</u>

Total rent expense was \$245 thousand for the year ended December 31, 2018.

Note 14. Commitments and Contingencies

Financial Instruments with Off-Balance-Sheet Risk

The Bank is a party to financial instruments with off-balance-sheet risk in the normal course of business. These financial instruments include commitments to extend credit to meet the financing needs of its customers. Such commitments have been made in the normal course of business and at current prevailing market terms. The commitments, once funded, are principally to originate commercial loans and other loans secured by real estate. The Bank uses the same credit policies in making commitments and conditional obligations as it does for on-balance-sheet instruments.

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Commitments issued to potential borrowers of the Bank at December 31, 2019 and 2018 were as follows:

(In thousands)	As of December 31,	
	2019	2018
Fixed rate commitments	\$ 2,657	\$ 499
Variable/adjustable rate commitments	56,654	60,371
Total commitments	<u>\$ 59,311</u>	<u>\$ 60,870</u>

Legal Proceedings

From time to time, the Bank is a party to legal proceedings within the normal course of business wherein it enforces its security interest in loans made, and other matters of a similar nature. At December 31, 2019, the Company was neither engaged in any existing nor aware of any pending legal proceedings.

Note 15. Related-Party Transactions

The Bank routinely enters into transactions with its directors and executive officers. Such transactions are made in the ordinary course of business on substantially the same terms and conditions, including interest rates and collateral, as those prevailing at the same time for comparable transactions with other customers, and do not, in the opinion of management, involve more than normal credit risk or present other unfavorable features. The aggregate amount of loans to such related parties was \$1.4 million and \$1.5 million at December 31, 2019 and 2018, respectively. During 2019 and 2018, new loans and credit line advances to such related parties amounted to \$25 thousand and \$362 thousand, respectively, and repayments amounted to \$184 thousand and \$79 thousand, respectively. The aggregate amount of deposits from related parties was \$42.5 million and \$42.8 million at December 31, 2019 and 2018, respectively.

The Bank engaged in certain property inspection and construction services with an entity that is affiliated with a director of the Bank. Such aggregate services amounted to fees of \$24 thousand and \$27 thousand for the years ended December 31, 2019 and 2018, respectively. In management's opinion, the terms of the services provided were substantially equivalent to that which would have been obtained from unaffiliated parties.

Note 16. Dividend Policy

Company

The Company has not paid a cash dividend since its inception in June 2000. Any payment of cash dividends to its shareholders would be dependent on the payment of a cash dividend from the Bank to the Company. The payment of cash dividends by the Bank to the Company is limited under federal banking law. The Company's future dividend policy is subject to the discretion of its board of directors and will depend upon a number of factors, including future earnings, financial conditions, cash needs, and general business conditions. Holders of common stock will be entitled to receive dividends as and when declared by the board of directors out of funds legally available for that purpose.

Bank

The amount of dividends that may be paid by the Bank depends upon the Bank's earnings and capital position, and is limited by New Jersey and federal law, regulations, and policies. As a state chartered bank subject to New Jersey and FDIC regulations, the Bank cannot pay any dividend if the dividend would reduce the required surplus of the Bank as defined in New Jersey statutes. As a matter of policy, the FDIC expects state banks to follow the national bank dividend limits, which allow a bank to pay dividends up to the amount of net profits of the current year plus the retained net profits from the last two years. Amounts in excess of that would require prior approval of the FDIC. In addition, the FDIC and the state of New Jersey have authority to further limit any dividends to be paid by the Bank in a specific case. No specific dividend restrictions have been imposed on the Bank at this time.

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Notes to Consolidated Financial Statements

Note 17. Employee Benefits

The Bank instituted a qualified defined contribution plan (“the 401(K) Plan”) for all current employees in August 2005. All eligible employees are 100% vested in any required safe harbor contributions. The Bank made safe harbor contributions in the amount of \$189 thousand and \$179 thousand during 2019 and 2018, respectively.

Note 18. Stock Option Plans

We have two current stock option programs the 2013 Outside Director Plan and the 2013 Employee Stock Option Plan. The 2013 Outside Director Plan provides up to 245,861 options for nonemployee directors. The exercise price of options granted under this program is required to be equal to at least the fair market value of common stock as of the grant date. All options granted under this plan vest in five equal annual installments or upon retirement. These options expire 10 years from the grant date. At December 31, 2019, 161,683 options were outstanding under this plan.

The 2013 Employee Stock Option Plan provides up to 243,805 options for key employees. The exercise price of options granted under this program will be equal to at least the fair market value of common stock as of the grant date. All options granted under this plan vest in five equal annual installments, upon retirement or a change in control of the Company. These options expire 10 years from the grant date. At December 31, 2019, 120,026 options were outstanding under this plan.

Compensation expense for stock options is recognized over the requisite service period. During 2019 and 2018, we recognized \$82 thousand and \$106 thousand, respectively, in compensation expense for stock options. At December 31, 2018, approximately \$143 thousand remained to be recognized in compensation expense over a weighted-average period of less than three years.

We had two other stock option programs, the 2003 Outside Director Plan and the 2003 Employee Stock Option Plan. The ability to grant new options under these plans has expired.

Under the 2003 Outside Director Plan, as amended, 31,770 options remain outstanding at December 31, 2019 for nonemployee directors. The exercise price of options granted under this program is required to be equal to at least the fair market value of common stock as of the grant date. All options granted under this plan are fully vested. These options expire 10 years from the grant date. Under the 2003 Employee Stock Option Plan, as amended, no options remain outstanding at December 31, 2019 for key employees.

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The fair value of each stock option award is estimated on the date of the grant using the Black-Scholes option-pricing model. The risk-free interest rate for the expected term of the stock option awarded is based on the U.S. Treasury yield curve in effect at the time of the grant. The volatility of the Company's stock is based on a combination of historical volatility and peer data over a span of time equal to the expected life of stock option awards, which is the period of time the Company estimates that stock options granted will remain outstanding. There were no stock options granted in 2019 and 2018. The simplified method averages an award's weighted average vesting period and its contractual term.

A summary status of the Company's stock option plans as of December 31, 2019 and 2018, and the changes during the years then ended, is as follows:

	2019				2018	
	Options	Weighted Average Exercise Price	Weighted Average Remaining Term (yrs)	(1) Aggregate Intrinsic Value	Options	Weighted Average Exercise Price
Options outstanding at beginning of year	412,474	\$ 6.50	7.3		464,443	\$ 6.30
Granted	-	-			-	-
Exercised	(87,820)	4.23			(50,309)	4.80
Forfeited or expired	(11,175)	5.99			(1,660)	4.15
Options outstanding at the end of the year	<u>313,479</u>	<u>\$ 7.15</u>	8.4	<u>\$ 1,228</u>	<u>412,474</u>	<u>\$ 6.50</u>
Options exercisable at the end of the year	<u>265,531</u>	<u>\$ 6.12</u>	6.7	<u>\$ 1,150</u>	<u>320,167</u>	<u>\$ 5.38</u>

- (1) The aggregate intrinsic value of a stock option in the table above (shown in thousands) represents the total pre-tax intrinsic value (the amount by which the current market value of the underlying stock exceeds the exercise price of the option) that would have been received by the option holders had they exercised their options on December 31, 2019. The intrinsic value varies based on the changes in the market value in the Company's stock.

The Company issues new shares upon the exercise of stock options.

The following table provides detail for non-vested stock options under the 2013 Outside Director and Employee Stock Option Plans as of December 31, 2019:

	Options	Weighted Average Exercise Price
Non-vested options December 31, 2018	92,307	\$ 8.07
Granted	-	-
Forfeited	(5,626)	8.23
Vested	<u>(38,733)</u>	<u>7.10</u>
Non-vested options December 31, 2019	<u>47,948</u>	<u>\$ 8.47</u>

Note 19. Regulatory Matters

The Bank is subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory – and possibly additional discretionary – actions

1ST COLONIAL BANCORP, INC. AND SUBSIDIARY

Notes to Consolidated Financial Statements

by regulators that, if undertaken, could have a direct material effect on the Bank's consolidated financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of the Bank's assets, liabilities, and certain off-balance-sheet items as calculated under regulatory accounting practices. The Bank's capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

In July 2013, the federal bank regulatory agencies adopted the final reforms on capital and liquidity generally referred to as "Basel III", which were published by the Basel Committee on Banking Supervision and the Financial Stability Board. Under Basel III, 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 comprised of Common Equity Tier 1 above its minimum risk-based capital requirements in an amount greater than 2.5% of total risk-weighted assets. The new minimum capital requirements became effective on January 1, 2015. The capital conservation buffer requirements phase in over a three-year period beginning January 1, 2016. The capital conservation buffer for 2019 was 2.5% and for 2018 was 1.875%. As of December 31, 2019, the Bank met all capital adequacy requirements to which it is subject and met the criteria for a well-capitalized institution.

The Bank's actual capital amounts and ratios at December 31, 2019 and 2018 are presented in the following:

(Dollars in thousands)	Actual		For capital adequacy purposes		For capital adequacy purposes with capital conservation buffer*		To be well capitalized under prompt corrective action provision	
	Amount	Ratio	Amount	Ratio*	Amount	Ratio*	Amount	Ratio
Total capital (to risk-weighted assets)								
At December 31, 2019	\$ 51,758	14.443%	\$ 28,668	8.00%	\$ 37,627	10.500%	\$ 35,835	10.00%
At December 31, 2018	\$ 48,042	13.416%	\$ 28,647	8.00%	\$ 35,361	9.875%	\$ 35,808	10.00%
Tier 1 capital (to risk-weighted assets)								
At December 31, 2019	\$ 47,252	13.186%	\$ 21,501	6.00%	\$ 30,460	8.500%	\$ 28,668	8.00%
At December 31, 2018	\$ 43,552	12.163%	\$ 14,323	6.00%	\$ 28,199	7.875%	\$ 28,647	8.00%
Tier 1 capital (to average assets, leverage)								
At December 31, 2019	\$ 47,252	8.249%	\$ 22,913	4.00%	\$ 22,913	4.000%	\$ 28,641	5.00%
At December 31, 2018	\$ 43,552	7.977%	\$ 21,838	4.00%	\$ 21,838	4.000%	\$ 27,297	5.00%
Common equity Tier 1 (to risk-weighted assets)								
At December 31, 2019	\$ 47,252	13.186%	\$ 16,126	4.50%	\$ 25,085	7.000%	\$ 23,293	6.50%
At December 31, 2018	\$ 43,552	12.163%	\$ 16,114	4.50%	\$ 22,828	6.375%	\$ 23,275	6.50%

Note 20. Parent Company Financial Information

A summary of the statements of financial condition at December 31, 2019 and 2018 is as follows:

(In thousands)	December 31, 2019	December 31, 2018
Assets		
Cash in subsidiary	\$ 133	\$ 260
Investment in subsidiary	47,510	43,276
Deferred tax asset	138	147
Other assets	129	85
Total assets	<u>\$ 47,910</u>	<u>\$ 43,768</u>
Liabilities and Shareholders' Equity		
Other liabilities	\$ 4	\$ 72
Shareholders' equity	47,906	43,696
Total liabilities and shareholders' equity	<u>\$ 47,910</u>	<u>\$ 43,768</u>

1ST COLONIAL BANCORP, INC. AND SUBSIDIARY

Notes to Consolidated Financial Statements

A summary of the statements of operations for the years ended December 31, 2019 and 2018 is as follows:

(In thousands)	2019	2018
Equity income from subsidiary	\$ 3,350	\$ 5,348
Interest income	-	-
Total income	3,350	5,348
Other expenses:		
Other operating expenses	162	213
Total other expenses	162	213
Income before income tax benefit	3,188	5,135
Income tax benefit	(36)	(80)
Net income	\$ 3,224	\$ 5,215

A summary of the statements of cash flows for the years ended December 31, 2019 and 2018 is as follows:

(In thousands)	2019	2018
Cash flows from operating activities:		
Net income	\$ 3,224	\$ 5,215
Adjustments to reconcile net income to net cash (used in) provided by operating activities:		
Equity in income from subsidiary	(3,350)	(5,348)
Stock-based compensation expense	82	106
Decrease (increase) deferred income tax benefit	8	(36)
Increase in other assets	(44)	(43)
(Decrease) increase in other liabilities	(67)	70
Total adjustments	(3,371)	(5,251)
Net cash used in operating activities	(147)	(36)
Cash flows from investing activities:		
Investment in subsidiary	(350)	-
Net cash used in investing activities	(350)	-
Cash flows from financing activities:		
Cost of processing stock dividend	(3)	(5)
Proceeds from sale of stock	373	245
Net cash provided by financing activities	370	240
Net (decrease) increase in cash and cash equivalents	(127)	204
Cash and cash equivalents at beginning of year	260	56
Cash and cash equivalents at end of year	\$ 133	\$ 260
Cash paid during the year for:		
Interest	\$ 5,434	\$ 4,026
Income taxes paid	1,021	2,271
Supplemental disclosures:		
Net change in unrealized losses on securities available for sale, net of taxes of \$204 and \$(105) for 2019 and 2018, respectively	\$ 534	\$ (275)

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Notes to Consolidated Financial Statements

Note 21. Subsequent Events

Subsequent events are events or transactions that occur after the balance sheet date but before financial statements are issued. Recognized subsequent events are events or transactions that provide additional evidence about conditions that existed at the date of the balance sheet, including the estimates inherent in the process of preparing financial statements. Non-recognized subsequent events are events that provide evidence about conditions that did not exist at the date of the statement of financial condition but arose after that date and warrant disclosure. Management has reviewed events occurring through the date the financial statements were issued and no subsequent events occurred requiring accrual or disclosure except as noted below:

On January 29, 2020, the Company declared a 5% stock dividend to all shareholders of record as of April 1, 2020 payable on April 15, 2020. The number of shares issued was 236,169 and the transaction amount reclassified from Retained Earnings to Additional Paid-In Capital was \$1.1 million. Additionally, on January 29, 2020, the Company announced the retirement of our President and Chief Executive Officer, Gerard Banmiller, and the appointment of his successor, Robert White.

Also subsequent to December 31, 2019, is the ongoing COVID-19 global pandemic, which has caused severe economic and social disruption. We continue to assess the affects of the pandemic on our customers, team members, and the communities we serve. The extent of the effect of the COVID-19 pandemic on the Company is uncertain.

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Stock Listing

1st Colonial's Common Stock is traded under the Symbol "FCOB"

Board of Directors

Linda M. Rohrer, Chairman
Letitia G. Colombi
Michael C. Haydinger
Stanley H. Molotsky

Curt Byerley
John J. Donnelly, IV
Harvey Johnson, Esquire

Thomas A. Clark, III, Esquire
Eduardo F. Enriquez, M. D.
Harrison Melstein

Advisory Board

Linda M. Rohrer, Chairman
Elaine M. Damm
Lawrence A. Levine, D.P.M
Tammy Savidge
Dr. Charles N. Wahl, DMD

William Bittner, Jr.
William Getzinger, III
James Poliero
Peter R. Thorndike, Esquire
Charles Zambito

Steve Cordasco
Richard Hardenbergh
Dean Ragone
John F. Wachter, Jr.

Executive Officers

Robert B. White, President and Chief Executive Officer
Frank J. Monaghan, Executive Vice President and Chief Operating Officer
Irene H. Clark, Executive Vice President, Deposit Operations
Mary Kay Shea, Senior Vice President and Chief Financial Officer

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