

**NOBLE BANCSHARES, INC.
AND SUBSIDIARY**

CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2019 AND 2018

**NOBLE BANCSHARES, INC. AND SUBSIDIARY
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DECEMBER 31, 2019 AND 2018**

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INDEPENDENT AUDITORS' REPORT

To the Board of Directors and Stockholders
Noble Bancshares, Inc.

We have audited the accompanying consolidated statements of financial condition of Noble Bancshares, Inc. and Subsidiary (the Company) 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 Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; 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 auditors consider 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 Noble Bancshares, Inc. and 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 accounting principles generally accepted in the United States of America.

Warren Averett, LLC

Anniston, Alabama
April 10, 2020

**NOBLE BANCSHARES, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION
DECEMBER 31, 2019 AND 2018**

ASSETS	2019	2018
	<u> </u>	<u> </u>
CASH AND CASH EQUIVALENTS		
Cash and due from banks	\$ 4,789,838	\$ 4,412,107
Interest bearing deposits in banks	7,729,476	9,077,369
Federal funds sold	<u>4,900,000</u>	<u>4,899,930</u>
Total cash and cash equivalents	17,419,314	18,389,406
SECURITIES, AVAILABLE-FOR-SALE	58,800,311	61,732,511
SECURITIES RESTRICTIVE INVESTMENTS	1,344,450	1,266,850
INVESTMENT IN ANNUITIES	1,724,693	1,724,693
LOANS, NET OF ALLOWANCE FOR LOAN LOSSES	173,679,252	159,783,313
LOANS, HELD-FOR-SALE	160,700	1,215,250
ACCRUED INTEREST RECEIVABLE	987,787	1,069,561
PREPAID EXPENSES	311,680	271,852
FORECLOSED REAL ESTATE	234,343	187,000
PREMISES AND EQUIPMENT, NET	6,922,595	6,960,666
BANK-OWNED LIFE INSURANCE	4,223,226	4,130,593
DEFERRED TAX	857,539	649,320
INCOME TAXES RECEIVABLE	4,771	186,480
OTHER ASSETS	<u>839,058</u>	<u>1,241,070</u>
TOTAL ASSETS	<u><u>\$ 267,509,719</u></u>	<u><u>\$ 258,808,565</u></u>

See notes to the consolidated financial statements

**NOBLE BANCSHARES, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION
DECEMBER 31, 2019 AND 2018**

LIABILITIES AND STOCKHOLDERS' EQUITY	2019	2018
DEPOSITS		
Noninterest-bearing checking	\$ 42,864,250	\$ 38,766,121
Interest-bearing:		
Checking	124,052,352	128,963,104
Savings	11,080,217	10,330,964
Time deposits	61,894,787	53,013,854
Total deposits	239,891,606	231,074,043
BORROWINGS	3,500,000	3,500,000
ACCRUED INTEREST PAYABLE	266,171	213,343
DEFERRED COMPENSATION	561,233	462,922
OTHER LIABILITIES	64,627	1,446,738
Total liabilities	244,283,637	236,697,046
STOCKHOLDERS' EQUITY		
Common stock, \$1 par value; 5,000,000 shares authorized; 1,478,360 shares issued and 1,451,444 and 1,464,860 shares outstanding for the years ended December 31, 2019 and 2018, respectively	1,478,360	1,478,360
Additional paid-in capital	18,795,074	18,766,399
Accumulated other comprehensive loss	(196,449)	(1,021,142)
Treasury stock, 26,916 and 13,500 shares at cost at December 31, 2019 and 2018, respectively	(379,680)	(173,175)
Retained earnings	3,528,777	3,061,077
Total stockholders' equity	23,226,082	22,111,519
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$ 267,509,719	\$ 258,808,565

See notes to the consolidated financial statements

**NOBLE BANCSHARES, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF INCOME
FOR THE YEARS ENDED DECEMBER 31, 2019 AND 2018**

	<u>2019</u>	<u>2018</u>
INTEREST INCOME		
Interest and fees on loans	\$ 9,905,815	\$ 9,020,722
Interest on investment securities	1,614,703	1,637,454
Interest on due from accounts	420,385	213,653
	<u>11,940,903</u>	<u>10,871,829</u>
INTEREST EXPENSE		
Interest on money market and checking	633,627	502,942
Interest on savings	35,637	28,524
Interest on certificates of deposit	1,194,049	680,888
Interest on borrowed funds	187,882	106,362
	<u>2,051,195</u>	<u>1,318,716</u>
Total interest expense	<u>2,051,195</u>	<u>1,318,716</u>
NET INTEREST INCOME	9,889,708	9,553,113
PROVISION FOR LOAN LOSSES	<u>2,839,492</u>	<u>417,136</u>
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	<u>7,050,216</u>	<u>9,135,977</u>

See notes to the consolidated financial statements

**NOBLE BANCSHARES, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF INCOME
FOR THE YEARS ENDED DECEMBER 31, 2019 AND 2018**

	<u>2019</u>	<u>2018</u>
NONINTEREST INCOME		
Service charges, fees, and commissions	\$ 2,303,030	\$ 2,203,159
Bank-owned life insurance income	92,634	93,814
Realized gain on sale of securities	730,276	-
Realized gain on sale of foreclosed real estate	-	20,211
Miscellaneous noninterest income	382,906	17,052
Total noninterest income	<u>3,508,846</u>	<u>2,334,236</u>
NONINTEREST EXPENSES		
Salaries and employee benefits	5,109,202	4,945,163
Data processing expense	1,742,449	1,375,654
Occupancy expense	753,176	712,867
Professional fees	358,259	214,797
Business development expense	282,241	240,503
Insurance expense	123,063	121,469
Equipment expense	184,963	171,078
Supplies expense	118,765	121,947
Write-downs and losses on foreclosed real estate	29,359	-
Realized loss on sale of securities	-	2,548
Deferred compensation expense	115,355	103,203
Communication expense	77,109	75,678
Travel expense	75,088	65,251
Teller outages and other losses	35,233	18,063
Other expenses	281,409	278,226
Total noninterest expenses	<u>9,285,671</u>	<u>8,446,447</u>
INCOME BEFORE INCOME TAXES	1,273,391	3,023,766
INCOME TAX PROVISION	<u>146,503</u>	<u>472,326</u>
NET INCOME	<u>\$ 1,126,888</u>	<u>\$ 2,551,440</u>

See notes to the consolidated financial statements

**NOBLE BANCSHARES, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
FOR THE YEARS ENDED DECEMBER 31, 2019 AND 2018**

	<u>2019</u>	<u>2018</u>
NET INCOME	\$ 1,126,888	\$ 2,551,440
OTHER COMPREHENSIVE INCOME (LOSS)		
Unrealized gains (losses) on available-for-sale securities:		
Unrealized holding gains (losses) arising during the period	1,774,191	(663,363)
Reclassification adjustments for (gains) losses included in net income	<u>(730,276)</u>	<u>2,548</u>
Net unrealized gain (loss)	1,043,915	(660,815)
Income tax related to items of other comprehensive income	<u>(219,222)</u>	<u>56,641</u>
Other comprehensive gain (loss)	<u>824,693</u>	<u>(604,174)</u>
COMPREHENSIVE INCOME	<u>\$ 1,951,581</u>	<u>\$ 1,947,266</u>

See notes to the consolidated financial statements

NOBLE BANCSHARES, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY
FOR THE YEARS ENDED DECEMBER 31, 2019 AND 2018

	Common Stock	Additional Paid-in Capital	Accumulated Other Comprehensive Income (Loss)	Treasury Stock	Retained Earnings	Total
BALANCE AT DECEMBER 31, 2017	\$ 1,478,360	\$ 18,766,399	\$ (416,968)	\$ (173,175)	\$ 1,095,581	\$ 20,750,197
Dividends declared and paid	-	-	-	-	(585,944)	(585,944)
Net income	-	-	-	-	2,551,440	2,551,440
Other comprehensive loss	-	-	(604,174)	-	-	(604,174)
BALANCE AT DECEMBER 31, 2018	1,478,360	18,766,399	(1,021,142)	(173,175)	3,061,077	22,111,519
Purchase of treasury stock	-	-	-	(206,505)	-	(206,505)
Stock options	-	28,675	-	-	-	28,675
Dividends declared and paid	-	-	-	-	(659,188)	(659,188)
Net income	-	-	-	-	1,126,888	1,126,888
Other comprehensive gain	-	-	824,693	-	-	824,693
BALANCE AT DECEMBER 31, 2019	<u>\$ 1,478,360</u>	<u>\$ 18,795,074</u>	<u>\$ (196,449)</u>	<u>\$ (379,680)</u>	<u>\$ 3,528,777</u>	<u>\$ 23,226,082</u>

See notes to the consolidated financial statements

**NOBLE BANCSHARES, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2019 AND 2018**

	<u>2019</u>	<u>2018</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	\$ 1,126,888	\$ 2,551,440
Adjustments to reconcile net income to net cash provided by operating activities:		
Change in deferred tax	(427,441)	(45,081)
Change in income tax receivable	181,709	(186,480)
Provision for loan losses	2,839,492	417,136
Net amortization of securities	327,348	442,894
Depreciation of premises and equipment	424,791	377,626
Write-down of foreclosed real estate	17,005	-
(Gain) loss on sale of foreclosed real estate	12,354	(20,211)
(Gain) loss on disposal of premises and equipment	7,553	-
Realized gain on sale of securities, net	(730,276)	(775)
Change in accrued interest receivable	81,774	(146,564)
Change in prepaid expenses	(39,828)	(20,056)
Change in accrued interest payable	52,828	87,605
Change in deferred compensation	98,311	94,703
Change in income tax payable	-	(70,263)
Change in other, net	(980,097)	25,737
Net cash provided by operating activities	<u>2,992,411</u>	<u>3,507,711</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Activity in available-for-sale securities:		
Purchases	(38,362,297)	(3,558,233)
Sales	37,028,012	1,253,480
Maturities, paydowns, and calls	5,713,328	2,278,968
Purchases of securities restrictive investments	(77,600)	83,950
Net change in annuities value	-	(164,503)
Net change in loans receivable	(16,882,868)	(28,216,953)
Net change in loans held-for-sale	1,054,550	(598,750)
Proceeds from the sale of foreclosed real estate	70,735	357,811
Purchases of premises and equipment	(394,273)	(1,034,896)
Change in bank owned life insurance	(92,633)	(93,814)
Net cash used in investing activities	<u>(11,943,046)</u>	<u>(29,692,940)</u>

See notes to the consolidated financial statements

**NOBLE BANCSHARES, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2019 AND 2018**

	<u>2019</u>	<u>2018</u>
CASH FLOWS FROM FINANCING ACTIVITIES		
Net increase in deposits	\$ 8,817,563	\$ 28,145,192
Allocation from granting of warrants/options	28,673	-
Treasury stock	(206,505)	-
Net change in borrowings	-	2,500,000
Cash dividends	<u>(659,188)</u>	<u>(585,944)</u>
Net cash provided by financing activities	<u>7,980,543</u>	<u>30,059,248</u>
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(970,092)	3,874,019
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	<u>18,389,406</u>	<u>14,515,387</u>
CASH AND CASH EQUIVALENTS AT END OF YEAR	<u>\$ 17,419,314</u>	<u>\$ 18,389,406</u>
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION		
Cash paid during the year for interest	<u>\$ 1,998,367</u>	<u>\$ 1,231,111</u>
NONCASH DISCLOSURES		
Loans transferred to other real estate owned	<u>\$ 162,637</u>	<u>\$ 127,500</u>
Proceeds from sales of foreclosed real estate financed through loans	<u>\$ 15,200</u>	<u>\$ 196,650</u>
Net change in unrealized gain (loss) on securities available-for-sale, net of taxes	<u>\$ 824,693</u>	<u>\$ (604,174)</u>

See notes to the consolidated financial statements

NOBLE BANCSHARES, INC. AND SUBSIDIARY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2019 AND 2018

1. ORGANIZATION

Noble Bancshares, Inc. (the Company), an Alabama corporation, formed on June 1, 2017, operates in the domestic commercial banking industry. The Company's subsidiary, Noble Bank & Trust (the Bank) was formed on October 5, 2005, by national charter and on June 27, 2013, the Bank was permitted to change its charter from a national bank to a state bank. It is now regulated by the State of Alabama Banking Department and the Federal Reserve. The Bank operates five branches in Alabama, with the main branch being located in Anniston and the other branches being located in Oxford, Piedmont, Alexandria, and Birmingham.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting and reporting policies of the Company and its subsidiary conform to accounting principles generally accepted in the United States of America (U.S. GAAP) and to general practice within the banking industry. The following summarizes the most significant of these policies.

Principles of Consolidation

The consolidated financial statements include the accounts of the Company and the Bank. All significant intercompany balances and transactions have been eliminated. Unless otherwise indicated herein, the financial results of the Company refer to the Company and the Bank on a consolidated basis.

Use of Estimates

The preparation of consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term are related to the determination of the allowance for loan losses, the valuation of deferred tax assets, the valuation of real estate acquired in connection with foreclosures or in satisfaction of loans, and the fair value of financial instruments.

The determination of the adequacy of the allowance for loan losses is based on estimates that are particularly susceptible to significant changes in the economic environment and market conditions. In connection with the determination of the estimated losses on loans, management obtains independent appraisals for significant collateral. The Bank's loans are generally secured by specific items of collateral, including real property, consumer assets, and business assets. Although the Bank has a diversified loan portfolio, a substantial portion of its debtors' ability to honor their contracts is dependent on local economic conditions.

NOBLE BANCSHARES, INC. AND SUBSIDIARY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2019 AND 2018

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

While management used available information to recognize losses on loans, further reduction in the carrying amounts of loans may be necessary based on changes in local economic conditions. In addition, regulatory agencies, as an integral part of their examination process, periodically review the estimated losses on loans. Such agencies may require the Bank to recognize additional losses based on their judgments about information available to them at the time of their examination. Because of these factors, it is reasonably possible that the estimated losses on loans may change materially in the near term. However, the amount of the change that is reasonably possible cannot be estimated.

Significant Group Concentrations of Credit Risk

The majority of the Company's activities are with customers in north central Alabama. The types of securities in which the Company invests are discussed in Note 3. The types of lending performed by the Company are discussed in Note 4. The Company does not have any concentrations to any one industry or customer. The Company's geographic concentration and the risk therein is discussed in Note 11.

Cash and Cash Equivalents

The Company considers cash and due from banks, federal funds sold, and all highly liquid debt instruments purchased with a maturity of three months or less to be cash and cash equivalents.

The Company maintains cash and cash equivalents in various correspondent or other bank accounts. The amounts by which cash and cash equivalents exceeded Federal Deposit Insurance Corporation (FDIC) insurance coverage at December 31, 2019 and 2018, were \$9,560,767 and \$10,905,886, respectively. Management monitors these bank accounts and does not expect to incur any losses from such accounts. In addition, federal funds sold are not insured or guaranteed by other parties.

The Bank is required by regulatory authorities to maintain reserve balances in cash or on deposit with the Federal Reserve Bank based on a percentage of deposits (approximately \$2,743,000 and \$2,742,000 at December 31, 2019 and 2018, respectively).

Securities Available-for-Sale

Securities available-for-sale represent those securities intended to be held for an indefinite period of time, including securities that management intends to use as part of its asset/liability strategy or that may be sold in response to changes in interest rates, changes in prepayment risk, the need to increase regulatory capital, or other similar factors. Securities available-for-sale are recorded at market value with unrealized gains and losses, net of any tax effect, and are reported as other comprehensive income (loss) in a separate component of stockholders' equity until realized. Gains or losses on disposition are based on the net proceeds and the adjusted carrying amount on the securities sold, using the specific identification method. The estimated values are provided by security dealers who have obtained quoted prices.

NOBLE BANCSHARES, INC. AND SUBSIDIARY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2019 AND 2018

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

Purchase premiums and discounts are recognized in interest income using a method which approximates the interest method over the terms of the securities. Declines in the fair value of available-for-sale securities below their cost that are deemed to be other-than-temporary are reflected in earnings as realized losses. In estimating other-than-temporary impairment losses, management considers (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, and (3) the intent and ability of the Bank to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery of fair value. Gains and losses on the sale of securities are recorded on the trade date and are determined using the specific identification method.

Securities Restrictive Investments

Securities restrictive investments represent those securities whose sale is restricted to approved other organizations or the issuing company. Those securities are carried at cost, and their value is determined by the ultimate recoverability of par value.

Investment in Annuities

The Company has purchased annuity contracts on certain key employees. These contracts are recorded at their cash surrender value or the amount that can be realized. Income from these contracts and changes in the cash surrender value are recorded in noninterest income.

Loans

Loans that management has the intent and ability to hold for the foreseeable future are reported at their outstanding principal balances net of any unearned income, charge-offs, and unamortized fees and costs. Loan origination and commitment fees, as well as certain origination costs, when material, are deferred and amortized as a yield adjustment over the lives of the related loans using the interest method or the straight-line method.

Troubled Debt Restructurings (TDRs)

Modifications to a borrower's debt agreement are considered troubled debt restructurings (TDRs) if a concession is granted for economic or legal reasons related to a borrower's financial difficulties that otherwise would not be considered. TDRs are undertaken in order to improve the likelihood of recovery on the loan and may take the form of modifications made with the stated interest rate lower than the current market rate for new debt with similar risk, other modifications to the structure of the loan that fall outside of normal underwriting policies and procedures, or in certain limited circumstances, forgiveness of principal or interest. TDRs can involve loans remaining on nonaccrual, moving to nonaccrual, or continuing on accruing status, depending on the individual facts and circumstances of the borrower.

Income Recognition on Impaired and Nonaccrual Loans

Loans, including impaired loans, are generally classified as nonaccrual if they are past due as to maturity or payment of principal or interest for a period of more than 90 days, unless such loans are well-collateralized and in the process of collection. If a loan or a portion of a loan is classified as doubtful or is partially charged off, the loan is generally classified as nonaccrual.

NOBLE BANCSHARES, INC. AND SUBSIDIARY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2019 AND 2018

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

Loans that are on a current payment status or past due less than 90 days may also be classified as nonaccrual if repayment in full of principal and/or interest is in doubt. Loans may be returned to accrual status when all principal and interest amounts contractually due are reasonably assured of repayment within an acceptable period of time, and there is a sustained period of repayment performance by the borrower, in accordance with the contractual terms of interest and principal.

While a loan is classified as nonaccrual, and the future collectability of the recorded loan balance is doubtful, collections of principal and interest are generally applied as a reduction to principal outstanding, except in the case of loans with scheduled amortizations where the payment is generally applied to the oldest payment due. When the future collectability of the recorded loan balance is expected, interest income may be recognized on a cash basis. In the case where a nonaccrual loan has been partially charged off, recognition of interest on a cash basis is limited to that which would have been recognized on the recorded loan balance at the contractual interest rate. Receipts in excess of that amount are recorded as recoveries to the allowance for loan losses until prior charge-offs have been fully recovered. Interest income recognized on a cash basis was immaterial for the years ended December 31, 2019 and 2018.

Allowance for Loan Losses

The allowance for loan losses represents management's estimate of probable and reasonable credit losses in loans as of the balance sheet date. The estimate of the allowance is based on a variety of factors, including an evaluation of the loan portfolio, past loss experience, adverse situations that have occurred, but are not yet known, that may affect the borrower's ability to repay, the estimated value of underlying collateral, and current economic conditions.

For purposes of determining the allowance for loan losses, the Bank has segmented loans into the following segments: commercial, financial, and agricultural; real estate – construction, land development, and other land; real estate – mortgage; and consumer. Significant judgment is used to determine the estimation method that fits the credit risk characteristics of each portfolio segment. The Bank uses internally developed models in this process. Management must use judgment in establishing input metrics for the modeling processes. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as information becomes available and as economic conditions change.

Loans considered to be uncollectible are charged-off against the allowance. The amount and timing of charge-offs on loans includes consideration of the loan type, length of delinquency, insufficiency of collateral value, lien priority, and the overall financial condition of the borrower. Recoveries on loans previously charged-off are credited back to the allowance. Loans that have been charged-off against the allowance are periodically monitored to evaluate whether further adjustments to the allowance are necessary.

NOBLE BANCSHARES, INC. AND SUBSIDIARY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2019 AND 2018

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

The allowance for loan losses consists of three components: general, specific, and unallocated, as follows:

- The general component covers non-classified loans and is based on historical loss experience adjusted for qualitative factors, which includes trend assessments in delinquent and nonaccrual loans, unanticipated charge-offs, prevailing economic conditions, changes in lending personnel experience, changes in lending policies or procedures, and other influencing factors.
- The specific component is determined for impaired loans, including TDRs, individually based on management's evaluation of the borrower's overall financial condition, resources, and payment record; the prospects for support from any financially responsible guarantors; and the realizable value of any collateral. Reserves are established for these loans based upon an estimate of probable losses for the individual loans deemed to be impaired. This estimate considers all available evidence using one of the methods provided by applicable authoritative guidance. Loans determined to be collateral dependent are measured at the fair value of collateral less disposal costs. Loans for which impaired reserves are provided are excluded from the general component reserve calculations described above to prevent duplicate reserves.
- The unallocated component is not allocated to any specific category of loans. This unallocated portion of the allowance reflects management's best estimate of the elements of imprecision and estimation of risk inherent in the calculation of the overall allowance. Due to the subjectivity involved in determining the overall allowance, including the unallocated portion, the portion considered unallocated may fluctuate from period to period based on management's evaluation of the factors affecting the assumptions used in calculating the allowance, including historical loss experience, current economic conditions, industry or borrower concentrations, and the status of merged institutions.

A loan is considered impaired when, based on current information and events, it is probable that the Bank will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. If management determines that the value of the impaired loan is less than the recorded investment in the loan, impairment is recognized through a charge-off to the allowance. Interest income is recognized as earned unless the loan is placed on nonaccrual status.

NOBLE BANCSHARES, INC. AND SUBSIDIARY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2019 AND 2018

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed. Impairment is measured on a loan-by-loan basis for commercial and construction loans by either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's obtainable market price, or the fair value of the collateral if the loan is collateral dependent. Generally, impaired loans include loans on nonaccrual status, loans that have been assigned a specific allowance for credit losses, loans that have been partially charged off, and loans designated as troubled debt restructurings.

Based on facts and circumstances available, management believes that the allowance for loan losses is adequate to cover any probable losses in the Bank's loan portfolio. However, future adjustments to the allowance may be necessary, and the Bank's results of operations could be adversely affected if circumstances differ substantially from the assumptions used by management in determining the allowance for loan and lease losses. Management believes that it has established the allowance in accordance with generally accepted accounting principles and has taken into account the views of its regulators and the current economic environment. There can be no assurance that in the future the Bank's regulators or its economic environment will not require further increases in the allowance.

Asset Quality

Written underwriting standards established by management govern the lending activities of the Bank. An established loan policy requires appropriate documentation including borrower financial data and credit reports. For loans secured by real property, the Bank generally requires property appraisals, title insurance or a title opinion, hazard insurance, and flood insurance, where appropriate. Loan payment performance is monitored, and late charges are assessed on past due accounts. Legal proceedings are instituted, as necessary, to minimize loss. Commercial and residential loans of the Bank are periodically reviewed through a loan review process. All other loans are also subject to loan review through a periodic sampling process.

The Bank uses an asset risk classification system consistent with guidelines established by the Uniform Financial Institution Ratings System (UFIRS) as part of its efforts to monitor asset quality. In connection with examinations of insured institutions, both federal and state examiners also have the authority to identify problem assets and, if appropriate, classify them. The Bank has eight credit quality indicators for loans, as follows:

Superior Quality (minimal risk) – Loans in this category are considered to be of the highest quality. The borrower is very liquid. Overall asset quality is very good. Leverage is very low and is stable or decreasing. For consumer loans, debt to income ratio should be very low and for business loans, cash flow is continually very high relative to all demands. Earnings are always very strong, being stable or even increasing through economic swings. Multiple sources of financing exist and can be easily obtained by this borrower.

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2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

High Quality (low risk) – Loans in this category are considered to be of above average quality. The borrower is very liquid. Overall, leverage is relatively low and is stable. Earnings are very strong and stable. For consumer loans, the debt to income ratio should be low and for business loans, cash flow is more than sufficient to meet total demands. Other sources of financing are available and are readily available to this borrower.

Good Quality (normal risk) – Loans in this category are considered to be of good quality. These consumer borrowers have a history of successful credit performance and the business borrowers have successful financial performance, but could be susceptible to economic changes. Asset quality is good. The balance sheet shows decent liquidity. Overall leverage is at a normal level. Income and cash flow may fluctuate but are still sufficient to meet demands. Other sources of financing should be easily obtainable.

Acceptable Quality (increased risk) – Loans in this grade are considered to be acceptable credit risk but may require more than the normal servicing. Loans should be in this category not because they are problem credits, but because they may be higher than normal risk and the Bank needs to follow their performance more closely than others. Asset quality is marginally acceptable. Overall, leverage may fluctuate and is frequently at the upper end of the range of what is considered normal. Income and cash flow may be marginal but continue to support demands. The outlook for continued improvement is good. Access to other financing sources is limited to a few banks.

Special Mention (high risk) – A “Special Mention” loan has potential weaknesses that deserve management’s close attention. Such weaknesses could be that the borrower’s ability to repay from primary (intended) sources (i.e., income or cash flow) is marginal and is threatened by a potential weakness which, if not checked or corrected, could result in deterioration of the repayment prospects for the loan and/or the Bank being inadequately protected against the risk of principal or income loss at some future date. The borrower is highly susceptible to current economic or market conditions, which may adversely affect the borrower’s ability to repay the debt. A consumer borrower may have had a reduction of income or have an unusually high level of financial leverage. A business borrower may be experiencing adverse operating trends or operating with unusually high financial leverage, thereby increasing the risk of untimely payment. A loan classified as “Special Mention” should be transitional and temporary (6 months).

Classified Substandard – Loans with a rating of “Substandard” show that the borrower’s ability to repay is threatened by a clearly defined weakness which jeopardizes liquidation of the loan. The distinct possibility exists that the Bank will sustain some principal or income loss if the deficiencies are not corrected.

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2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

Classified Doubtful – Loans with a rating of “Doubtful” show that the borrower’s ability to repay in full, on the basis of currently existing facts, is highly questionable and improbable. Some loss of principal or income is likely; however, the total amount of such loss cannot be determined at the present time. A “Doubtful” risk grade should be temporary; therefore, when and if loss exposure is determined, the amount of loss will be charged off or the loan should be upgraded. Loans in this category shall be immediately placed on non-accrual with all payments applied to principal until such time as the potential loss exposure is eliminated.

Classified Loss – Loans classified as “Loss” are considered partially or totally uncollectible and of such little value that their continuation as bankable assets is not warranted. This classification does not mean that the loan has absolutely no recovery or salvage value, but rather, it is not practical or desirable to defer writing off this asset even though partial recovery may be affected in the future.

Loans Held-for-Sale

Loans held-for-sale consist of loans originated by the Bank’s loan department that are sold without recourse, normally within 10 working days. All of the loans are sold at face value plus any interest accrued from the date of origination. The loans are reflected at cost, which is also market value. The Bank had \$160,700 and \$1,215,250 in loans held-for-sale as of December 31, 2019 and 2018, respectively.

Premises and Equipment

Land is carried at cost. Other premises and equipment are stated at cost less accumulated depreciation. Expenditures for additions and major improvements that significantly extend the useful life of assets are capitalized. Expenditures for repairs and maintenance are charged against income when incurred.

Depreciation is provided generally by straight-line method based on the estimated useful lives of the respective assets, which generally range from 3 to 39 years.

Foreclosed Real Estate

Foreclosed real estate includes both formally foreclosed property and in-substance foreclosed property. In-substance foreclosed properties are those properties for which the Bank has taken physical possession, regardless of whether formal foreclosure proceedings have taken place.

At the time of foreclosure, foreclosed real estate is recorded at the fair value less estimated costs to sell, which becomes the property's new cost basis. Any write-downs based on the asset's fair value at date of acquisition are charged to the allowance for loan losses. Subsequent to foreclosure, valuations are periodically performed by management, and the assets are carried at the lower of carrying value amount or fair value less cost to sell. Costs incurred in maintaining other real estate and subsequent adjustments to the carrying amount of the property are included in income (loss) on other real estate. Costs incurred to complete, repair/renovate, or make the property whole are capitalized, if these costs increase the fair value of the property.

NOBLE BANCSHARES, INC. AND SUBSIDIARY
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2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

Bank-Owned Life Insurance

The Company has purchased life insurance policies on certain key employees. These policies are recorded 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 other operating income.

Deposits

Customer deposits include public funds held on deposit under the Security for Alabama Funds Enhancement Act (SAFE) Program. The SAFE Program was established by the Alabama legislature to provide protection for public funds enrolled in the SAFE Program. Under this program, financial institutions are required to collateralize public fund deposits (see Note 3).

The Bank participates in the Certificate of Deposit Account Registry Service (CDARS), which is a network of banks that offer certificates of deposit products to individual and corporate customers in such amounts that allow such deposits to qualify for Federal Deposit Insurance Corporation (FDIC) insurance coverage.

The Bank is party to an agreement with QwickRate, an internet-based certificate of deposit listing service, to utilize their program to raise institutional time deposits.

Borrowings

The Bank records Federal Home Loan Bank advances and federal funds purchased at their principal amounts. Interest expense is recognized based on the coupon rate of the obligations.

Common Stock

Common stock has voting rights that are equal to one vote per share.

Comprehensive Income

Comprehensive income or loss is generally defined as the change in equity of a business enterprise during a period from transactions and other events and circumstances from nonowner sources. It includes all changes in equity during a period except those resulting from investments by owners and distributions to owners. Other comprehensive income (loss) is comprised of items not recorded as components of net income. The accumulated balance of other comprehensive income (loss) is reported separately from retained earnings in the equity section of the statements of financial condition.

Stock Based Compensation

Pursuant to the provisions of the Amended and Restated 2005 Incentive Stock Compensation Plan (the Plan), the stockholders and the Board of Directors approved 180,000 shares of common stock as reserved for stock options, warrants, or restricted stock for various employees and directors. Note 14 summarizes the various grants of options, warrants, and restricted stock.

Major Services and Principal Markets

The Company's main line of business consists of providing banking services for its customers, most of whom are located in Calhoun County, Alabama and Jefferson County, Alabama.

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2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

Advertising

The Bank's policy is to expense advertising costs as incurred. Advertising expense was \$24,858 and \$26,213 for the years ended December 31, 2019 and 2018, respectively.

Employee Benefit Plans

The Bank has a qualified 401(k) profit-sharing plan covering substantially all employees. Eligible participating employees may elect to contribute tax-deferred contributions. Bank contributions include matching annual and discretionary amounts as determined by the Board of Directors. The 401(k) plan allows participants to invest in unrelated mutual funds.

The Bank has also provided a deferred compensation plan for certain key employees and directors. These plans are target benefit arrangements with defined contributions based on the key employee's earned salary. The amounts are unfunded and are included in other liabilities on the Bank's books. As such, the beneficiaries are general creditors of the Bank.

Bank contributions to these benefit plans are included in salaries and employee benefits (see Notes 15 and 16).

Income Taxes

The Bank and holding company filed separate federal income and State of Alabama excise tax returns for 2018. Beginning in 2018, the Bank and holding company filed a consolidated federal income tax return but will continue to file separate State of Alabama excise tax returns. These returns are filed using the accrual basis of accounting. Provisions for income taxes are based on amounts reported in the statements of income (after exclusion of nontaxable income, such as interest on state and municipal securities) and include deferred taxes on temporary differences in the recognition of income and expense for tax and financial statement purposes.

Transfers of Financial Assets

Transfers of financial assets are accounted for as sales when control over assets has been surrendered. Control over transferred assets is deemed surrendered when (1) the assets have been isolated from the Bank and put presumptively beyond the reach of the transferor and its creditors, even in bankruptcy or other receivership, (2) the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets, and (3) the Bank does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity or the ability to unilaterally cause the holder to return specific assets.

Off-Balance Sheet Financial Instruments

In the ordinary course of business, the Bank has entered into off-balance sheet financial instruments consisting of commitments to extend credit, commitments under credit card arrangements, commercial letters of credit, and standby letters of credit. Such financial instruments are recorded in the consolidated financial statements when they are funded. See Note 10 for a further discussion of these financial instruments.

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2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

The Bank has available as a source of short-term financing the purchase of federal funds from other commercial banks from available lines totaling \$12,800,000, all of which is available and unused.

The Bank also has a line of credit with the Federal Home Loan Bank of Atlanta (FHLB) of up to approximately \$66,700,750, of which all is available and unused as of December 31, 2019. The ability to utilize the remaining line is dependent on the amount of eligible collateral that is free to pledge to the FHLB. In addition, as part of the borrowing agreement, the Bank is required to purchase FHLB stock (see Note 3).

Fair Value Measurements

The Bank adopted authoritative guidance issued by the Financial Accounting Standards Board (FASB) on fair value measurements. This standard defines fair value for financial reporting purposes as the price that would be received to sell an asset or paid to transfer a liability in an orderly market transaction between market participants at the measurement date (reporting date). Fair value is based on an exit price in the principal market or most advantageous market in which the reporting entity could execute a transaction. New fair value measurements are not required, but fair value disclosures are required for financial assets or liabilities where other accounting pronouncements require or permit fair value reporting.

For each asset and liability required to be reported at fair value, management has identified the unit of account and valuation premise to be applied for purposes of measuring fair value. The unit of account is the level at which an asset or liability is aggregated or disaggregated. The valuation premise is a concept that determines whether an asset is measured on a stand-alone basis or in combination with other assets. The Bank measures its assets and liabilities on a stand-alone basis then aggregates assets and liabilities with similar characteristics for disclosure purposes.

The standard establishes a hierarchy for inputs used in measuring fair value that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that the observable inputs be used when available. Observable inputs are inputs that market participants would use in pricing the asset or liability developed based on market data obtained from sources independent of the Bank. Unobservable inputs are inputs that reflect the Bank's assumptions about the assumptions market participants would use in pricing the asset or liability developed based on the best information available in the circumstances.

The fair value guidance established three categories within a fair value hierarchy which are presented below:

Level 1 – Valuations based on quoted prices in active markets for identical assets or liabilities that the Bank has the ability to access. Since valuations are based on quoted prices that are readily and regularly available in an active market, valuation of these products does not entail a significant degree of judgment.

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2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

Level 2 – Valuations based on observable inputs, including quoted prices (other than Level 1) in active markets for similar assets or liabilities, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability, such as interest rates, yield curves, volatilities, and default rates, and inputs that are derived principally from or corroborated by observable market data.

Level 3 – Valuations based on inputs that are unobservable and significant to the overall fair value measurement.

The adoption of this authoritative guidance had no impact on the consolidated financial statements of the Bank other than the additional disclosures included in Note 17.

Subsequent Events

Management has evaluated subsequent events and their potential effects on these consolidated financial statements through the date of the independent auditors' report, which is the date the consolidated financial statements were available to be issued.

Reclassifications

Certain reclassifications have been made to the 2018 consolidated financial statements included herein to conform to the 2019 presentation. These reclassifications had no effect on the financial position, results of operations, or cash flows of the Bank.

Recently Issued Accounting Standards

In May 2014, the FASB issued ASU 2014-09 and in August 2015 issued ASU 2015-14, *Revenue from Contracts with Customers* (Topic 606), a comprehensive new revenue recognition standard that will supersede nearly all existing revenue recognition guidance under U.S. GAAP. The standard's core principle is that an entity will recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods and services. The guidance may be applied retrospectively to each prior reporting period presented or retrospectively with the cumulative effect of initial application recognized at January 1, 2019. Interest income is exempt from the ASU; therefore, the effect of the adoption of this ASU is minimal.

In January 2016, the FASB issued ASU 2016-01, *Financial Instruments – Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities*. The amendments in this ASU, among other things: a) requires equity investments (except those accounted for under the equity method of accounting, or those that result in consolidation of the investee) to be measured at fair value with changes in fair value recognized in net income; b) requires public business entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes; and c) requires separate presentation of financial assets and financial liabilities by measurement category and form of financial asset (i.e., securities or loans and receivables). The effective date of this ASU for the Bank is January 1, 2019. The adoption of this ASU did not have a material impact to the Bank.

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2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

In June 2016, the FASB issued ASU 2016-13, in November 2018 issued ASU 2018-19, in April 2019 issued ASU 2019-04, in May 2019 issued ASU 2019-05, and in November 2019 issued ASU 2019-10 and 2019-11, *Financial Instruments — Credit Losses* (Topic 326). The amendments in this ASU cover two areas: assets measured at amortized cost and available-for-sale debt securities. For assets measured at amortized cost, the amendments in this ASU 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. For available-for-sale debt securities, 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 this ASU are effective for fiscal years beginning after December 15, 2022. All entities may adopt the amendments in this ASU as early as the fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. The Bank is reviewing the impact that the adoption of this ASU may have on its financial statements.

In December 2019, the FASB issued ASU 2019-12, *Income Taxes (Topic 740): Simplifying the Accounting for Income Taxes*. The amendments of this ASU simplify the accounting for income taxes by removing certain exceptions to the general principles in Topic 740 and improve consistent application of and simplify GAAP for other areas of Topic 740 by clarifying and amending existing guidance. This ASU is effective for fiscal years beginning after January 1, 2022. The Financial Institution is reviewing the impact that the adoption of this ASU may have on its financial statements.

NOBLE BANCSHARES, INC. AND SUBSIDIARY
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3. SECURITIES

Securities Available-for-Sale

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

	<u>Amortized Cost</u>	<u>Gross Unrealized Gains</u>	<u>Gross Unrealized Losses</u>	<u>Fair Value</u>
As of December 31, 2019				
Debt securities:				
U.S. government-sponsored enterprises (GSEs)*	\$ 9,994,878	\$ -	\$ 204,955	\$ 9,789,923
State and municipal	43,548,280	479,273	489,412	43,538,141
Mortgage-backed:				
GSE residential	<u>5,505,824</u>	<u>-</u>	<u>33,577</u>	<u>5,472,247</u>
	<u>\$ 59,048,982</u>	<u>\$ 479,273</u>	<u>\$ 727,944</u>	<u>\$ 58,800,311</u>
	<u>Amortized Cost</u>	<u>Gross Unrealized Gains</u>	<u>Gross Unrealized Losses</u>	<u>Fair Value</u>
As of December 31, 2018				
Debt securities:				
U.S. government-sponsored enterprises (GSEs)*	\$ 5,024,457	\$ -	\$ 311,770	\$ 4,712,687
State and municipal	47,154,958	124,480	849,231	46,430,207
Mortgage-backed:				
GSE residential	<u>10,845,682</u>	<u>-</u>	<u>256,065</u>	<u>10,589,617</u>
	<u>\$ 63,025,097</u>	<u>\$ 124,480</u>	<u>\$ 1,417,066</u>	<u>\$ 61,732,511</u>

* Such as Federal National Mortgage Association, Federal Home Loan Mortgage Corporation, and Federal Home Loan Banks.

The Bank did not classify any investments as held-to-maturity at December 31, 2019 and 2018.

Investment securities with a carrying amount of \$13,693,863 and \$14,814,633 were pledged to secure various public funds under the SAFE Program at December 31, 2019 and 2018, respectively.

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3. SECURITIES – CONTINUED

The amortized cost and fair value of available-for-sale securities by contractual maturity at December 31, 2019, were as follows:

	<u>Amortized Cost</u>	<u>Fair Value</u>
Within one year	\$ 626,493	\$ 626,457
After one year through five years	3,921,513	3,897,772
After five years through ten years	16,736,843	16,751,532
Over ten years	<u>37,764,133</u>	<u>37,524,550</u>
	<u>\$ 59,048,982</u>	<u>\$ 58,800,311</u>

Mortgage-backed securities have been included in the maturity tables based upon the guaranteed pay-off date of each security.

The actual maturities may differ from the contractual maturities because borrowers may have the right to call or repay obligations with or without call or prepayment penalties.

For the years ended December 31, 2019 and 2018, proceeds from sales, maturities, and calls of securities available-for-sale amounted to \$41,198,012 and \$1,713,480; gross realized gains were \$760,901 and \$1,645 and gross realized losses were \$30,988 and \$870, respectively.

The following table shows the gross unrealized losses and fair value of the entity's available-for-sale securities with unrealized losses that are not deemed to be other-than-temporarily impaired, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position at December 31, 2019 and 2018.

	<u>Less Than 12 Months</u>		<u>More Than 12 Months</u>		<u>Total</u>	
	<u>Fair Value</u>	<u>Gross Unrealized Losses</u>	<u>Fair Value</u>	<u>Gross Unrealized Losses</u>	<u>Fair Value</u>	<u>Gross Unrealized Losses</u>
As of December 31, 2019						
Debt securities:						
U.S. GSEs	\$ 9,789,923	\$ 204,955	\$ -	\$ -	\$ 9,789,923	\$ 204,955
State and municipals	19,494,532	487,732	265,486	1,680	19,760,018	489,412
Mortgage-backed securities:						
GSE residential	<u>5,472,247</u>	<u>33,577</u>	<u>-</u>	<u>-</u>	<u>5,472,247</u>	<u>33,577</u>
	<u>\$ 34,756,702</u>	<u>\$ 726,264</u>	<u>\$ 265,486</u>	<u>\$ 1,680</u>	<u>\$ 35,022,188</u>	<u>\$ 727,944</u>

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3. SECURITIES – CONTINUED

	Less Than 12 Months		More Than 12 Months		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
As of December 31, 2018						
Debt securities:						
U.S. GSEs	\$ -	\$ -	\$ 4,712,687	\$ 311,770	\$ 4,712,687	\$ 311,770
State and municipals	4,657,028	40,762	26,666,750	808,469	31,323,778	849,231
Mortgage-backed securities:						
GSE residential	-	-	10,589,617	256,065	10,589,617	256,065
	<u>\$ 4,657,028</u>	<u>\$ 40,762</u>	<u>\$ 41,969,054</u>	<u>\$ 1,376,304</u>	<u>\$ 46,626,082</u>	<u>\$ 1,417,066</u>

U.S. Government-Sponsored Enterprises (GSEs)

The Bank has 10 U.S. Government-sponsored enterprise securities with unrealized losses at December 31, 2019. The unrealized losses on these investments were caused by the current interest rate environment and reflected aggregate depreciation from amortized cost of 2.09%. The expected present value of future cash flows is expected to approximate the contractual cash flows. Accordingly, it is expected that the securities would not be settled at a price less than the amortized cost of the Bank's investment.

The Bank does not consider these investments to be other-than-temporarily impaired at December 31, 2019, because the decline in market value is attributable to the current interest rate environment and not credit quality; moreover, the Bank does not intend to sell the investments, and it is not more likely than not that the Bank will be required to sell the investments before recovery of their amortized cost basis, which may be maturity.

State and Municipal

The Bank has 26 state and municipal securities with unrealized losses at December 31, 2019. The unrealized losses on these investments were caused by the current interest rate environment and reflected aggregate depreciation from amortized cost of 2.48%. The expected present value of future cash flows is expected to approximate the contractual cash flows. Accordingly, it is expected that the securities would not be settled at a price less than the amortized cost of the Bank's investment.

The Bank does not consider these investments to be other-than-temporarily impaired at December 31, 2019, because the decline in market value is attributable to the current interest rate environment and not credit quality; moreover, the Bank does not intend to sell the investments, and it is not more likely than not that the Bank will be required to sell the investments before recovery of their amortized cost basis, which may be maturity.

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3. SECURITIES – CONTINUED

Mortgage-Backed Securities: Residential GSEs

The Bank had four mortgage-backed securities with unrealized losses at December 31, 2019. The unrealized losses on these investments were caused by the current interest rate environment and reflected aggregate depreciation from amortized cost of 0.61%. The expected present value of future cash flows is expected to approximate the contractual cash flows. Accordingly, it is expected that the securities would not be settled at a price less than the amortized cost of the Bank's investment.

The Bank does not consider these investments to be other-than-temporarily impaired at December 31, 2019, because the decline in market value is attributable to the current interest rate environment and not credit quality; moreover, the Bank does not intend to sell the investments, and it is not more likely than not that the Bank will be required to sell the investments before recovery of their amortized cost basis, which may be maturity.

Other-than-Temporary Impairment

The Bank recognizes other-than-temporary impairment (OTTI) in accordance with ASC Topic 320, *Investments – Debt and Equity Securities*, which requires that the Bank assess whether it intends to sell or it is more likely than not that the Bank will be required to sell a security before recovery of its amortized cost basis less any current-period credit losses. For debt securities that are considered other-than-temporarily impaired and that the Bank does not intend to sell, and will not be required to sell prior to anticipated recovery of the amortized cost basis, the amount of the impairment is separated into the amount that is credit related (credit loss component) and the amount due to all other factors. The credit loss component is recognized in earnings and is the difference between the security's amortized cost basis and the present value of its expected future cash flows discounted at the security's effective yield. The remaining difference between the security's fair value and the present value of future expected cash flows is due to factors that are not credit related and, therefore, is not required to be recognized as a loss in the statements of income but is recognized in other comprehensive income (loss). The Bank believes that it will fully collect the carrying value of securities on which it has recorded a noncredit related impairment in other comprehensive income (loss). The Bank held no investments with an other-than-temporary impairment at December 31, 2019 and 2018.

Securities, Restrictive Investment

The aggregate carrying value of the Bank's cost-method investments totaled \$1,344,450 and \$1,266,850 at December 31, 2019 and 2018, respectively. These investments were not evaluated for impairment because (1) the Bank did not estimate the fair value of these investments in accordance with ASC Topic 825, *Financial Instruments*, and (2) the Bank did not identify any events or changes in circumstances that may have had a significant adverse effect on the fair value of these investments. As of December 31, 2019, the Bank concluded that any impairments identified were temporary with no adjustments needed.

NOBLE BANCSHARES, INC. AND SUBSIDIARY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
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3. SECURITIES – CONTINUED

The carrying amount of securities restrictive investment at December 31 is as follows:

	<u>2019</u>	<u>2018</u>
Federal Reserve Bank	\$ 578,250	\$ 578,250
First National Bankers Bank	534,200	485,600
Federal Home Loan Bank	<u>232,000</u>	<u>203,000</u>
	<u>\$ 1,344,450</u>	<u>\$ 1,266,850</u>

4. LOANS

The composition of loans by primary loan classification and by performing and impaired loan status at December 31, 2019 and 2018, is as follows:

	<u>December 31, 2019</u>		
	<u>Performing Loans</u>	<u>Impaired Loans</u>	<u>Total</u>
Commercial, financial, and agricultural	\$ 37,444,455	\$ 1,622,573	\$ 39,067,028
Real estate – construction, land, and other land	14,662,984	312,751	14,975,735
Real estate – mortgage	117,019,457	1,989,295	119,008,752
Consumer	<u>4,619,529</u>	<u>40,018</u>	<u>4,659,547</u>
Subtotal	173,746,425	3,964,637	177,711,062
Allowance for loan losses	<u>(2,299,738)</u>	<u>(1,732,072)</u>	<u>(4,031,810)</u>
Net loans	<u>\$ 171,446,687</u>	<u>\$ 2,232,565</u>	<u>\$ 173,679,252</u>

NOBLE BANCSHARES, INC. AND SUBSIDIARY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2019 AND 2018

4. LOANS – CONTINUED

	December 31, 2018		
	Performing Loans	Impaired Loans	Total
Commercial, financial, and agricultural	\$ 38,993,380	\$ 123,488	\$ 39,116,868
Real estate – construction, land, and other land	13,541,509	345,520	13,887,029
Real estate – mortgage	103,315,382	585,904	103,901,286
Consumer	4,785,678	54,287	4,839,965
Subtotal	160,635,949	1,109,199	161,745,148
Allowance for loan losses	(1,856,503)	(105,332)	(1,961,835)
Net loans	<u>\$ 158,779,446</u>	<u>\$ 1,003,867</u>	<u>\$ 159,783,313</u>

The changes in the allowance for loan losses for the years ended December 31, 2019 and 2018, are as follows:

	2019	2018
Balance at beginning of year	\$ 1,961,835	\$ 1,681,553
Loans charged off	(802,720)	(207,503)
Recoveries on loans previously charged off	33,203	70,649
Net charge-offs	(769,517)	(136,854)
Provision charged to operating expenses	2,839,492	417,136
Balance at end of year	<u>\$ 4,031,810</u>	<u>\$ 1,961,835</u>

NOBLE BANCSHARES, INC. AND SUBSIDIARY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2019 AND 2018

4. LOANS – CONTINUED

The allocation and changes in the allowance for loan losses, by loan classification, as of and for the years ended December 31, 2019 and 2018, are as follows:

	December 31, 2019					Total
	Commercial, Financial, and Agricultural	Real Estate – Construction, Land Development, and Other Land	Real Estate – Mortgage	Consumer	Unallocated	
Balance at beginning of year	\$ 372,831	\$ 157,895	\$ 1,273,639	\$ 88,926	\$ 68,544	\$ 1,961,835
Charge-offs	(312,357)	(277,152)	(130,401)	(82,810)	-	(802,720)
Recoveries	-	-	4,586	28,617	-	33,203
Net charge-offs	(312,357)	(277,152)	(125,815)	(54,193)	-	(769,517)
Provision	2,109,621	409,811	423,244	50,672	(153,856)	2,839,492
Ending balance	<u>\$ 2,170,095</u>	<u>\$ 290,554</u>	<u>\$ 1,571,068</u>	<u>\$ 85,405</u>	<u>\$ (85,312)</u>	<u>\$ 4,031,810</u>
	December 31, 2018					
	Commercial, Financial, and Agricultural	Real Estate – Construction, Land Development, and Other Land	Real Estate – Mortgage	Consumer	Unallocated	Total
Balance at beginning of year	\$ 321,729	\$ 102,581	\$ 1,205,982	\$ 51,421	\$ (160)	\$ 1,681,553
Charge-offs	(29,528)	-	(80,154)	(97,821)	-	(207,503)
Recoveries	11,000	-	24,897	34,752	-	70,649
Net charge-offs	(18,528)	-	(55,257)	(63,069)	-	(136,854)
Provision	69,630	55,314	122,914	100,574	68,704	417,136
Ending balance	<u>\$ 372,831</u>	<u>\$ 157,895</u>	<u>\$ 1,273,639</u>	<u>\$ 88,926</u>	<u>\$ 68,544</u>	<u>\$ 1,961,835</u>

NOBLE BANCSHARES, INC. AND SUBSIDIARY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2019 AND 2018

4. LOANS – CONTINUED

The following table outlines the amount of each loan classification based on internally assigned risk ratings as of December 31, 2019 and 2018:

	December 31, 2019				
	Commercial, Financial, and Agricultural	Real Estate – Construction, Land Development, and Other Land	Real Estate – Mortgage	Consumer	Total
Grade:					
Pass*	\$ 36,714,455	\$ 14,662,984	\$ 114,909,628	\$ 4,619,529	\$ 170,906,596
Pass – impaired	-	312,751	99,324	-	412,075
Special mention	430,000	-	-	-	430,000
Substandard	300,000	-	2,109,829	-	2,409,829
Substandard – impaired	1,622,573	-	1,889,971	40,018	3,552,562
Total	<u>\$ 39,067,028</u>	<u>\$ 14,975,735</u>	<u>\$ 119,008,752</u>	<u>\$ 4,659,547</u>	<u>\$ 177,711,062</u>

* Loans graded as superior quality, high quality, good quality, and acceptable quality are classified as "Pass" grade for disclosure purposes.

	December 31, 2018				
	Commercial, Financial, and Agricultural	Real Estate – Construction, Land Development, and Other Land	Real Estate – Mortgage	Consumer	Total
Grade:					
Pass*	\$ 35,741,731	\$ 13,541,509	\$ 101,061,358	\$ 4,785,678	\$ 155,130,276
Pass – impaired	-	345,520	103,605	-	449,125
Special mention	1,617,321	-	474,890	-	2,092,211
Substandard	1,634,328	-	1,779,134	-	3,413,462
Substandard – impaired	123,488	-	482,299	54,287	660,074
Total	<u>\$ 39,116,868</u>	<u>\$ 13,887,029</u>	<u>\$ 103,901,286</u>	<u>\$ 4,839,965</u>	<u>\$ 161,745,148</u>

* Loans graded as superior quality, high quality, good quality, and acceptable quality are classified as "Pass" grade for disclosure purposes.

NOBLE BANCSHARES, INC. AND SUBSIDIARY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2019 AND 2018

4. LOANS – CONTINUED

The following table details the recorded investments, unpaid principal balance, and the related allowance of impaired loans as of December 31, 2019 and 2018, and the average recorded investment of impaired loans for the years ended December 31, 2019 and 2018:

	At December 31, 2019			For the Year Ended December 31, 2019
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment
Impaired loans with no recorded allowance:				
Real estate – construction, land development, and other land	\$ 322,559	\$ 312,751	\$ -	\$ 338,196
Real estate – mortgage	1,802,634	1,796,838	-	1,977,975
Total	2,125,193	2,109,589	-	2,316,171
Impaired loans with a recorded allowance:				
Commercial, financial, and agricultural	1,693,695	1,622,573	1,622,573	1,556,631
Real estate – mortgage	196,077	192,457	69,481	203,354
Consumer	40,910	40,018	40,018	47,398
Total	1,930,682	1,855,048	1,732,072	1,807,383
Total impaired loans	<u>\$ 4,055,875</u>	<u>\$ 3,964,637</u>	<u>\$ 1,732,072</u>	<u>\$ 4,123,554</u>

NOBLE BANCSHARES, INC. AND SUBSIDIARY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2019 AND 2018

4. LOANS – CONTINUED

	At December 31, 2018			For the Year Ended December 31, 2018
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment
Impaired loans with no recorded allowance:				
Commercial, financial, and agricultural	\$ 123,488	\$ 123,488	\$ -	\$ 137,915
Real estate – construction, land development, and other land	405,695	345,520	-	368,825
Real estate – mortgage	379,497	379,497	-	391,601
Consumer	9,658	9,658	-	12,579
Total	918,338	858,163	-	910,920
Impaired loans with a recorded allowance:				
Real estate – mortgage	681,938	206,407	60,703	212,199
Consumer	57,344	44,629	44,629	48,698
Total	739,282	251,036	105,332	260,897
Total impaired loans	\$ 1,657,620	\$ 1,109,199	\$ 105,332	\$ 1,171,817

For the years ended December 31, 2019 and 2018, the interest income recognized on impaired loans was immaterial.

Past due balances and loans on nonaccrual status at December 31, 2019 and 2018, by loan classification, are as follows:

	December 31, 2019					
	Past Due 30-89 Days and Still Accruing	Past Due 90 Days or More and Still Accruing	Total Past Due and Performing	Loans on Nonaccrual Status	Current	Total Loans
Commercial, financial, and agricultural	\$ 81,680	\$ 97,239	\$ 178,919	\$ 1,622,573	\$ 37,265,536	\$ 39,067,028
Real estate – construction, land development, and other land	-	-	-	-	14,975,735	14,975,735
Real estate – mortgage	202,820	-	202,820	1,003,955	117,801,977	119,008,752
Consumer	5,584	-	5,584	40,018	4,613,945	4,659,547
Total	\$ 290,084	\$ 97,239	\$ 387,323	\$ 2,666,546	\$ 174,657,193	\$ 177,711,062

NOBLE BANCSHARES, INC. AND SUBSIDIARY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2019 AND 2018

4. LOANS – CONTINUED

	December 31, 2018					
	Past Due 30-89 Days and Still Accruing	Past Due 90 Days or More and Still Accruing	Total Past Due and Performing	Loans on Nonaccrual Status	Current	Total Loans
Commercial, financial, and agricultural	\$ 11,461	\$ -	\$ 11,461	\$ 123,488	\$ 38,981,919	\$ 39,116,868
Real estate – construction, land development, and other land	-	-	-	-	13,887,029	13,887,029
Real estate – mortgage	531,731	-	531,731	275,891	103,093,664	103,901,286
Consumer	31,484	-	31,484	-	4,808,481	4,839,965
Total	\$ 574,676	\$ -	\$ 574,676	\$ 399,379	\$ 160,771,093	\$ 161,745,148

At December 31, 2019 and 2018, there were no loans classified as nonaccrual that were not deemed to be impaired. At the date such loans were placed on nonaccrual status, the Bank reversed all previously accrued interest income against current year earnings. Had such nonaccrual loans been on accrual status, interest income would have been immaterial for the year ended December 31, 2019. Interest income is subsequently recognized to the extent cash payments are received while the loan is classified as nonaccrual, but is reviewed on a loan-by-loan basis.

The Bank has no commitments to loan additional funds to the borrowers of impaired loans.

NOBLE BANCSHARES, INC. AND SUBSIDIARY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2019 AND 2018

4. LOANS – CONTINUED

The following table details the number of TDRs by loan classification as of December 31, 2019 and 2018:

	December 31, 2019		
	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Real estate – construction, land development, and other land	1	\$ 745,188	\$ 312,751
Real estate – mortgage	2	356,770	291,782
Consumer	1	83,535	36,629
Total	4	\$ 1,185,493	\$ 641,162

	December 31, 2018		
	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Real estate – construction, land development, and other land	1	\$ 745,188	\$ 345,520
Real estate – mortgage	2	356,770	310,013
Consumer	1	83,535	44,629
Total	4	\$ 1,185,493	\$ 700,162

Impaired loans also include loans that the Bank may elect to formally restructure due to the weakening credit status of a borrower such that the restructuring may facilitate a repayment plan that minimizes the potential losses, if any, that the Bank may have to otherwise incur. These loans are classified as impaired loans, and, if on nonaccrual status as of the date of restructuring, the loans are included in the nonperforming loan balances noted above. Not included in nonperforming loans are loans that have been restructured that were performing as of the restructure date.

There were no troubled debt restructurings that subsequently defaulted for the year ended December 31, 2019.

NOBLE BANCSHARES, INC. AND SUBSIDIARY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2019 AND 2018

4. LOANS – CONTINUED

The following table details the number of troubled debt restructurings by loan classification that have subsequently defaulted for the year ended December 31, 2018:

	December 31, 2018	
	Number of Contracts	Recorded Investment
Real estate – mortgage	1	\$ 162,648

The Bank has pledged eligible one to four family real estate mortgage loans, commercial mortgage loans, multifamily mortgage loans, and investments as collateral to the Federal Home Loan Bank of Atlanta to secure a line of credit in the amount of \$66,700,750. At December 31, 2019 and 2018, there was not an outstanding balance on the line of credit. See Note 7.

Certain directors, executive officers, and principal stockholders, including their immediate families and associates, were loan customers of the Bank during 2019 and 2018. A summary of activity and amounts outstanding as of December 31 is as follows:

	2019	2018
Balance at beginning of year	\$ 3,332,431	\$ 1,907,421
New loans or advances	18,739,139	24,540,541
Principal repayments	(20,249,991)	(23,115,532)
Balance at end of year	\$ 1,821,579	\$ 3,332,430

NOBLE BANCSHARES, INC. AND SUBSIDIARY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2019 AND 2018

5. PREMISES AND EQUIPMENT

Major classifications of premises and equipment at December 31 are summarized below:

	2019	2018
Building and improvements	\$ 6,596,590	\$ 6,515,440
Equipment	1,436,770	1,297,115
Furniture and fixtures	708,337	623,906
Computer software	185,161	158,294
Leasehold improvements	346,108	365,284
	9,272,966	8,960,039
Less accumulated depreciation	3,856,257	3,483,370
	5,416,709	5,476,669
Land	1,483,997	1,483,997
Construction-in-progress	21,889	-
Premises and equipment, net	<u>\$ 6,922,595</u>	<u>\$ 6,960,666</u>

The provision for depreciation charged to occupancy and equipment expense was \$424,791 and \$377,626 for the years ended December 31, 2019 and 2018, respectively.

6. DEPOSITS

The aggregate amount of deposits from executive officers, directors, and principal stockholders was \$19,092,703 and \$15,891,874 at December 31, 2019 and 2018, respectively.

The Bank had \$32,289,721 and \$27,474,592 of time deposits outstanding greater than the Federal Deposit Insurance Corporation (FDIC) insurance limit of \$250,000 at December 31, 2019 and 2018.

Demand deposit overdrafts reclassified as loan balances amounted to \$156,413 and \$211,046 at December 31, 2019 and 2018, respectively.

NOBLE BANCSHARES, INC. AND SUBSIDIARY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2019 AND 2018

6. DEPOSITS – CONTINUED

The maturity schedule for all time deposits as of December 31, 2019, over the next five years and in the aggregate is as follows:

Years Ending December 31,	
2020	\$ 46,105,825
2021	7,052,408
2022	1,922,179
2023	1,348,997
2024	<u>5,465,378</u>
	<u>\$ 61,894,787</u>

7. BORROWINGS

Borrowings at December 31 consist of the following:

	2019	2018
Note payable to a financial institution with a variable interest rate of prime as published by the Wall Street Journal, which was 4.75% as of December 31, 2019, due in quarterly interest installments and annual principal payments of \$555,556 will begin in June 2020, maturing June 2028, collateralized by Bank stock.	\$ 3,500,000	\$ 3,500,000
	<u>\$ 3,500,000</u>	<u>\$ 3,500,000</u>

The maturity schedule for all borrowings as of December 31, 2019, is as follows:

Years Ending December 31,	
2020	\$ -
2021	555,556
2022	555,556
2023	555,556
2024	555,556
Thereafter	<u>1,277,776</u>
	<u>\$ 3,500,000</u>

NOBLE BANCSHARES, INC. AND SUBSIDIARY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2019 AND 2018

8. OPERATING LEASES

Land

The bank renewed the Alexandria, Alabama branch lease for an additional five-year period. The lease expires in 2021. The lease requires the Bank to pay maintenance, insurance, and property taxes.

The Bank renewed a two-year, noncancelable operating lease agreement in March 2016 for the Piedmont, Alabama branch. The lease expires in 2018 and provides a one-year renewal option, which the Bank exercised. The lease requires the Bank to pay maintenance and insurance. This lease expired in 2019.

The Bank entered into a long-term, noncancelable operating lease agreement in 2015 for the Birmingham, Alabama branch. The lease expires in 2022 and provides for renewal options of three consecutive five-year periods. The lease requires the Bank to pay maintenance, insurance, and property taxes.

Lease expense totaled \$141,321 and \$152,674 for the years ended December 31, 2019 and 2018, respectively.

The following is a schedule by year of future minimum rental payments required under the operating lease agreements:

Year Ending December 31,	
2020	\$ 139,216
2021	106,953
2022	55,939
2023	-
Thereafter	-
	<hr/>
	\$ 302,108
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NOBLE BANCSHARES, INC. AND SUBSIDIARY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2019 AND 2018

9. INCOME TAX PROVISION

The components of income tax expense for the years ended December 31, 2019 and 2018, were as follows:

	<u>2019</u>	<u>2018</u>
Current:		
Federal	\$ 450,436	\$ 435,808
State	<u>115,999</u>	<u>81,599</u>
	566,435	517,407
Deferred:		
Federal	<u>(419,932)</u>	<u>(45,081)</u>
	<u>\$ 146,503</u>	<u>\$ 472,326</u>

The provision for federal income taxes differs from that computed by applying the federal statutory rates to income before federal income tax expense, as indicated in the following analysis:

	<u>2019</u>	<u>2018</u>
Federal statutory income tax at 21%	\$ 267,412	\$ 634,990
Tax-exempt interest	(176,141)	(196,575)
State income tax, net of federal benefit	91,639	64,462
Other temporary or permanent differences	<u>(36,408)</u>	<u>(30,551)</u>
	<u>\$ 146,503</u>	<u>\$ 472,326</u>

NOBLE BANCSHARES, INC. AND SUBSIDIARY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2019 AND 2018

9. INCOME TAX PROVISION – CONTINUED

A cumulative net deferred tax asset is included in other assets. The components of the net deferred tax assets are as follows:

	<u>2019</u>	<u>2018</u>
Differences in accounting for loan losses, less valuation allowance	\$ 846,680	\$ 411,985
Differences in depreciation methods	(174,652)	(161,548)
Differences in unrealized gains and losses on investments	52,221	271,443
Differences in stock options and warrants	7,509	1,487
Difference in deferred compensation	117,859	97,214
Other differences	<u>7,922</u>	<u>28,739</u>
	<u>\$ 857,539</u>	<u>\$ 649,320</u>
Deferred tax assets	\$ 1,032,191	\$ 810,868
Deferred tax liabilities	<u>(174,652)</u>	<u>(161,548)</u>
	<u>\$ 857,539</u>	<u>\$ 649,320</u>

Temporary differences giving rise to the deferred tax asset consist primarily of differences in the bad debt deduction for tax purposes and financial reporting purposes, differences in depreciation for tax purposes and financial reporting purposes, and the difference in unrealized gains and losses on investments.

10. FINANCIAL INSTRUMENTS WITH OFF-BALANCE SHEET RISK

The Bank is a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers and to reduce its own exposure to fluctuations in interest rates. These financial instruments include commitments to extend credit and standby letters of credit. Those instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amounts recognized in the consolidated statements of financial condition.

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

NOBLE BANCSHARES, INC. AND SUBSIDIARY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2019 AND 2018

10. FINANCIAL INSTRUMENTS WITH OFF-BALANCE SHEET RISK – CONTINUED

Unless noted otherwise, the Bank does not require collateral or other security to support financial instruments with credit risk. The approximate outstanding notional amount of off-balance sheet risks at December 31, 2019 and 2018, is as follows:

	<u>2019</u>	<u>2018</u>
Unused lines of credit	\$ 45,879,000	\$ 34,543,000
Standby letters of credit	<u>1,085,000</u>	<u>50,000</u>
	<u>\$ 46,964,000</u>	<u>\$ 34,593,000</u>

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements.

Performance and financial letters of credit are conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in loan facilities extended to customers.

11. CONCENTRATION OF CREDIT RISK

Most of the Bank's deposit and lending activities occur with customers located within Calhoun, Jefferson, and Shelby Counties in Alabama. The Bank grants commercial, residential, and consumer loans primarily to customers in central and east Alabama. The concentrations of loans by type are set forth in Note 4.

12. RESTRICTIONS ON DIVIDENDS

The Bank is subject to the dividend restrictions set forth by the State Banking Department. Under such restrictions, the Bank may not, without the prior approval of the State Banking Department, declare dividends in excess of the sum of the current year's earnings plus the net earnings from the prior two years. For the year ending December 31, 2020, the Bank can declare dividends, without regulatory approval, of approximately \$4,783,000 plus an additional amount equal to its net profits for 2020. However, restrictions exist related to the maintenance of adequate capital and, as such, may further restrict the amounts of allowable dividends which can be paid.

NOBLE BANCSHARES, INC. AND SUBSIDIARY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2019 AND 2018

13. REGULATORY CAPITAL

The Company and Bank is subject to various regulatory capital requirements administered by state and federal banking agencies. Failure to meet the minimum regulatory capital requirements can initiate certain mandatory and possible additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the consolidated financial statements. Under the regulatory capital adequacy guidelines and the regulatory framework for prompt corrective action, the Company and its subsidiary bank must meet specific capital guidelines involving 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 under the prompt corrective action guidelines are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors. Prompt corrective action provisions are not applicable to bank holding companies. Quantitative measures established by regulation to ensure capital adequacy require the Company and the Bank to maintain minimum amounts and ratios of total risk-based capital, common equity Tier 1 to risk-weighted assets, Tier 1 capital to risk-weighted assets, and Tier 1 capital to adjusted total assets (as defined by regulations). The Bank will have to maintain minimum total risk-based, common equity Tier 1, Tier 1 risk-based, and Tier 1 leverage ratios as set forth by the regulators to meet the regulatory capital requirements. Management believes, as of December 31, 2019 and 2018, that the Bank met all the capital adequacy requirements to which it was subject.

In July 2013, the banking regulators (or FDIC) published final rules establishing a new comprehensive capital framework for U.S. banking organizations (the final rules). The final rules implement the Basel Committee of Banking Supervision's December 2010 framework, known as Basel III, as well as certain provisions of the Dodd-Frank Act. The final rules, which define the components of capital and also address risk weights, became effective on January 1, 2015. The final rules include: a new capital ratio designated as common equity Tier 1 ratio, which is a tighter definition of Tier 1 capital (banks must hold 4.5% by January 2015 and then a further 2.5% capital conservation buffer, totaling 7%, that is implemented annually through January 2019); an increase in Tier 1 capital ratio from 4% to 6%; a framework for countercyclical buffers; adjustments to prompt corrective action thresholds; and short- and medium-term quantitative liquidity ratios, and establishes criteria that instruments must meet in order to be considered regulatory capital.

NOBLE BANCSHARES, INC. AND SUBSIDIARY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2019 AND 2018

13. REGULATORY CAPITAL – CONTINUED

The Bank's capital amounts and ratios under the new capital guidance are as follows (dollars in thousands):

	Actual		For Capital Adequacy Purposes		To Be Well-Capitalized Under the Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2019						
Total risk-based capital						
Consolidated	\$ 19,563	9.496%	\$ 21,631	10.500%	N/A	N/A
Bank	29,093	14.152%	21,586	10.500%	20,558	10.000%
Common equity Tier 1						
Consolidated	23,595	11.453%	14,421	7.000%	N/A	N/A
Bank	26,506	12.893%	14,391	7.000%	13,363	6.500%
Tier 1 risk-based capital						
Consolidated	23,595	11.453%	17,511	8.500%	N/A	N/A
Bank	26,506	12.893%	17,474	8.500%	16,446	8.000%
Tier 1 leverage						
Consolidated	23,595	8.809%	10,714	4.000%	N/A	N/A
Bank	26,506	9.907%	10,701	4.000%	13,377	5.000%
As of December 31, 2018						
Total risk-based capital						
Consolidated	\$ 21,334	10.885%	\$ 19,355	9.875%	N/A	N/A
Bank	28,389	14.500%	19,334	9.875%	19,579	10.000%
Common equity Tier 1						
Consolidated	23,296	11.886%	12,495	6.375%	N/A	N/A
Bank	26,427	13.498%	12,481	6.375%	12,726	6.500%
Tier 1 risk-based capital						
Consolidated	23,296	11.886%	15,435	7.875%	N/A	N/A
Bank	26,427	13.498%	15,418	7.875%	15,663	8.000%
Tier 1 leverage						
Consolidated	23,296	9.027%	10,323	4.000%	N/A	N/A
Bank	26,427	10.245%	10,318	4.000%	12,898	5.000%

NOBLE BANCSHARES, INC. AND SUBSIDIARY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
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14. STOCK-BASED COMPENSATION

On April 18, 2006, the stockholders and directors approved and adopted the Plan, a stock-based compensation plan for key employees and directors. The purpose of the Plan is to enhance stockholder investment by attracting, retaining, and motivating key employees and directors of the Bank and to align the interests of management with those of stockholders.

The weighted-average estimated fair value of the warrants and options was determined using the Black-Scholes option-pricing model, which values options based on the stock price at the grant date, the expected life of the option, the estimated volatility of the stock, the expected dividend payments, and the risk-free interest rate over the expected life of the option.

The Black-Scholes option valuation model was developed for estimating the fair value of traded options that have no vesting restrictions and are fully transferable. Because option valuation models require the use of subjective assumptions, changes in these assumptions can materially affect the fair value of the options and, since the Bank's options do not have the characteristics of traded options, the option valuation models do not necessarily provide a reliable measure of the fair value of its options.

Compensation expense recorded for the following plans totaled \$28,675 and \$0 for the years ended December 31, 2019 and 2018, respectively.

Stock Option Agreements - 2008

Stock options may be granted to certain Bank officers and employees. The maximum number of options that can be issued is 65,500. In 2008, the Board of Directors approved the issuance of stock options for five Bank officers/managers. Each of the five employees would receive an option for 500 shares of stock at a strike price of \$15. The Board of Directors ratified the granting of these options on February 17, 2009. The total expense over the five-year vesting period will be \$11,804.

The weighted-average estimated fair value of stock options granted during 2008 was \$4.7218 per share.

The assumptions used in the Black-Scholes model were as follows for stock options granted in 2008:

Risk-free interest rate	2.85%
Expected volatility of common stock	15%
Dividend yield	0%
Expected life of options	10 years

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14. STOCK-BASED COMPENSATION – CONTINUED

	Number of Shares	Weighted- Average Exercise Price
Options outstanding at December 31, 2018	1,500	\$ 22,500
Granted	-	-
Exercised	(1,500)	(22,500)
Forfeited	-	-
	-	\$ -
Options outstanding at December 31, 2019	-	\$ -
Options exercisable at December 31, 2019	-	\$ -
Remaining contractual life		0 years

Stock Option Agreements - 2014

In 2014, the Board of Directors approved the issuance of stock options to one Bank officer/manager. The employee received an option for 10,000 shares of stock at a strike price of \$12. The total expense over the five-year vesting period will be \$36,447.

The weighted-average estimated fair value of stock options granted during 2014 was \$3.6447 per share.

The assumptions used in the Black-Scholes model were as follows for stock options granted in 2008:

Risk-free interest rate	2.59%
Expected volatility of common stock	15%
Dividend yield	0%
Expected life of options	10 years

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14. STOCK-BASED COMPENSATION – CONTINUED

	Number of Shares	Weighted- Average Exercise Price
Options outstanding at December 31, 2018	10,000	\$ 120,000
Granted	-	-
Exercised	-	-
Forfeited	-	-
Options outstanding at December 31, 2019	<u>10,000</u>	<u>\$ 120,000</u>
Options exercisable at December 31, 2019	<u>10,000</u>	<u>\$ 120,000</u>
Remaining contractual life		5.5 years

15. EMPLOYEE BENEFIT PLAN

On November 1, 2005, the Bank adopted the Noble Bank and Trust 401(k) Profit Sharing Plan (401(k)) to provide eligible participants with retirement benefits. This 401(k) is a safe harbor 401(k) plan and the Bank will contribute a matching portion of employee contributions up to a maximum of 5.0% of compensation.

Profit-sharing contributions to the 401(k) are made at the discretion of the employer. The 401(k) covers substantially all employees who meet certain age and length of service requirements. The employees are not required to contribute to participate in the profit-sharing contributions. Contributions charged to operations for the years ended December 31, 2019 and 2018, were \$184,998 and \$137,010, respectively.

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16. POSTRETIREMENT BENEFITS

The Bank has also entered into nonqualified deferred compensation agreements (the Agreements) covering certain executive officers. The Agreements provide for payments of scheduled benefits to the participants or their beneficiaries for a period between 7 to 13 years following specified retirement dates (Full Benefit Dates). The Full Benefit Dates range from year 2022 through 2036 and reflect the participant having reached age 65. The Agreements provide for defined retirement benefits (Full Retirement Benefits) upon the fulfillment of certain conditions related primarily to continued length of service. Reduced retirement benefits (Limited Retirement Benefits) are also scheduled in the Agreements should separation of service occur prior to the Full Benefit Date, under certain conditions. The scheduled Limited Retirement Benefits reflect annual increases until reaching the Full Retirement Benefits on the Full Benefit Date. The Agreements provide that each annual increase is subject to annual approval by, and at the discretion of, the Bank's Board of Directors, thereby potentially reducing the scheduled Full Retirement Benefits and the Limited Retirement Benefits. The Agreements also provide for acceleration of the length of service requirement to receive the Full Retirement Benefits upon change of control (as defined in the Agreements) and acceleration of both the Full Retirement Benefits and the Full Benefit Date as a result of death or disability (as defined). The present value of the estimated liability under the Agreements is being accrued over the expected remaining years of service.

The aggregate benefit cost expected to be accrued for the year ending December 31, 2020, is \$96,995.

The measurement date for the agreement is December 31 of each year. A weighted average assumed discount rate of 5.50% was used in calculating the accumulated benefit obligation. The agreement is not considered a pay-related plan, and there are no plan assets on which to compute long-term rates of return. Since there are no plan assets, the agreement is underfunded by the total amount of the benefit obligation liability. Furthermore, the Bank plans on funding the required payments through the continuing operations of the Bank.

The present value of the agreement's accumulated benefit obligation amounted to \$561,233 and \$462,922 at December 31, 2019 and 2018, respectively. The benefit obligation expense for the years ended December 31, 2019 and 2018, was \$115,355 and \$103,203, respectively.

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16. POSTRETIREMENT BENEFITS – CONTINUED

Expected benefit payments for the deferred compensation plan for the 10-year period following December 31, 2019, are as follows:

Years Ending December 31,	
2020	\$ -
2021	-
2022	25,000
2023	60,000
2024	60,000
2025-2029	<u>302,500</u>
	<u>\$ 447,500</u>

17. FAIR VALUE OF FINANCIAL INSTRUMENTS

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

Cash Equivalents and Short-Term Investments – For those short-term instruments, the carrying amount is a reasonable estimate of fair value.

Securities – For securities held-to-maturity, fair values are based on quoted market prices or dealer quotes. For other investments, fair value is estimated to be approximately the carrying amount.

Loans – For certain homogeneous categories of loans, such as some residential mortgage, credit card receivables, and other consumer loans, fair value is estimated using the quoted market prices for securities backed by similar loans, adjusted for differences in loan characteristics. The fair value of other types of loans is estimated by discounting the future cash flows using the current rates at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturities.

Loans held-for-sale – For these short-term investments, the carrying amount is a reasonable estimate of fair value.

Accrued Interest Receivable and Payable – The carrying amount of accrued interest receivable and payable approximates its fair value.

Deposits – The fair value of demand deposits, savings accounts, and certain money market deposits is the amount payable on demand at the reporting date. The fair value of fixed-maturity certificates of deposit is estimated using the rates currently offered for deposits of similar remaining maturities.

NOBLE BANCSHARES, INC. AND SUBSIDIARY
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
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17. FAIR VALUE OF FINANCIAL INSTRUMENTS – CONTINUED

Borrowings – The fair value of borrowings, including federal funds purchased, is estimated to be approximately the same as the carrying value.

Commitments to Extend Credit, Standby Letters of Credit, and Financial Guarantees Written – The fair value of commitments, letters of credit, and financial guarantees is estimated to be approximately the fees charged for these arrangements.

The estimated fair values of the Bank's financial instruments as of December 31, 2019 and 2018, are as follows:

	2019		2018	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Financial assets:				
Cash and cash equivalents	\$ 17,419,314	\$ 17,419,314	\$ 18,389,406	\$ 18,389,406
Securities available-for-sale	58,800,311	58,800,311	61,732,511	61,732,511
Restrictive equity investments	1,344,450	1,344,450	1,266,850	1,266,850
Investments in annuities	1,724,693	1,724,693	1,724,693	1,724,693
Loans, net	173,679,252	173,773,876	159,783,313	158,880,491
Loans held-for-sale	160,700	160,700	1,215,250	1,215,250
Accrued interest payable	987,787	987,787	1,069,561	1,069,561
Financial liabilities:				
Deposits	239,891,606	224,382,512	231,074,043	203,470,024
Borrowings	3,500,000	3,500,000	3,500,000	3,500,000
Accrued interest payable	266,171	266,171	213,343	213,343
Unrecognized financial instruments:				
Commitments to extend credit	45,879,000	45,879	34,543,000	34,543
Standby letters of credit	1,085,000	1,085	50,000	50

The Bank's assets and liabilities recorded at fair value have been categorized based upon a fair value hierarchy in accordance with FASB ASC Topic 820. See Note 1.

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17. FAIR VALUE OF FINANCIAL INSTRUMENTS – CONTINUED

Items Measured at Fair Value on a Recurring Basis

The following fair value hierarchy table presents information about the Bank's assets and liabilities measured at fair value on a recurring basis as of December 31, 2019 and 2018:

	December 31, 2019			
	Fair Value	Fair Value Measurement at Report Date Using		
		Quoted Prices in Active Markets Level 1	Significant Other Observable Inputs Level 2	Significant Unobservable Inputs Level 3
Debt securities:				
U.S. GSEs	\$ 9,789,923	\$ -	\$ 9,789,923	\$ -
State and municipals	43,538,141	-	43,538,141	-
Mortgage-backed:				
GSE residential	5,472,247	-	5,472,247	-
	<u>\$ 58,800,311</u>	<u>\$ -</u>	<u>\$ 58,800,311</u>	<u>\$ -</u>
	December 31, 2018			
	Fair Value	Fair Value Measurement at Report Date Using		
		Quoted Prices in Active Markets Level 1	Significant Other Observable Inputs Level 2	Significant Unobservable Inputs Level 3
Debt securities:				
U.S. GSEs	\$ 4,712,687	\$ -	\$ 4,712,687	\$ -
State and municipals	46,430,207	-	46,430,207	-
Mortgage-backed:				
GSE residential	10,589,617	-	10,589,617	-
	<u>\$ 61,732,511</u>	<u>\$ -</u>	<u>\$ 61,732,511</u>	<u>\$ -</u>

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17. FAIR VALUE OF FINANCIAL INSTRUMENTS – CONTINUED

The valuation techniques used to measure fair value for the items in the table above are as follows:

Securities available-for-sale – Where quoted prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. If quoted market prices are not available, fair values are estimated using pricing models and discounted cash flows that consider standard input factors, such as observable market data, benchmark yields, interest rate volatilities, broker/dealer quotes, and credit spreads. Examples of such instruments, which would generally be classified within Level 2 of the valuation hierarchy, include GSE obligations, corporate bonds, and other securities. Mortgage-backed securities are included in Level 2 if observable inputs are available. In certain cases where there is limited activity or less transparency around inputs to the valuation, the securities are classified in Level 3.

Items Measured at Fair Value on a Nonrecurring Basis

The following fair value hierarchy table presents information about the Bank’s assets and liabilities measured at fair value on a nonrecurring basis as of December 31, 2019 and 2018:

December 31, 2019					
Fair Value Measurement at Report Date Using					
Fair Value	Quoted Prices in Active Markets Level 1	Significant Other Observable Inputs Level 2	Significant Unobservable Inputs Level 3		
Impaired loans	\$ 2,232,565	\$ -	\$ -	\$ 2,232,565	
Foreclosed real estate	234,343	-	-	234,343	
	<u>\$ 2,466,908</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 2,466,908</u>	

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17. FAIR VALUE OF FINANCIAL INSTRUMENTS – CONTINUED

	December 31, 2018			
	Fair Value	Fair Value Measurement at Report Date Using		
		Quoted Prices in Active Markets Level 1	Significant Other Observable Inputs Level 2	Significant Unobservable Inputs Level 3
Impaired loans	\$ 1,003,867	\$ -	\$ -	\$ 1,003,867
Foreclosed real estate	187,000	-	-	187,000
	<u>\$ 1,190,867</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 1,190,867</u>

The valuation techniques used to measure fair value for the items in the table above are as follows:

Impaired Loans – Nonrecurring fair value adjustments to loans reflect full or partial write-downs that are based on the loan’s observable market price or current appraised value of the collateral in accordance with FASB ASC Section 310-10-35, *Receivables, Subsequent Measurement, Loan Impairment*. Loans subjected to nonrecurring fair value adjustments based on the current appraised value of the collateral may be classified as Level 2 or Level 3 depending on the type of asset and the inputs to the valuation. When appraisals are used to determine impairment, and these appraisals require significant adjustments to market-based valuation inputs or apply an income approach based on unobservable cash flows to measure fair value, the related loans subjected to nonrecurring fair value adjustments are typically classified as Level 3 due to the fact that Level 3 inputs are significant to the fair value measurement.

Foreclosed Real Estate – Nonrecurring fair value adjustments to foreclosed real estate reflect full or partial write-downs that are based on the real estate’s observable market price or current appraised value of the collateral.

18. SUBSEQUENT EVENTS

The outbreak of the novel coronavirus has adversely impacted global commercial activity and contributed to significant declines and volatility in financial markets. The coronavirus pandemic and government responses are creating disruption in global supply chains and adversely impacting many industries. The outbreak could have a continued material adverse impact on economic and market conditions and trigger a period of global economic slowdown. The rapid development and fluidity of this situation precludes any prediction as to the ultimate material adverse impact of the novel coronavirus. Nevertheless, the novel coronavirus presents material uncertainty and risk with respect to the Company, its performance, and its financial results.

NOBLE BANCSHARES, INC. AND SUBSIDIARY
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19. CONDENSED PARENT COMPANY INFORMATION

Statements of Financial Condition at December 31:

ASSETS

	2019	2018
CASH AND DUE FROM BANKS – eliminated upon consolidation	\$ 428,606	\$ 211,799
INVESTMENT IN SUBSIDIARY (equity method) – eliminated upon consolidation	26,308,673	25,405,833
TOTAL ASSETS	\$ 26,737,279	\$ 25,617,632

LIABILITIES AND SHAREHOLDERS' EQUITY

BORROWINGS	\$ 3,500,000	\$ 3,500,000
ACCRUED INTEREST ON BORROWINGS	1,847	2,139
OTHER LIABILITIES	9,350	3,974
Total liabilities	3,511,197	3,506,113
Total shareholders' equity	23,226,082	22,111,519
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	\$ 26,737,279	\$ 25,617,632

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19. CONDENSED PARENT COMPANY INFORMATION – CONTINUED

Statements of Income for the Years Ended December 31:

	<u>2019</u>	<u>2018</u>
INCOME		
Dividends	\$ 1,265,262	\$ 1,073,149
Total income	<u>1,265,262</u>	<u>1,073,149</u>
EXPENSES		
Interest	187,663	95,715
License, taxes, and fees	182	509
Miscellaneous	1	-
Total expenses	<u>187,846</u>	<u>96,224</u>
INCOME (LOSS) BEFORE EQUITY IN UNDISTRIBUTED EARNINGS OF SUBSIDIARY	1,077,416	976,925
EQUITY IN UNDISTRIBUTED EARNINGS OF SUBSIDIARY	<u>49,472</u>	<u>1,574,515</u>
NET INCOME	<u>\$ 1,126,888</u>	<u>\$ 2,551,440</u>

NOBLE BANCSHARES, INC. AND SUBSIDIARY
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19. CONDENSED PARENT COMPANY INFORMATION – CONTINUED

Statements of Cash Flows for the Years Ended December 31:

	2019	2018
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	\$ 1,126,888	\$ 2,551,440
Adjustments to reconcile net income to net cash provided by operating activities:		
Equity in undistributed earnings of subsidiaries	(49,472)	(1,574,515)
Other, net	5,084	6,113
	1,082,500	983,038
CASH FLOWS FROM INVESTING ACTIVITIES		
Capital injection in subsidiary	-	(3,500,000)
	-	(3,500,000)
Net cash used in investing activities		
CASH FLOWS FROM FINANCING ACTIVITIES		
Change in borrowings	-	3,500,000
Cash dividends	(659,188)	(585,944)
Change in subsidiary payable	-	(234,801)
Treasury stock purchased	(206,505)	-
	(865,693)	2,679,255
Net cash provided by (used in) financing activities		
NET INCREASE IN CASH AND CASH EQUIVALENTS	216,807	162,293
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	211,799	49,506
CASH AND CASH EQUIVALENTS AT END OF YEAR	\$ 428,606	\$ 211,799