Board of Governors of the Federal Reserve System

Annual Report of Holding Companies—FR Y-6

Report at the close of business as of the end of fiscal year

This Report is required by law: Section 5(c)(1)(A) of the Bank Holding Company Act (12 U.S.C. § 1844(c)(1)(A)); sections 8(a) and 13(a) of the International Banking Act (12 U.S.C. §§ 3106(a) and 3108(a)); sections 11(a)(1), 25, and 25A of the Federal Reserve Act (12 U.S.C. §§ 248(a)(1), 602, and 611a); and sections 113, 165, 312, 618, and 809 of the Dodd-Frank Act (12 U.S.C. §§ 5361, 5365, 5412, 1850a(c)(1), and 5468(b)(1)). Return to the appropriate Federal Reserve Bank the original and the number of copies specified.

This report form is to be filed by all top-tier bank holding companies, top-tier savings and loan holding companies, and U.S. intermediate holding companies organized under U.S. law, and by any foreign banking organization that does not meet the requirements of and is not treated as a qualifying foreign banking organization under Section 211.23 of Regulation K (12 C.F.R. § 211.23). (See page one of the general instructions for more detail of who must file.) The Federal Reserve may not conduct or sponsor, and an organization (or a person) is not required to respond to, an information collection unless it displays a currently valid OMB control number.

NOTE: The *Annual Report of Holding Companies* must be signed by one director of the top-tier holding company. This individual should also be a senior official of the top-tier holding company. In the event that the top-tier holding company does not have an individual who is a senior official and is also a director, the chairman of the board must sign the report. If the holding company is an ESOP/ESOT formed as a corporation or is an LLC, see the General Instructions for the authorized individual who must sign the report.

I, N. Richard Kalikow
Name of the Holding Company Director and Official

Managing Member
Title of the Holding Company Director and Official

attest that the *Annual Report of Holding Companies* (including the supporting attachments) for this report date has been prepared in conformance with the instructions issued by the Federal Reserve System and are true and correct to the best of my knowledge and belief.

With respect to information regarding individuals contained in this report, the Reporter certifies that it has the authority to provide this information to the Federal Reserve. The Reporter also certifies that it has the authority, on behalf of each individual, to consent or object to public release of information regarding that individual. The Federal Reserve may assume, in the absence of a request for confidential treatment submitted in accordance with the Board's "Rules Regarding Availability of Information," 12 C.F.R. Part 261, that the Reporter and individual consent to public release of all details in the report concerning that individual.

Signature of Holding Company Director and Official

Date of Signature

Date of Report (top-tier holding company's fiscal year-end):
December 31, 2019
Month / Day / Year

no LEI
Reporter's Legal Entity Identifier (LEI) (20-Character LEI Code)

Reporter's Name, Street, and Mailing Address

Max Bancorp, LLC
Legal Title of Holding Company

1020 Highway 17 North
(Mailing Address of the Holding Company) Street / P.O. Box

North Myrtle Beach	SC	29582
City	State	Zip Code

Physical Location (if different from mailing address)

Person to whom questions about this report should be directed:

Wess Brewer	CFO
Name	Title

843-280-2265
Area Code / Phone Number / Extension

843-280-9923
Area Code / FAX Number

wbrewer@sandhillsbank.com
E-mail Address

N/A
Address (URL) for the Holding Company's web page

For holding companies not registered with the SEC–
Indicate status of Annual Report to Shareholders:

- ☐ is included with the FR Y-6 report
- ☐ will be sent under separate cover
- ☒ is not prepared

For Federal Reserve Bank Use Only

RSSD ID
C.I.

Is confidential treatment requested for any portion of this report submission? (0=No, 1=Yes) 0

In accordance with the General Instructions for this report (check only one),

1. a letter justifying this request is being provided along with the report ☐
2. a letter justifying this request has been provided separately ... ☐

NOTE: Information for which confidential treatment is being requested must be provided separately and labeled as "confidential."

For Use By Tiered Holding Companies

Top-tiered holding companies must list the names, mailing address, and physical locations of each of their subsidiary holding companies below.

Sandhills Holding Company, Inc.
Legal Title of Subsidiary Holding Company

1020 Highway 17 North
(Mailing Address of the Subsidiary Holding Company) Street / P.O. Box

North Myrtle Beach	SC	29582
City	State	Zip Code

Physical Location (if different from mailing address)

Legal Title of Subsidiary Holding Company

(Mailing Address of the Subsidiary Holding Company) Street / P.O. Box

City | State | Zip Code

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City | State | Zip Code

Physical Location (if different from mailing address)

Max Bancorp, LLC

Responses for Annual Report of Bank Holding Companies – FRY-6
Period Ending December 31, 2019

Report Item 1: No annual report is prepared for shareholders.
Audited financials for Sandhills Holding Company, Inc. are included.

Report Item 2a: Organization Chart

Max Bancorp, LLC
North Myrtle Beach, SC USA
Incorporated in DE
No LEI

Max Bancorp, LLC owns 94% of stock in the following:

Sandhills Holding Company, Inc.
North Myrtle Beach, SC USA
Incorporated in SC
No LEI

Sandhills Holding Company, Inc. owns 100% of stock in the following:

Sandhills Bank
North Myrtle Beach, SC USA
Incorporated in SC
LEI 549300LYOOWYZPR8M567

2b: Domestic Branch Listing – Confirmed and sent by email 3/17/2020 to Phyllis.Strum@rich.frb.org; also uploaded to Reporting Central in this packet.

Report Item 3: Shareholders - See attached spreadsheets for:
Max Bancorp, LLC
Sandhills Holding Company, Inc.

Report Item 4: Insiders – See attached spreadsheets for:
Max Bancorp, LLC
Sandhills Holding Company, Inc.

Results: A list of branches for your depository institution: SANDHILLS BANK (ID_RSSD: 806220).
This depository institution is held by MAX BANCORP, LLC (3878835) of NORTH MYRTLE BEACH, SC.
The data are as of 12/31/2019. Data reflects information that was received and processed through 01/07/2020.

Reconciliation and Verification Steps
1. In the **Data Action** column of each branch row, enter one or more of the actions specified below
2. If required, enter the date in the **Effective Date** column

Actions
OK: If the branch information is correct, enter 'OK' in the **Data Action** column.
Change: If the branch information is incorrect or incomplete, revise the data, enter 'Change' in the **Data Action** column and the date when this information first became valid in the **Effective Date** column.
Close: If a branch listed was sold or closed, enter 'Close' in the **Data Action** column and the sale or closure date in the **Effective Date** column.
Delete: If a branch listed was never owned by this depository institution, enter 'Delete' in the **Data Action** column.
Add: If a reportable branch is missing, insert a row, add the branch data, and enter 'Add' in the **Data Action** column and the opening or acquisition date in the **Effective Date** column.

If printing this list, you may need to adjust your page setup in MS Excel. Try using landscape orientation, page scaling, and/or legal sized paper.

Submission Procedure
When you are finished, send a saved copy to your FRB contact. See the detailed instructions on this site for more information.
If you are e-mailing this to your FRB contact, put your institution name, city and state in the subject line of the e-mail.

Note:
To satisfy the **FR Y-10 reporting requirements**, you must also submit FR Y-10 Domestic Branch Schedules for each branch with a **Data Action** of Change, Close, Delete, or Add.
The FR Y-10 report may be submitted in a hardcopy format or via the FR Y-10 Online application - https://y10online.federalreserve.gov.

* FDIC UNINUM, Office Number, and ID_RSSD columns are for reference only. Verification of these values is not required.

Data Action	Effective Date	Branch Service Type	Branch ID_RSSD*	Popular Name	Street Address	City	State	Zip Code	County	Country	FDIC UNINUM*	Office Number*	Head Office	Head Office ID_RSSD*	Comments
OK		Full Service (Head Office)	806220	SANDHILLS BANK	1020 HIGHWAY 17 NORTH	NORTH MYRTLE BEACH	SC	29582	HORRY	UNITED STATES	Not Required	Not Required	SANDHILLS BANK	806220	
OK		Full Service	3677001	CAROLINA FOREST BRANCH	273 CAROLINA FOREST BLVD	MYRTLE BEACH	SC	29579	HORRY	UNITED STATES	Not Required	Not Required	SANDHILLS BANK	806220	
OK		Full Service	5339705	FARROW COMMONS BRANCH	3600 DORSETT DRIVE	MYRTLE BEACH	SC	29577	HORRY	UNITED STATES	Not Required	Not Required	SANDHILLS BANK	806220	
OK		Full Service	4978068	MYRTLE BEACH- INTERNATIONAL DRIVE	610 INTERNATIONAL DRIVE	MYRTLE BEACH	SC	29579	HORRY	UNITED STATES	Not Required	Not Required	SANDHILLS BANK	806220	
OK		Full Service	3282526	WINDY HILL BRANCH	4400 HIGHWAY 17 SOUTH	NORTH MYRTLE BEACH	SC	29582	HORRY	UNITED STATES	Not Required	Not Required	SANDHILLS BANK	806220	

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Max Bancorp, LLC
Fiscal Year Ending December 31, 2019

Report Item 3: Shareholders
(1)(a)(b)(c) and (2)(a)(b)(c)

Current Shareholders with ownership, control or holdings of 5% or more with power of vote as of fiscal year ending 12-31-2019			Shareholders not listed in 3 (1)(a) through 3(1)(c) that had ownership, control or holdings of 5% or more with power to vote during the fiscal year ending 12-31-2019		
(1)(a) Name & Address (City, State, Country)	(1)(b) Country of Citizenship or Incorporation	(1)(c) Number and Percentage of Each Class of Voting Securities	(2)(a) Name & Address (City, State, Country)	(2)(b) Country of Citizenship or Incorporation	(2)(c) Number and Percentage of Each Class of Voting Securities
N. Richard Kalikow New York, NY USA	USA	75% of the voting interests	None	N/A	N/A
Martin B. Greenberg Boca Raton, FL USA	USA	25% of the voting interests			

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Sandhills Holding Company, Inc.
Fiscal Year Ending December 31, 2019

Report Item 3: Shareholders
(1)(a)(b)(c) and (2)(a)(b)(c)

Current Shareholders with ownership, control or holdings of 5% or more with power of vote as of fiscal year ending 12-31-2019			Shareholders not listed in 3 (1)(a) through 3(1)(c) that had ownership, control or holdings of 5% or more with power to vote during the fiscal year ending 12-31-2019		
(1)(a) Name & Address (City, State, Country)	(1)(b) Country of Citizenship or Incorporation	(1)(c) Number and Percentage of Each Class of Voting Securities	(2)(a) Name & Address (City, State, Country)	(2)(b) Country of Citizenship or Incorporation	(2)(c) Number and Percentage of Each Class of Voting Securities
Max Bancorp, LLC North Myrtle Beach,SC USA	USA	1,184,712.28 shares 94.8998%	None	N/A	N/A

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Max Bancorp, LLC
Fiscal Year Ending December 31, 2019

Report Item 4: Insiders
(1), (2), (3)(a)(b)(c) and (4)(a)(b)©

(1) Names & Address (City, State, Country)	(2) Principal Occupation, if other than with Bank Holding Company	(3)(a) Title & Position with Bank Holding Company	(3)(b) Title & Position with Subsidiaries (include names of subsidiaries)	(3)(c) Title & Position with Other Businesses (includes names of other businesses)	(4)(a) Percentage of Voting Shares in Bank Holding Company	(4)(b) Percentage of Voting Shares in Subsidiaries (include names of subsidiaries)	(4)(c) List names of other companies (includes partnerships) if 25% or more of voting securities are held (List names of companies and percentage of voting securities held)
Martin B. Greenberg Boca Raton, FL USA	Chairman, Sterling Commodities Corp.	Member	Director and Vice-Chair of Sandhills Holding Company, Inc.	Chairman of Sterling Commodities Corp.	25% of voting interests	**Sandhills Holding Company, Inc.** 0.3364%	Sterling Commodities Corp. (100%); G. Martin Associates (50%); Beta Capital, LLC (25%)
N. Richard Kalikow New York, NY USA	Chairman & CEO, Gamma Real Estate, LLC	Managing Member	Director & Chair of Sandhills Holding Company, Inc.	President and Managing Member of Manchester Real Estate & Construction, LLC; Managing Member of Max Bancorp, LLC President of Kalikow Realty & Construction Corp.; General Partner of Kalikow Realty Company; Managing Member of Fortune Funding, LLC; Manager of Beta Capital, LLC; Chairman & CEO of Gamma Real Estate, LLC; Managing Member of Gamma Funding Special Limited Partner, LLC; Managing Member of Gamma Funding Management, LLC; Managing Member of Triton Real Estate Special Limited Partner, LLC; Managing Member of Gamma Development, LLC; Managing Member of GRE 50 Hurt SLP, LLC Managing Member of GRE Pencil Factory Investor MM, LLC Trustee of The Heisman Trophy Trust	75% of voting interests	**Sandhills Holding Company, Inc.** 3.4685%	Manchester Real Estate & Construction, LLC (100%); Max Bancorp, LLC (75%) Kalikow Realty & Construction Corp. (100%); Fortune Funding, LLC (99.99%); Kalikow Realty Company (50%); Triton Real Estate Special Limited Partner (100%); Gamma Real Estate, LLC (50%); Gamma Funding Special Limited Partner, LLC (50%) Gamma Funding Management, LLC (50%); Gamma Development, LLC (50%); Gamma Funding Management, LP (49.5%) GRE 50 Hurt SLP, LLC (25%) *The following entities are owned through Fortune Funding, LLC:* Beta Capital, LLC (75%);

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Sandhills Holding Company, Inc.
Fiscal Year Ending December 31, 2019

Report Item 4: Insiders
(1), (2), (3)(a)(b)(c) and (4)(a)(b)(c)

(1) Names & Address (City, State, Country)	(2) Principal Occupation, if other than with Bank Holding Company	(3)(a) Title & Position with Bank Holding Company	(3)(b) Title & Position with Subsidiaries (include names of subsidiaries)	(3)(c) Title & Position with Other Businesses (includes names of other businesses)	(4)(a) Percentage of Voting Shares in Bank Holding Company	(4)(b) Percentage of Voting Shares in Subsidiaries (include names of subsidiaries)	(4)(c) List names of other companies (includes partnerships) if 25% or more of voting securities are held (List names of companies and percentage of voting securities held)
Darra W. Cothran Columbia, SC USA	Attorney	Director	Director of Sandhills Bank	Limited partner of Heniford Farms Ltd. Ptsp.; General partner of Woodward, Cothran & Herndon Member & Manager of DOH, LLC Trustee of the Heniford Trust B.	Total 0.1040%	None	Woodward, Cothran & Herndon (33.33%) The Heniford Trust B (33.3%)
Martin B. Greenberg Boca Raton, FL USA	Chairman, Sterling Commodities Corp.	Director & Vice-Chair	Director & Vice-Chair of Sandhills Bank	Member of Max Bancorp, LLC; Chairman of Sterling Commodities Corp.	Total 0.3364%	None	Sterling Commodities Corp. (100%); G. Martin Associates (50%); Max Bancorp, LLC (25%); Beta Capital, LLC (25%)
Max Bancorp, LLC North Myrtle Beach,SC USA	N/A	N/A	N/A	N/A	Total 94.8998%; ownership in this company is of Greenberg and Kalikow of this schedule	N/A	N/A
Jonathan G. Kalikow New York, NY USA	President, Gamma Real Estate, LLC	Director	Director of Sandhills Bank	President of Gamma Real Estate, LLC	Total 0.8010%	None	Gamma Real Estate, LLC (50%); Gamma Funding Special Limited Partner, LLC (50%) Gamma Funding Management, LLC (50%); Gamma Development, LLC (50%); Gamma Funding Management, LP (49.5%) GRE 50 Hurt SLP, LLC (25%)
N. Richard Kalikow New York, NY USA	Chairman & CEO, Gamma Real Estate, LLC	Director & Chair	Director & Chair of Sandhills Bank	President and Managing Member of Manchester Real Estate & Construction, LLC; Managing Member of Max Bancorp, LLC President of Kalikow Realty & Construction Corp.; General Partner of Kalikow Realty Company; Managing Member of Fortune Funding, LLC; Manager of Beta Capital, LLC; Chairman & CEO of Gamma Real Estate, LLC; Managing Member of Gamma Funding Special Limited Partner, LLC; Managing Member of Gamma Funding Management, LLC; Managing Member of Triton Real Estate Special Limited Partner, LLC; Managing Member of Gamma Development, LLC Managing Member of GRE 50 Hurt SLP, LLC Managing Member of GRE Pencil Factory Investor MM, LLC Trustee of The Heisman Trophy Trust	Total 3.4685%	None	Manchester Real Estate & Construction, LLC (100%); Max Bancorp, LLC (75%) Kalikow Realty & Construction Corp. (100%); Fortune Funding, LLC (99.99%); Kalikow Realty Company (50%); Triton Real Estate Special Limited Partner (100%); Gamma Real Estate, LLC (50%); Gamma Funding Special Limited Partner, LLC (50%) Gamma Funding Management, LLC (50%); Gamma Development, LLC (50%); Gamma Funding Management, LP (49.5%) GRE 50 Hurt SLP, LLC (25%) *The following entities are owned through Fortune Funding, LLC:* Beta Capital, LLC (75%);
James B. Smith Myrtle Beach, SC USA	N/A	Director & President & CEO	Director, President and CEO of Sandhills Bank	Manager of A&K Futures, LLC	Total 0.1335%	None	A&K Futures, LLC (50%)

Sandhills Holding Company
and Subsidiaries

Report on Consolidated Financial Statements

For the years ended December 31, 2019 and 2018

Contents

Independent Auditor's Report

To the Shareholders and Board of Directors
Sandhills Holding Company and Subsidiaries
North Myrtle Beach, South Carolina

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of Sandhills Holding Company and Subsidiaries (the "Company"), which comprise the consolidated balance sheet as of December 31, 2019, the related consolidated statements of income, comprehensive income, changes in shareholders' equity, and cash flows for the year then ended, and the related notes to the consolidated financial statements (collectively, the "financial statements").

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these 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.

Auditor's Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the 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 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 financial statements referred to above present fairly, in all material respects, the financial position of Sandhills Holding Company and Subsidiaries as of December 31, 2019 and 2018, and the results of their operations and their cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Prior Period Financial Statements

The financial statements of Sandhills Holding Company and Subsidiaries as of December 31, 2018 were audited by other auditors whose report dated April 4, 2019, expressed an unmodified opinion on those statements.

Elliott Davis, LLC

Columbia, South Carolina
March 6, 2020

Sandhills Holding Company and Subsidiaries

Consolidated Balance Sheets

As of December 31, 2019 and 2018

	2019	2018
Assets:		
Cash and cash equivalents:		
Cash and due from banks	$ 4,861,193	$ 4,690,051
Interest-bearing cash	161,249	5,419,712
Federal funds sold	2,947,000	1,329,000
Total cash and cash equivalents	7,969,442	11,438,763
Investment securities:		
Securities available-for-sale	19,302,928	10,954,305
Other investments	1,133,450	986,950
Time deposits at other institutions	140,231	1,639,380
Total investment securities	20,716,840	13,580,635
Loans receivable, net	144,946,776	127,515,065
Mortgage loans held for sale	158,629	293,888
Premises and equipment, net	16,147,726	16,557,528
Accrued interest receivable	715,171	645,600
Other real estate owned	-	130,000
Cash surrender value of life insurance	400,874	388,887
Core deposit intangible	99,879	150,039
Goodwill	681,690	681,690
Deferred tax asset, net	3,437,580	3,495,411
Other assets	328,342	660,839
Total assets	$ 195,462,718	$ 175,538,345
Liabilities:		
Deposits:		
Noninterest-bearing transaction accounts	$ 15,011,918	$ 12,657,250
Interest-bearing transaction accounts	17,305,050	18,527,110
Money market and savings	44,663,884	36,292,610
Time deposits $250,000 and over	18,857,432	12,891,297
Other time deposits	66,585,245	67,854,165
Total deposits	162,423,529	148,222,432
Advances from Federal Home Loan Bank	10,500,000	5,000,000
Subordinated debt	8,349,753	8,322,843
Accrued interest payable	242,377	247,309
Other liabilities	494,598	502,921
Total liabilities	182,010,257	162,295,505
Commitments and contingencies - Notes 17 and 19		
Shareholders' equity:		
Preferred stock, $1.00 par value; 50,000,000 shares authorized; none issued and outstanding	-	-
Common stock, $1.00 par value; 200,000,000 shares authorized; 1,248,382 and 1,247,609 issued and outstanding at December 31, 2019 and 2018, respectively	1,248,382	1,247,609
Additional paid in capital	21,285,065	21,277,690
Accumulated deficit	(8,981,595)	(9,127,473)
Accumulated other comprehensive loss	(99,391)	(154,986)
Total shareholders' equity	13,452,461	13,242,840
Total liabilities and shareholders’ equity	$ 195,462,718	$ 175,538,345

See Notes to Consolidated Financial Statements

Sandhills Holding Company and Subsidiaries

Consolidated Statements of Income

For the years ended December 31, 2019 and 2018

	2019	2018
Interest income:		
Interest on loans receivable	$ 7,578,833	$ 7,146,404
Interest on investment securities	449,184	276,987
Other interest income	123,194	178,001
Total interest income	8,151,211	7,601,392
Interest expense:		
Interest on deposits	1,944,801	1,410,312
Interest on borrowings	740,551	707,267
Total interest expense	2,685,352	2,117,579
Net interest income	5,465,859	5,483,813
Provision for loan losses	-	30,000
Net interest income after provision for loan losses	5,465,859	5,453,813
Non-interest income:		
Service charges	40,352	49,919
Non-sufficient funds service charges	126,684	132,396
Overdraft privilege fees	93,151	95,642
Other service charges and fees	133,322	114,214
Gain (loss) on sale of investment securities	77,477	(4,000)
Gain on sale of fixed assets	30,203	47,242
Gain on sale of loans	253,966	170,611
ATM income	264,930	264,263
Gain on sale of branch held for sale	-	278,009
Other	42,588	40,558
Total non-interest income	1,062,673	1,188,854
Non-interest expense:		
Salaries and employee benefits	3,325,705	2,951,771
Net occupancy	923,328	952,313
Insurance	74,301	74,368
Professional services	170,998	200,465
Amortization of core deposit intangible	50,160	50,160
Writedown on other assets	-	250,000
Net cost of operation of other real estate owned	38,878	755
Other operating expenses	1,732,963	1,777,927
Total non-interest expense	6,316,333	6,257,757
Income before income taxes	212,199	384,910
Income tax expense	66,321	103,434
Net income	$ 145,878	$ 281,476
Basic earnings per share	$ 0.12	$ 0.29
Weighted average basic shares outstanding	1,248,200	960,740

See Notes to Consolidated Financial Statements

Sandhills Holding Company and Subsidiaries

Consolidated Statements of Comprehensive Income

For the years ended December 31, 2019 and 2018

	2019	2018
Net income	$ 145,878	$ 281,476
Other comprehensive income (loss)		
Unrealized holding gains (losses) arising during the period	151,169	(132,646)
Tax effect	(37,118)	29,891
Reclassification adjustment for realized (gains) losses included in net income	(77,477)	4,000
Tax effect	19,021	(982)
Other comprehensive income (loss)	55,595	(99,737)
Comprehensive income	$ 201,473	$ 181,739

See Notes to Consolidated Financial Statements

Sandhills Holding Company and Subsidiaries

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

	Common Stock Shares	Common Stock Amount	Additional Paid in Capital	Accumulated Deficit	Accumulated Other Comprehensive Income (loss)	Total
Balance, December 31, 2017	944,279	$ 944,279	$ 18,832,247	$ (9,408,949)	$ (55,249)	$ 10,312,328
Net income	-	-	-	281,476	-	281,476
Other comprehensive loss, net of tax	-	-	-	-	(99,737)	(99,737)
Issuance of common stock	303,330	303,330	2,445,443	-	-	2,748,773
Balance, December 31, 2018	1,247,609	1,247,609	21,277,690	(9,127,473)	(154,986)	13,242,840
Net income	-	-	-	145,878	-	145,878
Other comprehensive income, net of tax	-	-	-	-	55,595	55,595
Issuance of common stock	773	773	7,375	-	-	8,148
Balance, December 31, 2019	1,248,382	$ 1,248,382	$ 21,285,065	$ (8,981,595)	$ (99,391)	$ 13,452,461

See Notes to Consolidated Financial Statements

Sandhills Holding Company and Subsidiaries

Consolidated Statements of Cash Flows

For the years ended December 31, 2019 and 2018

	2019	2018
Operating activities:		
Net income	$ 145,878	$ 281,476
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	-	30,000
Depreciation	623,258	636,979
Amortization of core deposit intangible	50,160	50,160
Net amortization/accretion	127,077	104,509
(Gain) loss on sale of investments	(77,477)	4,000
Gain on sale of fixed assets	(30,203)	(47,242)
Gain on sale of loans	(253,966)	(170,611)
Net gain on sale of government guaranteed loans	(101,086)	-
Gain on sale of branch held for sale	-	(278,009)
Disbursements for mortgages held for sale	8,265,378	8,265,578
Proceeds from sales of mortgages held for sale	(7,977,239)	(8,388,855)
(Gain) loss on sale of other real estate owned	6,685	(55,733)
Writedown on other real estate owned	30,000	42,537
Decrease in deferred income taxes	39,737	69,763
Increase in accrued interest receivable	(69,571)	(58,811)
(Decrease) increase in accrued interest payable	(4,932)	152,035
Increase in cash surrender value life insurance	(11,987)	(8,937)
Decrease in other assets	364,770	254,477
Decrease in other liabilities	(40,598)	(57,689)
Net cash provided by operating activities	1,186,970	825,627
Cash flows from investing activities:		
Proceeds from sales, maturities, calls, and paydowns of securities available-for-sale	15,205,465	2,516,185
Purchase of securities available-for-sale	(23,579,999)	(4,053,195)
Purchase of other investments	(146,500)	(5,100)
Sales of time deposits at other institutions, net	1,549,151	526,769
Net (decrease) increase of loans receivable	(17,330,625)	435,607
Purchase of premises and equipment, net	(183,253)	(1,867,409)
Cash transferred related to branch sale, net	-	(10,810,246)
Proceeds from sales of other real estate owned	93,315	733,952
Net cash used in investing activities	(24,392,446)	(12,523,437)
Cash flows from financing activities:		
Net increase in deposit accounts	14,201,097	13,157,545
Proceeds from advances from the Federal Home Loan Bank, net	5,500,000	-
Amortization of subordinated debt issuance costs	26,910	26,910
Proceeds from issuance of common stock	8,148	2,748,773
Net cash provided by financing activities	19,736,155	15,933,228
Net change in cash and cash equivalents	(3,469,321)	4,235,418
Cash and cash equivalents, beginning of year	11,438,763	7,203,345
Cash and cash equivalents, end of year	$ 7,969,442	$ 11,438,763
Noncash investing and financing activities		
Net change in unrealized (loss) gain on securities available-for-sale	$ 73,691	$ (128,646)
Supplemental information		
Cash paid during the year for interest	$ 2,690,284	$ 1,965,546
Cash paid during the year for income taxes	$ 15,000	$ 1,000

See Notes to Consolidated Financial Statements

Note 1. Summary of Significant Accounting Policies

Sandhills Holding Company (the "Company") is a bank holding company whose principal activity is the ownership and management of its wholly owned subsidiaries, Sandhills Bank (the "Bank") and South Investments, LLC (South Investments). The Bank operates under a state charter and provides full banking services. South Investments is used to hold certain real estate and loans.

The accounting and reporting policies of the Company conform to accounting principles generally accepted in the United States of America and to general practices within the banking industry. Financial position and operating results are determined by use of the accrual method of accounting, which endeavors to recognize income in the period earned and to match income with all costs of earning it.

Principles of Consolidation:

The accompanying consolidated financial statements include the accounts of Sandhills Holding Company and its wholly owned subsidiaries, Sandhills Bank and South Investments, LLC. The Company operates as one business segment. All significant intercompany balances and transactions between the Company and its subsidiaries have been eliminated.

Use of Estimates:

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

Material estimates that are particularly susceptible to significant change relate to the determination of the allowance for loan losses, including valuation allowances for impaired loans, the carrying amount of real estate acquired in connection with foreclosures or in satisfaction of loans, the fair value estimates for financial instruments, the valuation of deferred tax assets, and goodwill. Management must also make estimates in determining the estimated useful lives and methods for depreciating premises and equipment.

While management uses available information to recognize losses on loans and foreclosed real estate, future additions to the allowance 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 Company's allowances for losses on loans and foreclosed real estate. Such agencies may require the Company to recognize additions to the allowances 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 allowances for losses on loans and foreclosed real estate may change materially in the near term.

Note 1. Summary of Significant Accounting Policies, Continued

Concentrations of Credit Risk:

Financial instruments, which potentially subject the Company to concentrations of credit risk, consist principally of loans receivable, investment securities, federal funds sold and amounts due from banks.

In addition to monitoring potential concentrations of loans to particular borrowers or groups of borrowers, industries and geographic regions, management monitors exposure to credit risk from concentrations of lending products and practices such as loans that subject borrowers to substantial payment increases (e.g. principal deferral periods, loans with initial interest-only periods) and loans with high loan-to-value ratios. Additionally, there are industry practices that could subject the Company to increased credit risk should economic conditions change over the course of a loan’s life. For example, the Company makes variable rate loans and fixed rate principal-amortizing loans with maturities prior to the loan being fully paid (i.e. balloon payment loans). These loans are underwritten and monitored to manage the associated risks. Therefore, management believes that these particular practices do not subject the Company to unusual credit risk.

The Company’s investment portfolio consists principally of obligations of the United States, its agencies or its corporations and general obligation municipal securities. In the opinion of management, there is no concentration of credit risk in its investment portfolio. The Company places its deposits and correspondent accounts with and sells its federal funds to high quality institutions. Management believes credit risk associated with correspondent accounts is not significant.

Cash and Cash Equivalents:

The Company considers all cash and amounts due from depository institutions, interest-bearing cash, and federal funds sold to be cash equivalents for purposes of the statements of cash flows.

Investment Securities:

Debt securities and time deposits with other institutions are classified as held-to-maturity when the Company has the positive intent and ability to hold the securities to maturity. Securities held-to-maturity are carried at the amortized cost. The amortization of premiums and accretion of discounts are recognized in interest income using methods approximating the interest method over the period to maturity.

Debt securities and time deposits with other institutions not classified as held-to-maturity are classified as available-for-sale. Securities available-for-sale are carried at amortized cost and adjusted to estimated market value by recognizing the aggregate unrealized gains or losses in a valuation account. Aggregate market valuation adjustments are recorded in stockholders' equity net of deferred income taxes. Reductions in market value considered by management to be other than temporary are reported as a realized loss and a reduction in the cost basis of the security. The adjusted cost basis of investments available-for-sale is determined by specific identification and is used in computing the gain or loss upon sale.

Note 1. Summary of Significant Accounting Policies, Continued

Investment Securities, continued:

Declines in the fair value of individual held-to-maturity and available-for-sale debt securities below their cost that are other than temporary result in write-downs of the individual securities to their fair value. The related write-downs are included in earnings as realized losses. In estimating other-than-temporary impairment losses on debt securities, 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 issuers, (3) the outlook for receiving the contractual cash flows of the investments, (4) the anticipated outlook for changes in the general level of the interest rates, and (5) the intent of the Company to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery of contractual cash flows, and whether it is more-likely-than-not that the Company will be required to sell the debt security prior to recovering its fair value.

Other Investments:

Other investments are nonmarketable equity securities that include the cost of the Company's investment in the stock of the Federal Home Loan Bank and an investment in two other community banker's banks. These stocks have no quoted market value and no ready market for them exists. Investment in Federal Home Loan Bank stock is a condition of borrowing from the Federal Home Loan Bank, and the stock is pledged to collateralize the borrowings.

Loans Receivable:

The Company grants mortgage, commercial and consumer loans to customers. The ability of the Company's debtors to honor their contracts is dependent upon the real estate and general economic conditions of surrounding areas.

Loans are stated at their unpaid principal balance, net of any charge-offs. Interest income is computed using the simple interest method and is recorded in the period earned. Loan fees and certain direct origination costs are deferred and amortized over the estimated terms of the loans using the level yield method. The accretion and amortization of loan fees and origination costs are presented as a component of loan interest income on the statements of operations.

Loans acquired in a business combination are recorded at estimated fair value on their purchase date; the purchaser cannot carry over the related allowance for loan losses. When the acquired loans have evidence of credit deterioration since origination and it is probable at the date of acquisition that the Company will not collect all contractually required principal and interest payments, the difference between contractually required payments at acquisition and the cash flows expected to be collected at acquisition is referred to as the nonaccretable difference which is included in the carrying amount of the loans. Subsequent decreases to the expected cash flows will generally result in a provision for loan losses. Subsequent increases in cash flows result in a reversal of the provision for loan losses to the extent of prior charges, or a reclassification of the difference from nonaccretable to accretable, with a positive impact on interest income.

Any excess of cash flows expected at acquisition over the estimated fair value is referred to as the accretable yield and is recognized into interest income over the remaining life of the loan when there is a reasonable expectation about the amount and timing of such cash flows. For acquired performing loans, the fair value adjustments are being accreted into income based on contractual cash flows, using the effective interest rate method over the remaining maturities of the underlying loans.

Note 1. Summary of Significant Accounting Policies, Continued

Loans Receivable, continued:

When serious doubt exists as to the collectability of a loan or when a loan becomes contractually 90 days past due as to principal or interest, interest income is generally discontinued unless the estimated net realizable value of collateral exceeds the principal balance and accrued interest and there is no doubt about the ultimate collectability of principal.

Loans are returned to accrual status when, in management's judgment, the borrower has demonstrated the ability to make periodic interest and principal payments on a timely basis.

The Bank identifies impaired loans through its normal internal loan review process. Loans on the Bank's problem loan watch list are considered potentially impaired loans. These loans are evaluated in determining whether the borrower will be able to perform in accordance with the loan agreement. Loans are not considered impaired if a minimal payment delay occurs and all amounts due, including accrued interest at the contractual interest rate for the period of delay, are expected to be collected.

Troubled Debt Restructurings (TDRs):

The Company designates loan modifications as TDRs when, for economic or legal reasons related to the borrower's financial difficulties, it grants a concession to the borrower that it would not otherwise consider. Loans on nonaccrual status at the date of modification are initially classified as nonaccrual TDRs. Loans on accruing status at the date of modification are initially classified as accruing TDRs at the date of modification, if the note is reasonably assured of repayment and performance is in accordance with its modified terms. Such loans may be designated as nonaccrual loans subsequent to the modification date if reasonable doubt exists as to the collection of interest or principal under the restructuring agreement. Nonaccrual TDRs are returned to accrual status when there is economic substance to the restructuring, there is well documented credit evaluation of the borrower's financial condition, the remaining balance is reasonably assured of repayment in accordance with its modified terms, and the borrower has demonstrated repayment performance in accordance with the modified terms for a reasonable period of time (generally a minimum of six months).

Allowance for Loan Losses:

The allowance for loan losses is based on management's ongoing evaluation of the loan portfolio and reflects an amount that, in management's opinion, is adequate to absorb losses in the existing portfolio. In evaluating the portfolio, management takes into consideration numerous factors, including current economic conditions, prior loan loss experience, the composition of the loan portfolio, and management's estimate of anticipated credit losses. An unallocated component is maintained to cover uncertainties that could affect management's estimate of the probability of losses. The unallocated component of the allowance reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating specific and general losses in the portfolio. Loans are charged-off against the allowance at such time as they are determined to be losses. Subsequent recoveries and provisions for loan losses are credited to the allowance. Management considers the year-end allowance appropriate and adequate to cover possible losses in the loan portfolio; however, management's judgment is based upon a number of assumptions about future events, which are believed to be reasonable, but which may or may not prove valid. Thus, there can be no assurance that charge-offs in future periods will not exceed the allowance for loan losses or that additional increases in the allowance for loan losses will not be required. Allowances for loan losses are subject to review by various regulatory authorities and may be subject to adjustment upon their examination.

Note 1. Summary of Significant Accounting Policies, Continued

Allowance for Loan Losses, continued:

Loans are placed in a non-accrual status when, in the opinion of management, the collection of additional interest is questionable. Thereafter, no interest is taken into income unless received in cash or until such time as the borrower demonstrates the ability to pay principal and interest.

A loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed. Impairment is measured on a loan by loan basis for commercial and construction loans by either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's obtainable market price, or the fair value of the collateral if the loan is collateral dependent.

Large groups of smaller balance homogeneous loans are collectively evaluated for impairment. Accordingly, the Company does not separately identify individual consumer and residential loans for impairment disclosures, unless such loans are the subject of a restructuring agreement.

Off-Balance Sheet Credit Related Financial Instruments:

In the ordinary course of business, the Company has entered into commitments to extend credit, including commitments under credit card arrangements, commercial letters of credit, and standby letters of credit. Such financial instruments are recorded when they become payable by the customer.

Residential Mortgage Loans Held for Sale:

Loans held for sale represent loans originated or acquired by the Company with the intent to sell. The Company has elected the fair value option of accounting for certain residential mortgage loans. Electing to use the fair value option of accounting allows a better offset of the changes in the fair values of the loans and the derivative instruments used to economically hedge them without the burden of complying with the requirements for hedge accounting. These loans are initially recorded and carried at fair value, with changes in fair value recognized in income from mortgage operations. Loan origination fees are recorded when earned.

The Company issues rate lock commitments to borrowers on prices quoted by secondary market investors. Derivatives related to these commitments are recorded as either assets or liabilities in the balance sheet and are measured at fair value. Changes in the fair value of the derivatives are reported in current income or other comprehensive income depending on the purpose for which the derivative is held. Accordingly, changes in fair value of these derivative instruments would normally be included in noninterest income in the consolidated statements of operations. However, these amounts were immaterial at December 31, 2019 and 2018.

Note 1. Summary of Significant Accounting Policies, Continued

Other Real Estate Owned:

Other real estate owned includes real estate acquired through foreclosure. Other real estate owned is initially recorded at fair value less cost to sell at the date of foreclosure, establishing a new cost basis. Subsequent to foreclosure, valuations are periodically performed by management and the assets are carried at the lower of carrying amount or fair value less cost to sell.

Any write-downs at the dates of acquisition are charged to the allowance for loan losses. Expenses to maintain such assets, subsequent write-downs, and gains and losses on disposal are included in net cost of operation of other real estate owned.

Premises and Equipment:

Premises and equipment are stated at cost less accumulated depreciation computed principally on the straight line method over the estimated useful lives of the assets. Estimated lives range up to 40 years for buildings and improvements and up to 10 years for furniture and equipment. The cost of assets sold or otherwise disposed of and the related allowance for depreciation are eliminated from the accounts and the resulting gains or losses are reflected in the statement of operations when incurred. The costs of major renewals and improvements are capitalized.

Acquired premises and equipment are initially stated at fair value based on third party appraisals. Subsequent to the fair value adjustment, the assets are depreciated using the same methods as above.

Intangible Assets:

Business combinations are accounted for using the acquisition method of accounting. Core deposit intangibles are recognized separately and are amortized over their estimated useful lives. The core deposit intangible is being amortized on a 150% declining balance basis for 7 years.

The Company reviews the carrying value of goodwill on an annual basis and on an interim basis if certain events or circumstances indicate that an impairment loss may have been incurred. An impairment charge is recognized if the carrying value of the reporting unit’s goodwill exceeds its implied fair value. The Company's evaluations for the years ended December 31, 2019 and 2018 indicated no impairment of goodwill.

Advertising Costs:

Advertising costs are expensed as incurred. Advertising costs amounted to $158,723 and $97,548 for the years ended December 31, 2019 and 2018, respectively and recorded within other operating expenses. External costs incurred in producing media advertising are expensed the first time the advertising takes place. External costs relating to direct mailing costs are expensed in the period in which the direct mailings are sent.

Note 1. Summary of Significant Accounting Policies, Continued

Income Taxes:

The Company accounts for income taxes in accordance with ASC 740, "Income Taxes". Under ASC 740, deferred tax assets or liabilities are computed based upon the difference between financial statement and income tax bases of assets and liabilities using the enacted marginal tax rate. If it is more likely than not that a tax asset will not be realized, a valuation allowance is required to reduce the recorded deferred tax assets to net realizable value. As of December 31, 2019 and 2018, management concluded that a partial valuation allowance was required.

The Company recognizes the tax benefit from an uncertain tax position only if it is more likely than not the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position. The tax benefits recognized in the financial statements from such positions are then measured based on the largest benefit that has a greater than 50% likelihood of being realized upon settlement. See Note 16, "Income Taxes" for additional information. The Company records any penalties and interest attributed to uncertain tax positions as a component of income tax expense.

Earnings per Share:

Earnings per share are calculated by dividing net income by the weighted average number of common shares outstanding during the year. The Company has no instruments which are considered common stock equivalents and therefore, diluted earnings per share are not presented.

Comprehensive Income:

The Company reports comprehensive income in accordance with Accounting Standards Codification (“ASC”) 220, “Comprehensive Income.” The standard requires that all items that are required to be reported under accounting standards as comprehensive income be reported in a financial statement that is displayed with the same prominence as other consolidated financial statements. The disclosure requirements have been included in the Company’s consolidated statements of comprehensive income.

Statement of Cash Flow:

For purposes of reporting cash flows, the Company considers certain highly liquid debt instruments purchased with an original maturity of three months or less to be cash equivalents. Cash equivalents include amounts from banks, interest-bearing cash, and federal funds sold.

Reclassifications and Prior Year Adjustments:

Certain captions and amounts in the financial statements as of December 31, 2018 were reclassified to conform to the December 31, 2019 presentation.

Note 1. Summary of Significant Accounting Policies, Continued

Recently Issued Accounting Pronouncements:

The following is a summary of recent authoritative pronouncements that could impact the accounting, reporting, and/or disclosure of financial information by the Company.

In May 2014 and August 2015, the FASB issued guidance to change the recognition of revenue from contracts with customers. The core principle of the new guidance is that an entity should recognize revenue to reflect the transfer of goods and services to customers in an amount equal to the consideration the entity receives or expects to receive. The guidance was effective for the Company for reporting periods beginning after December 15, 2018. The Company applied the guidance using a modified retrospective approach. The Company's revenue is comprised of net interest income and noninterest income. The scope of the guidance explicitly excludes net interest income as well as many other revenues for financial assets and liabilities including loans, leases, securities, and derivatives. Accordingly, the majority of our revenues were not affected. The Company has performed an assessment of our revenue contracts related to revenue streams that are within the scope of the standard. Our accounting policies have not changed materially since the principles of revenue recognition from the ASU are largely consistent with existing guidance and current practices applied by our businesses. We have not identified material changes to the timing or amount of revenue recognition.

In January 2016, the FASB amended the Financial Instruments topic of the Accounting Standards Codification to address certain aspects of recognition, measurement, presentation, and disclosure of financial instruments. The amendments became effective for 2019. The Company applied the guidance by means of a cumulative-effect adjustment to the balance sheet as of the beginning of the fiscal year of adoption. The amendments related to equity securities without readily determinable fair values were applied prospectively to equity investments that exist as of the beginning of 2019. These amendments had no material effect on the Company's financial statements.

In March 2016, the FASB amended the Revenue from Contracts with Customers topic of the Accounting Standards Codification to clarify the implementation guidance on principal versus agent considerations. The updates to the principal versus agent guidance: (i) require an entity to determine whether it is a principal or an agent for each distinct good or service (or a distinct bundle of goods or services) to be provided to the customer; (ii) illustrate how an entity that is a principal might apply the control principle to goods, services, or rights to services, when another party is involved in providing goods or services to a customer and (iii) clarify that the purpose of certain specific control indicators is to support or assist in the assessment of whether an entity controls a good or service before it is transferred to the customer, provide more specific guidance on how the indicators should be considered, and clarify that their relevance will vary depending on the facts and circumstances. The Company's revenue is primarily comprised of net interest income on financial assets and financial liabilities, which is explicitly excluded from the scope of ASU 2014-09, and non-interest income. A description of the Company's revenue streams accounted for under ASC 606, Revenue from contracts with customers follows:

> Deposit service charges: The Company earns fees from its deposit customers for transaction-based, account maintenance, and overdraft services. Transaction-based fees are recognized at the time the transaction is executed as that is the point in time the Company fulfills the customer's request. Overdraft fees are recognized at the point in time that the overdraft occurs. Service charges on deposits are withdrawn from the customer's account balance.

Note 1. Summary of Significant Accounting Policies, Continued

Recently Issued Accounting Pronouncements, continued:

Debit card income: The Company earns interchange fees from debit cardholder transactions conducted through payment networks. Interchange fees from cardholder transactions represent a percentage of the underlying transaction value and are recognized daily, with the transaction processing services provided to the cardholder. Fees are recognized on a daily basis.

In February 2016, the FASB amended the Leases topic of the ASC to revise certain aspects of recognition, measurement, presentation, and disclosure of leasing transactions. The amendments will be effective for fiscal years beginning after December 15, 2020, and interim periods within fiscal years beginning after December 15, 2021. Early adoption is permitted. The Company does not expect these amendments to have a material effect on its financial statements.

In June 2018, the FASB amended the Compensation—Stock Compensation Topic of the Accounting Standards Codification. The amendments expand the scope of Topic 718 to include share-based payment transactions for acquiring goods and services from nonemployees. The amendments are effective for fiscal years beginning after December 15, 2019, and interim periods within fiscal years beginning after December 15, 2020. Early adoption is permitted, but no earlier than an entity's adoption date of Topic 606. The Company does not expect these amendments to have a material effect on its financial statements.

In November 2018, the FASB issued guidance to amend the Financial Instruments—Credit Losses topic of the Accounting Standards Codification. The guidance aligns the implementation date of the topic for annual financial statements of nonpublic companies with the implementation date for their interim financial statements. The guidance also clarifies that receivables arising from operating leases are not within the scope of the topic, but rather, should be accounted for in accordance with the leases topic. The amendments will be effective for the Company for fiscal years beginning after December 15, 2021, including interim periods within those fiscal years. Early adoption is permitted for all organizations for periods beginning after December 15, 2018. The Company is currently in the process of evaluating the impact of adoption of this guidance on its financial statements.

In November 2019, the FASB issued guidance to defer the effective dates for private companies, not-for-profit organizations, and certain smaller reporting companies applying standards on current expected credit losses (CECL), and leases. The new effective dates will be; CECL: fiscal years beginning after December 15, 2022 including interim periods within those fiscal years; Leases: fiscal years beginning after December 15, 2020, and interim periods within fiscal years beginning after December 15, 2021. The Company is currently in the process of evaluating the impact of adoption of this guidance on its financial statements.

In November 2019, the FASB issued guidance that addresses issues raised by stakeholders during the implementation of ASU 2016-13, Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments. The amendments affect a variety of Topics in the Accounting Standards Codification. For entities that have not yet adopted the amendments in ASU 2016-13, the amendments are effective for fiscal years beginning after December 15, 2022 including interim periods within those fiscal years. Early adoption is permitted in any interim period as long as an entity has adopted the amendments in ASU 2016-13. The Company does not expect these amendments to have a material effect on its financial statements.

Note 1. Summary of Significant Accounting Policies, Continued

Recently Issued Accounting Pronouncements, continued:

In December 2019, the FASB issued guidance to simplify accounting for income taxes by removing specific technical exceptions that often produce information investors have a hard time understanding. The amendments also improve consistent application of and simplify GAAP for other areas of Topic 740 by clarifying and amending existing guidance. The amendments are effective for fiscal years beginning after December 15, 2021, and interim periods within annual reporting periods beginning after December 15, 2022. Early adoption is permitted. The Company does not expect these amendments to have a material effect on its financial statements.

Other accounting standards that have been issued or proposed by the FASB or other standards-setting bodies are not expected to have a material impact on the Bank's financial position, results of operations or cash flows.

Risks and Uncertainties:

In the normal course of its business, the Bank encounters two significant types of risks: economic and regulatory. There are three main components of economic risk: interest rate risk, credit risk and market risk. The Bank is subject to interest rate risk to the degree that its interest-bearing liabilities mature or reprice at different speeds, or on different basis, than its interest-earning assets. Credit risk is the risk of default on the Bank's loan portfolio that results from a borrower's inability or unwillingness to make contractually required payments. Market risk reflects changes in the value of collateral underlying loans receivable and the valuation of real estate held by the Bank.

The Bank is subject to the regulations of various governmental agencies. These regulations can and do change significantly from period to period. The Bank also undergoes periodic examinations by the regulatory agencies, which may subject it to further changes with respect to asset valuations, amounts of required loss allowances and operating restrictions from the regulators' judgments based on information available to them at the time of their examination.

Note 2. Branch Sale

On June 1, 2018, Sandhills Bank sold one branch in Bethune, South Carolina to First Palmetto Bank. In accordance with the definitive Purchase and Assumption Agreement, dated as of February 16, 2018, by and between Sandhills Bank and First Palmetto Bank (the "P&A Agreement"), the Bank sold approximately $18.49 million of deposits, approximately $6.98 million of performing loans and lines of credit, and the bank facilities and certain other assets and liabilities of the sold branch as of December 31, 2017. In consideration of the sold assets and transferred liabilities, the Bank paid cash of $10,810,246 and recorded a gain on sale of $278,009 for the difference between the cash paid and the net book value of the assets and liabilities sold.

Note 2. Branch Sale, Continued

The following table summarizes the book value of the assets sold and liabilities transferred during the year ended December 31, 2018.

	Bethune
Assets	
Loans, net of unearned income	$ 6,977,822
Premises and equipment, net	402,250
Accrued interest receivable	21,159
Total assets	$ 7,401,231
Liabilities	
Non-interest bearing deposits	$ 2,172,102
Interest bearing demand deposits	4,381,455
Savings and money market deposits	5,812,112
Time deposits - retail	6,117,828
Total deposits	18,483,497
Accrued expenses and other liabilities	5,989
Total liabilities	$ 18,489,486
Cash transferred to complete sale of assets and liabilities	10,810,246
Net gain on sale of assets and liabilities transferred	$ 278,009

Note 3. Cash and Due From Banks

At December 31, 2019 and 2018, the Company was not required to maintain compensating cash balances with its correspondent banks to cover cash letter transactions.

Note 4. Investment Securities

The amortized cost and estimated fair values of securities are summarized below as follows:

Available-for-sale	December 31, 2019			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Mortgage-backed securities	$ 17,943,689	$ 10,286	$ 87,784	$ 17,866,191
Government-sponsored enterprises	1,491,569	-	54,832	1,436,737
Time deposits at other institutions	139,730	591	-	140,231
Total	$ 19,574,988	$ 10,877	$ 142,616	$ 20,716,840

Note 4. Investment Securities, Continued

Available-for-sale	December 31, 2018			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Mortgage-backed securities	$ 5,793,882	$ 29,841	$ 30,670	$ 5,793,053
Obligations of state and local governments	2,750,433	134	55,218	2,695,349
Government-sponsored enterprises	2,552,517	-	86,614	2,465,903
Time deposits at other institutions	1,702,282	-	62,902	1,639,380
Total	$ 12,799,114	$ 29,975	$ 235,404	$ 13,580,635

Other investments at December 31, 2019 and 2018 included Federal Home Loan Bank stock of $602,200 and $455,700, respectively, and stock in two other community banker's banks totaling $531,250 for both of the years then ended.

The amortized cost and market value of investment securities available-for-sale, by contractual maturity, are shown below. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Amortized Cost	Estimated Fair Value
Due after one year but within five years	$ 6,091,930	$ 6,057,077
Due after five years but within ten years	4,010,112	3,955,686
Due after ten years	9,472,946	9,430,396
Total	$ 19,574,988	$ 20,716,840

As of December 31, 2019 and 2018, the Company had no investments pledged to secure deposits and other balances, including borrowings, with the Federal Home Loan Bank.

During the years ended December 31, 2019 and 2018, the Company sold available for sale investments for total proceeds of $13,084,655 and $1,345,312, respectively, resulting in gross gains of $77,477 and $0 and gross losses of $0 and $4,000, respectively.

Note 4. Investment Securities, Continued

The following table shows gross unrealized losses and fair value, aggregated by investment category, and length of time that individual securities have been in a continuous unrealized loss position at December 31, 2019.

	December 31, 2019					
	Less than twelve months		Twelve months or more		Total	
	Fair value	Unrealized losses	Fair value	Unrealized losses	Fair value	Unrealized losses
Mortgage-backed securities	$ 14,660,351	$ 69,616	$ 1,317,707	$ 18,168	$ 15,978,058	$ 87,784
Government-sponsored enterprises	-	-	1,436,737	54,832	1,436,737	54,832
	$ 14,660,351	$ 69,616	$ 2,754,444	$ 73,000	$ 17,414,795	$ 142,616

The following table shows gross unrealized losses and fair value, aggregated by investment category, and length of time that individual securities have been in a continuous unrealized loss position at December 31, 2018.

	December 31, 2018					
	Less than twelve months		Twelve months or more		Total	
	Fair value	Unrealized losses	Fair value	Unrealized losses	Fair value	Unrealized losses
Mortgage-backed securities	$ -	$ -	$ 1,706,835	$ 30,670	$ 1,706,835	$ 30,670
Obligations of state and local governments	228,955	719	2,231,259	54,499	2,460,214	55,218
Government-sponsored enterprises	-	-	2,465,903	86,614	2,465,903	86,614
Time deposits at other Institutions	1,639,380	62,902	-	-	1,639,380	62,902
	$ 1,868,335	$ 63,621	$ 6,403,997	$ 171,783	$ 8,272,332	$ 235,404

Securities classified as available-for-sale are recorded at fair market value. The Company held seven securities at December 31, 2019 in an unrealized loss position greater than twelve months. The Company has the ability and intent to hold these securities until such time as the value recovers or the security matures. The Company believes, based on industry analyst reports and credit ratings, that the deterioration in value is attributable to changes in market interest rates and is not in the credit quality of the issuer and therefore, the loss is not considered other-than-temporary.

Management evaluates securities for other-than-temporary impairment at least on a quarterly basis, and more frequently when economic or market concerns warrant such evaluation. Consideration is given to (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 Company to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value.

Note 4. Investment Securities, Continued

In analyzing an issuer's financial condition, management considers whether the securities are issued by the federal government or its agencies whether downgrades by bond rating agencies have occurred, and industry analysts' reports. As management has the ability to hold debt securities until maturity, or for the foreseeable future if classified as available-for-sale, no declines are deemed to be other-than-temporary.

Note 5. Loans Receivable

Following is a summary of loans by major classification as of December 31:

	2019	2018
Residential real estate	$ 76,540,203	$ 70,612,988
Commercial real estate	57,900,544	47,930,310
Commercial	8,330,886	5,919,828
Consumer	3,601,517	4,464,724
Total loans receivable, gross	146,373,150	128,927,850
Less unearned interest and deferred loan fees	(122,727)	(72,918)
Less fair market value adjustment	(18,876)	(47,192)
Less allowance for loan losses	(1,284,771)	(1,292,675)
Total loans, net	$ 144,946,776	$ 127,515,065

Loans with an unpaid principal balance of $40,215,787 and $24,442,057 as of December 31, 2019 and 2018, respectively, were pledged as collateral for borrowings with the Federal Home Loan Bank, as required or permitted by law.

On August 7, 2015, the Company purchased three branches from Horry County State Bank. The Company recorded a fair value adjustment on the purchased loans of $141,573. Accretion of this discount was $28,316 in the years ended December 31, 2019 and 2018, which is recorded as an adjustment within interest on loans receivable. The remaining discount to be accreted was $18,876 and $47,192 at December 31, 2019 and 2018, respectively.

Note 5. Loans Receivable, Continued

The following is a summary of information pertaining to our allowance for loan losses as of and for the year ending December 31, 2019:

	Residential Real Estate	Commercial Real Estate	Commercial	Consumer	Total
Allowance for loan losses:					
Beginning balance	$ 679,537	$ 494,487	$ 56,762	$ 61,889	$ 1,292,675
Charge-offs	-	-	-	(14,505)	(14,505)
Recoveries	900	-	2,250	3,451	6,601
Provisions	(54,424)	59,198	8,917	(13,691)	-
Ending balance	$ 626,013	$ 553,685	$ 67,929	$ 37,144	$ 1,284,771
Ending balances:					
Individually evaluated for impairment	$ -	$ 82,345	$ -	$ -	$ 82,345
Collectively evaluated for impairment	$ 626,013	$ 471,340	$ 67,929	$ 37,144	$ 1,202,426
Loans receivable:					
Ending balance - total	$ 76,540,203	$ 57,900,544	$ 8,330,886	$ 3,601,517	$ 146,373,150
Ending balances:					
Individually evaluated for impairment	$ 25,016	$ 310,405	$ -	$ -	$ 335,421
Collectively evaluated for impairment	$ 76,515,187	$ 57,590,139	$ 8,330,886	$ 3,601,517	$ 146,037,729

The following is a summary of information pertaining to our allowance for loan losses as of and for the year ending December 31, 2018:

	Residential Real Estate	Commercial Real Estate	Commercial	Consumer	Total
Allowance for loan losses:					
Beginning balance	$ 660,534	$ 494,038	$ 51,685	$ 65,667	$ 1,271,924
Charge-offs	(1,415)	-	-	(16,928)	(18,343)
Recoveries	900	-	3,000	5,194	9,094
Provisions	19,518	449	2,077	7,956	30,000
Ending balance	$ 679,537	$ 494,487	$ 56,762	$ 61,889	$ 1,292,675
Ending balances:					
Individually evaluated for impairment	$ -	$ 35,985	$ -	$ -	$ 35,985
Collectively evaluated for impairment	$ 679,537	$ 458,502	$ 56,762	$ 61,889	$ 1,256,690
Loans receivable:					
Ending balance - total	$ 70,612,988	$ 47,930,310	$ 5,919,828	$ 4,464,724	$ 128,927,850
Ending balances:					
Individually evaluated for impairment	$ 122,975	$ 336,445	$ -	$ -	$ 459,420
Collectively evaluated for impairment	$ 70,490,013	$ 47,593,865	$ 5,919,828	$ 4,464,724	$ 128,468,430

Note 5. Loans Receivable, Continued

Credit Quality Indicators

The Company uses a risk based approach based on the following credit quality measures when analyzing the loan portfolio: pass, weak pass, special mention, substandard, doubtful and classified loss. These indicators are used to rate the credit quality of loans for the purposes of determining the Company's allowance for loan losses.

Grades 1-3 are considered "Pass" - These grades are reserved for loans of sound quality. These loans have excellent sources of repayment, with no significant identifiable risk of collection, and conform in all respects to Bank policy, underwriting guidelines and Federal and State regulations (no exceptions of any kind).

Grades 4-5 are considered "Weak Pass" - These grades are given to acceptable loans with adequate sources of repayment, with little identifiable risk of collection. They may show signs of weakness in either adequate sources of repayment or collateral but have demonstrated mitigating factors that minimize the risk of delinquency or loss.

Grade 6 is considered "Special Mention" - These loans may include some or all of the following characteristics: numerous exceptions and insufficient mitigating factors; currently performing satisfactorily but with potential weaknesses that may, if not corrected, severely weaken the asset or inadequately protect the Bank's position at some future date; loans that have begun to exhibit some signs of delinquency or insufficient capacity to repay evidenced by default; or loans where the Bank has been forced to take special steps to protect the collateral.

Grade 7 is considered "Substandard" - These loans are inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any, and default is typically experienced. Loans classified as substandard have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt; they are characterized by the distinct possibility that the institution will sustain some loss if the deficiencies are not corrected.

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

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

Note 5. Loans Receivable, Continued

The following table lists the loan grades used by the Company as credit quality indicators and the balance in each category.

The following is an analysis of our loan portfolio by credit quality indicators at December 31, 2019:

	Residential Real Estate	Commercial Real Estate	Commercial	Consumer	Total
Grade 1-3	$ 57,642,098	$ 26,707,518	$ 3,654,615	$ 3,332,809	$ 91,337,040
Grade 4-5	16,974,037	28,746,220	4,676,271	268,708	50,665,236
Grade 6	1,924,068	2,111,385	-	-	4,035,453
Grade 7	-	335,421	-	-	335,421
	$ 76,540,203	$ 57,900,544	$ 8,330,886	$ 3,601,517	$ 146,373,150

The following is an analysis of our loan portfolio by credit quality indicators at December 31, 2018:

	Residential Real Estate	Commercial Real Estate	Commercial	Consumer	Total
Grade 1-3	$ 55,915,678	$ 22,668,612	$ 1,735,539	$ 4,119,154	$ 84,438,983
Grade 4-5	14,490,532	24,881,629	4,184,289	345,570	43,902,020
Grade 6	83,803	43,624	-	-	127,427
Grade 7	122,975	336,445	-	-	459,420
	$ 70,612,988	$ 47,930,310	$ 5,919,828	$ 4,464,724	$ 128,927,850

The following is an aging analysis of our loan portfolio at December 31, 2019:

	30 - 59 Days Past Due	60 - 89 Days Past Due	Greater Than 90 Days	Total Past Due	Current	Total Loans Receivable	Recorded Investment >90 Days and Accruing
Residential real estate	$ 963,041	$ 325,471	$ -	$ 1,288,512	$ 75,251,691	$ 76,540,203	$ -
Commercial real estate	951,271	349,868	25,016	1,326,155	56,574,389	57,900,544	25,016
Commercial	-	-	-	-	8,330,886	8,330,886	-
Consumer	-	-	-	-	3,601,517	3,601,517	-
	$ 1,914,312	$ 675,339	$ 25,016	$ 2,614,667	$ 143,758,483	$ 146,373,150	$ 25,016

Note 5. Loans Receivable, Continued

The following is an aging analysis of our loan portfolio at December 31, 2018:

	30 - 59 Days Past Due	60 - 89 Days Past Due	Greater Than 90 Days	Total Past Due	Current	Total Loans Receivable	Recorded Investment >90 Days and Accruing
Residential real estate	$ 235,042	$ -	$ -	$ 235,042	$ 70,377,946	$ 70,612,988	$ -
Commercial real estate	604,037	336,445	-	940,482	46,989,828	47,930,310	-
Commercial	49,980	-	-	49,980	5,869,848	5,919,828	-
Consumer	4,553	-	-	4,553	4,460,171	4,464,724	-
	$ 893,612	$ 336,445	$ -	$ 1,230,057	$ 127,697,793	$ 128,927,850	$ -

The following is an analysis of our impaired loan portfolio detailing the related allowance recorded at December 31, 2019:

	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
With no related allowance needed:					
Residential real estate	$ 25,016	$ 31,862	$ -	$ 29,745	$ -
Commercial real estate	-	-	-	-	-
	25,016	31,862	-	29,745	-
With an allowance recorded:					
Residential real estate	-	-	-	-	-
Commercial real estate	310,405	449,893	82,345	323,425	-
	310,405	449,893	82,345	323,425	-
Total:					
Residential real estate	25,016	31,862	-	29,745	-
Commercial real estate	310,405	449,893	82,345	323,425	-
	$ 335,421	$ 481,755	$ 82,345	$ 353,170	$ -

The following is an analysis of our impaired loan portfolio detailing the related allowance recorded at December 31, 2018:

	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
With no related allowance needed:					
Residential real estate	$ 122,975	$ 163,990	$ -	$ 128,285	$ -
Commercial real estate	-	-	-	-	-
	122,975	163,990	-	128,285	-
With an allowance recorded:					
Residential real estate	-	-	-	-	-
Commercial real estate	336,445	457,378	35,985	350,078	-
	336,445	457,378	35,985	350,078	-
Total:					
Residential real estate	122,975	163,990	-	128,285	-
Commercial real estate	336,445	457,378	35,985	350,078	-
	$ 459,420	$ 621,368	$ 35,985	$ 478,363	$ -

Note 5. Loans Receivable, Continued

The following is an analysis of our nonaccrual loan portfolio recorded at December 31, 2019 and 2018:

	2019	2018
Residential real estate	$ -	$ 122,945
Commercial real estate	310,405	336,445
	$ 310,405	$ 459,390

Troubled Debt Restructurings
The following table summarizes the carrying balance of troubled debt restructurings (TDRs) as of December 31, 2019 and 2018:

	2019	2018
Residential real estate	$ -	$ 122,945
Commercial real estate	310,405	336,445
Total TDRs	$ 310,405	$ 459,390

Loans classified as TDRs may be removed from this status for disclosure purposes after a specified period of time if the restructured agreement specifies an interest rate equal to or greater than the rate that the lender was willing to accept at the time of the restructuring for a new loan with comparable risk, and the loan is performing in accordance with the terms specified by the restructured agreement.

There were no additional loans identified as TDRs during the years ended December 31, 2019 and 2018, nor did any TDRs from prior periods default.

Note 6. Related Party Transactions

Certain parties (principally certain directors and executive officers of the Company, their immediate families and business interests) were loan customers of and had other transactions in the normal course of business with the Bank. Related party loans are made on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with unrelated persons and do not involve more than normal risk of collectability. For the year ended December 31, 2019 and 2018, there were no new loans originated to related parties. There were no outstanding loans to related parties at December 31, 2019. The aggregate dollar amount of loans to related parties was $1,055,000 at December 31, 2018. The Bank was committed to lend an additional $3,000 to these related parties at both December 31, 2019 and 2018.

Deposits for related parties at December 31, 2019 and 2018 amounted to $770,478 and $566,710, respectively.

Note 7. Premises and Equipment

Premises, furniture and equipment is summarized as follows as of December 31:

	2019	2018
Land	$ 7,512,257	$ 7,344,792
Buildings	8,841,918	7,259,654
Furniture and equipment	3,349,270	2,985,635
Construction in progress	37,041	2,072,274
	19,740,486	19,662,355
Less accumulated depreciation	(3,592,760)	(3,104,827)
Premises and equipment, net	$ 16,147,726	$ 16,557,528

Depreciation expense for the years ended December 31, 2019 and 2018 was $623,258 and $636,979, respectively.

Note 8. Other Real Estate Owned

Activity in other real estate owned is summarized as follows for the years ended December 31:

	2019	2018
Balance, beginning of year	$ 130,000	$ 850,756
Additions	-	-
Sales	(100,000)	(678,219)
Writedowns	(30,000)	(42,537)
Balance, end of year	$ -	$ 130,000

There were no consumer mortgage loans secured by residential real estate in the process of foreclosure for the years ended December 31, 2019 and 2018.

Note 9. Core Deposit Intangible

The following is a summary of the gross carrying amount and accumulated amortization of an amortizing intangible asset as of December 31, 2019 and 2018. The Bank recorded a core deposit premium intangible in 2015 of $351,117 in connection with the acquisition of three Horry County State Bank branches. This asset is being amortized on a straight line basis over the estimated life of the related deposits of 7 years.

	December 31, 2019		December 31, 2018	
	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Amortizing intangible assets:				
Core deposit intangible	$ 351,117	$ 251,238	$ 351,117	$ 201,078

Amortization expense totaled $50,160 for both years ended December 31, 2019 and 2018.

Note 9. Core Deposit Intangible, Continued

The following table presents the estimated remaining amortization expense for intangible assets. These estimates are subject to change in future periods to the extent management determines it is necessary to make adjustments to the carrying value or estimated useful lives of amortizing intangible assets.

2020	$ 50,160
2021	38,867
2022	10,852
	$ 99,879

Note 10. Deposits

At December 31, 2019, the scheduled maturities of time deposits are as follows:

2020	$ 65,779,614
2021	11,440,744
2022	3,995,536
2023	2,613,664
2024	1,613,119
	$ 85,442,677

Time deposits that met or exceeded the FDIC Insurance limit of $250,000 as of December 31, 2019 and 2018 were $18,857,432 and $12,891,297, respectively. Interest expense on these deposits was $269,994 in 2019 and $171,911 in 2018.

The amount of overdrafts classified as loans at December 31, 2019 and 2018 was $13,436 and $61,612, respectively.

The Company had brokered deposits totaling $750,000 as of December 31, 2019. The Company had brokered deposits totaling $10,000,000 as of December 31, 2018.

Note 11. Borrowings

Subordinated debt:

On July 31, 2015, the Company entered into a subordinated debt agreement that totaled $8,500,000. The debt initially bore interest at a fixed rate of 8.75% per annum payable quarterly in arrears on January 1st, April 1st, July 1st and October 1st. Once the issuer securitized this debt with other community bank subordinated debt, the interest rate reduced to a fixed rate of 7.25% on October 15, 2015. The Company may not prepay the debt for five years after issuance and the debt matures on July 31, 2025. The subordinated debt has been structured to fully count as Tier 2 regulatory capital on a consolidated basis. The subordinated debt balance as of December 31, 2019 and 2018 was $8,349,753 and $8,322,843, respectively.

Issuance costs associated with the debt are netted against the debt outstanding. The costs are being amortized over ten years. The unamortized balance of issuance costs totaled $150,247 and $177,157 at December 31, 2019 and 2018, respectively.

Note 11. Borrowings, Continued

Federal Home Loan Bank (FHLB) advances:

Advances from the FHLB consisted of the following at December 31, 2019 and 2018:

Description	Current Interest Rate	2019 Balance	2018 Balance
Fixed rate advances maturing:			
June 14, 2019	1.11%	$ -	$ 5,000,000
March 2, 2020	1.69%	3,000,000	-
May 1, 2020	1.70%	2,000,000	-
July 23, 2021	1.90%	5,500,000	-
		$ 10,500,000	$ 5,000,000

Loans with an unpaid principal balance of $40,215,787 and $24,442,057 as of December 31, 2019 and 2018, respectively, were pledged as collateral for borrowings with the FHLB, as required or permitted by law.

Each of the advances are subject to early termination options. The FHLB reserves the right to terminate each agreement at a date prior to maturity.

Note 12. Shareholder's Equity

During 2018, the Company initiated a capital raise whereby 303,330 shares of common stock were issued at ranges between $10.54 and $10.91 per share for net proceeds of $2,748,773. Costs associated with the capital raise totaled $339,507, and are netted against proceeds received within the statement of shareholders' equity.

Note 13. Benefit Plans

The Company has a 401(k) plan covering substantially all employees. The plan provides for an employer match up to 50% of the employee's contribution up to 3% of compensation. The Company's expense related to the matching contributions of the 401(k) plan amounted to $128,738 and $115,814 for the years ended December 31, 2019 and 2018, respectively and is included in salaries and employee benefit expense.

The Company has a deferred compensation plan for one current director. The plan provides for set payments for a period of 10 years after the beneficiaries have reached the age of sixty-five. The individual that participates in the plan is fully vested in the plan. The liability recorded for the plan at December 31, 2019 and 2018 was $53,345 and $67,694, respectively and is included in other liabilities.

Note 14. Other Expenses

A summary of the components of other operating expense is as follows for the years ended December 31, 2019 and 2018:

	2019	2018
Loan expenses	$ 94,883	$ 104,806
FDIC insurance	41,056	119,044
Examination fees	40,942	38,738
Staff and directors expenses	140,619	123,124
Data processing and networking	344,960	340,180
ATM expense	158,476	160,437
Internet banking	114,870	107,636
Information technology services	111,165	95,475
Telephone, postage, and supplies	107,613	104,060
Custodial and landscaping services	79,449	92,951
Marketing and business development	158,723	97,548
Other expenses	340,207	393,928
Total	$ 1,732,963	$ 1,777,927

Note 15. Unused Lines of Credit

At December 31, 2019 and 2018, the Bank had unused lines of credit with other financial institutions totaling $9,800,000 for each of the years then ended. In order to use these lines of credit, two financial institutions require $250,000 and $175,000, respectively, of deposit balances maintained at their institution. At December 31, 2019, the Company met both of those requirements.

The Bank also has a line of credit to borrow funds from the Federal Home Loan Bank for up to $49,000,000 as of December 31, 2019. As of December 31, 2019 and 2018, the Bank had borrowings on this line of $10,500,000 and $5,000,000, respectively.

Note 16. Income Taxes

Income tax expense is summarized as follows for the years ended December 31:

	2019	2018
Current income tax expense (benefit):		
Federal	$ (1,925)	$ (3,953)
State	28,509	37,624
Total current	26,584	33,671
Deferred income tax expense (benefit):		
Federal	39,737	69,763
State	(28,882)	(27,956)
Total deferred	10,885	41,807
Change in valuation allowance	28,882	27,956
Total income tax expense	$ 66,321	$ 103,434

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

	2019	2018
Deferred tax assets:		
Other real estate owned	$ -	$ 8,933
Net operating losses	4,534,687	4,533,932
Interest on nonaccrual loans	8,976	9,033
Deferred compensation	11,202	14,216
Unrealized loss on available for sale securities	32,349	50,443
Mark-to-market purchase accounting	31,459	25,841
Other	7,408	12,344
Gross deferred tax assets	4,626,081	4,654.742
Less, valuation allowance	(456,642)	(427,760)
Net deferred tax assets	4,169,439	4,226,982
Deferred tax liabilities:		
Accumulated depreciation	419,517	428,773
Goodwill	41,356	31,812
Allowance for loan losses	270,986	270,986
Total deferred tax liabilities	731,859	731,571
Net deferred tax asset	$ 3,437,580	$ 3,495,411

Deferred tax assets represent the future tax benefit of deductible differences and, if it is more likely than not that a tax asset will not be realized, a valuation allowance is required to reduce the net deferred tax assets to net realizable value. As of December 31, 2019 and 2018, we had a net deferred tax asset of approximately $3.4 million and $3.5 million, respectively, of which, approximately $4.5 million and $4.5 million, respectively, are due to accumulated net operating losses.

Note 16. Income Taxes, Continued

We record a valuation allowance to reduce deferred tax assets to an amount that we believe is more likely than not to be realized. Because of expected future taxable income, we have not recorded a valuation allowance to reduce our net deferred tax asset as of December 31, 2019, other than establishing such allowances related to the parent company's state operating loss carryforwards, for which realizability is uncertain. We regularly evaluate the likelihood that we will be able to realize our deferred tax assets and the continuing need for a valuation allowance. At December 31, 2019 and 2018, we determined, based on all available positive and negative evidence, that it is more-likely-than-not that future taxable income will be available during the carryforward periods to absorb all of the unreserved federal and state net operating loss carryforwards. A number of factors played a critical role in this determination, including:

- Our trend of profitability and utilization of past NOL carryforwards,
- Reasonable forecasts of future taxable income, and
- A tax planning strategy to change our tax accounting method for bad debts.

The Company has federal net operating losses of $19,445,291 as of December 31, 2019. These federal losses begin to expire in 2029. The Company has state net operating losses of $11,486,257 for the year ended December 31, 2019. These state losses begin to expire in 2029.

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

A reconciliation between the income tax expense and the amount computed by applying the Federal statutory rate of 21% to income before income taxes follows for the years ended December 31, 2019 and 2018:

	2019	2018
Tax benefit at statutory rate	$ 44,562	$ 80,831
State income tax, net of federal benefit	(295)	7,638
Tax exempt interest	(2,281)	(9,123)
Valuation allowance	28,883	27,956
Cash surrender value of life insurance	(2,517)	(1,877)
Other	(2,030)	(1,991)
Income tax expense	$ 66,321	$ 103,434

Tax returns for 2016 and subsequent years are subject to examination by taxing authorities.

Note 17. Financial Instruments With Off-Balance-Sheet Risk

In the normal course of business, the Bank has outstanding commitments and contingent liabilities, such as commitments to extend credit and standby letters of credit, which are not included in the accompanying consolidated financial statements. The Bank's exposure to credit loss in the event of nonperformance by the other party to the financial instruments for commitments to extend credit and standby letters of credit is represented by the contractual or notional amount of those instruments. The Bank uses the same credit policies in making such commitments as it does for instruments that are included in the consolidated balance sheet.

Financial instruments whose contract amount represents credit risk were as follows at December 31:

	2019	2018
Commitments to extend credit	$ 9,537,240	$ 9,650,524
Standby letters of credit and other	413,485	413,485

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 of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Bank evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Bank upon extension of credit, is based on management's credit evaluation. Collateral held varies but may include accounts receivable, inventory, property and equipment, and income-producing commercial properties.

Standby letters of credit are conditional lending commitments issued by the Bank to guarantee the performance of a customer to a third party. Standby letters of credit generally have fixed expiration dates or other termination clauses and may require payment of a fee. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. The Bank's policy for obtaining collateral, and the nature of such collateral, is essentially the same as involved in making commitments to extend credit.

Note 18. Fair Value of Financial Instruments

Accounting standards require disclosures about the fair value of assets and liabilities recognized in the balance sheet in periods subsequent to initial recognition, whether the measurements are made on a recurring basis (for example, available-for-sale investment securities) or on a nonrecurring basis (for example, impaired loans).

The accounting standard defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. It also establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair value:

Level 1 Quoted market prices in active markets for identical assets or liabilities. Level 1 assets and liabilities include debt and equity securities and derivative contracts that are traded in an active exchange market, as well as U.S. Treasuries, and money market funds.

Note 18. Fair Value of Financial Instruments, Continued

Level 2 Observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities. Level 2 assets and liabilities include debt securities with quoted prices that are traded less frequently than exchange-traded instruments, mortgage-backed securities, municipal bonds, corporate debt securities, and derivative contracts whose value is determined using a pricing model with inputs that are observable in the market or can be derived principally from or corroborated by observable market data.

Level 3 Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation.

Following is a description of valuation methodologies used for assets and liabilities recorded at fair value on a recurring and nonrecurring basis:

Investment Securities Available-for-Sale: Investment securities available for sale are recorded at fair value on a recurring basis. Fair value measurement is based upon quoted prices, if available. If quoted prices are not available, fair values are measured using independent pricing models or other model-based valuation techniques such as the present value of future cash flows, adjusted for the security's credit rating, prepayment assumptions and other factors such as credit loss assumptions. Level 1 securities include those traded on an active exchange such as the New York Stock Exchange, Treasury securities that are traded by dealers or brokers in active over-the counter markets and money market funds. Level 2 securities include mortgage backed securities issued by government sponsored entities, municipal bonds and corporate debt securities. Securities classified as Level 3 include asset-backed securities in less liquid markets.

Loans: Loans that are considered impaired are recorded at fair value on a non-recurring basis. Once a loan is considered impaired, the fair value is measured using one of several methods, including collateral liquidation value, market value of similar debt and discounted cash flows. Those impaired loans not requiring a specific charge against the allowance represent loans for which the fair value of the expected repayments or collateral meet or exceed the recorded investment in the loan. All impaired loans are reviewed for fair value on a nonrecurring basis and are considered Level 3 assets.

Mortgage Loans Held for Sale - Mortgage loans held for sale are comprised of loans originated for sale in the ordinary course of business. The fair value of mortgage loans originated for sale in the secondary market is based on purchase commitments or quoted prices for the same or similar loans and are classified as recurring Level 2.

Other Real Estate Owned (OREO): Other real estate owned is adjusted to fair value upon transfer of the loans to foreclosed assets. Subsequently, other real estate owned is carried at the lower of carrying value or fair value. Fair value is based upon independent market prices, appraised values of the collateral or management's estimation of the value of the collateral. All OREO is reviewed for fair value on a nonrecurring basis and is considered a Level 3 asset.

Note 18. Fair Value of Financial Instruments, Continued

The tables below present the balances of assets and liabilities measured at fair value on a recurring basis by level within the hierarchy.

	December 31, 2019			
	Total	Level 1	Level 2	Level 3
Mortgage-backed securities	$ 17,866,191	$ -	$ 17,866,191	$ -
Government-sponsored enterprises	1,436,737	-	1,436,737	
Mortgage loans held for sale	158,629	-	158,629	-
Total	$ 19,461,557	$ -	$ 19,461,557	$ -

	December 31, 2018			
	Total	Level 1	Level 2	Level 3
Mortgage-backed securities	$ 5,793,053	$ -	$ 5,793,053	$ -
Obligations of state and local governments	2,695,349	-	2,695,349	-
Government-sponsored enterprises	2,465,903	-	2,465,903	-
Mortgage loans held for sale	293,888	-	293,888	-
Total	$ 11,248,193	$ -	$ 11,248,193	$ -

Certain assets and liabilities are measured at fair value on a nonrecurring basis; that is, the instruments are not measured at fair value on an ongoing basis but are subject to fair value adjustments in certain circumstances (for example, when there is evidence of impairment). The following table presents the assets and liabilities carried on the balance sheet by caption and by level within the valuation hierarchy (as described above) as of December 31, 2019 and 2018 for which a nonrecurring change in fair value has been recorded during the years ended December 31, 2019 and 2018.

	December 31, 2019			
	Total	Level 1	Level 2	Level 3
Impaired loans, net:				
Residential real estate	$ 25,016	$ -	$ -	$ 25,016
Commercial real estate	228,060	-	-	228,060
Total impaired loans	253,076	-	-	253,076
Total	$ 253,076	$ -	$ -	$ 253,076

Note 18. Fair Value of Financial Instruments, Continued

	December 31, 2018			
	Total	Level 1	Level 2	Level 3
Other real estate owned	$ 130,000	$ -	$ -	$ 130,000
Impaired loans, net:				
Residential real estate	122,975	-	-	122,975
Commercial real estate	300,460	-	-	300,460
Total impaired loans	423,435	-	-	423,435
Total	$ 553,435	$ -	$ -	$ 553,435

For level 3 assets and liabilities measured at fair value on a recurring or non-recurring basis, the significant unobservable inputs used in the fair value measurements were as follows as of December 31, 2019 and 2018.

	Fair Value at December 31, 2019	Valuation Technique	Significant Unobservable Inputs	Range
Collateral dependent impaired loans, net	$253,076	Appraised value	Discount rates/discounts to appraised value	Appraisals discounted 6-10% for sales commissions and other holding costs

	Fair Value at December 31, 2018	Valuation Technique	Significant Unobservable Inputs	Range
Collateral dependent impaired loans, net	$423,435	Appraised value	Discount rates/discounts to appraised value	Appraisals discounted 6-10% for sales commissions and other holding costs
Other real estate owned	$130,000	Appraised value/comparable sales	Discount rates/discounts to appraised value	Appraisals discounted 6-10% for sales commissions and other holding costs

Note 19. Commitments and Contingencies

The Company is subject to claims and lawsuits which arise primarily in the ordinary course of business. Management is not aware of any legal proceedings, which would have a material adverse effect on the financial position or operating results of the Company.

Note 20. Capital Requirements and Regulatory Matters

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

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum ratios (set forth in the table below) of Tier 1, Common Equity Tier 1 (CET1), and total capital as a percentage of assets and off-balance-sheet exposures, adjusted for risk-weights ranging from 0% to 150%. Tier 1 capital of the Bank consists of common stockholders' equity, excluding the unrealized gain or loss on securities available-for-sale, minus certain intangible assets, while CET1 is comprised of Tier 1 capital, adjusted for certain regulatory deductions and limitations. Tier 2 capital consists of the allowance for loan losses subject to certain limitations. Total capital for purposes of computing the capital ratios consists of the sum of Tier 1 and Tier 2 capital.

The Bank is also required to maintain capital at a minimum level based on average assets (as defined), which is known as the leverage ratio. Only the strongest institutions are allowed to maintain capital at the minimum requirement. All others are subject to maintaining ratios 1% to 2% above the minimum.

Effective March 31, 2015, quantitative measures established by applicable regulatory standards, including the newly implemented Basel III revised capital adequacy standards and relevant provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd Frank Act"), require the Bank to maintain (i) a minimum ratio of Tier 1 capital to average total assets, after certain adjustments, of 4.00%, (ii) a minimum ratio of Tier 1 capital to risk-weighted assets of 6.00%, (iii) a minimum ratio of total-capital to risk-weighted assets of 8.00% and (iv) a minimum ratio of CET1 to risk-weighted assets of 4.50%. A "well-capitalized" institution must generally maintain capital ratios 2% higher than the minimum guidelines.

In order to avoid restrictions on capital distributions or discretionary bonus payments to executives, the Bank is required to maintain a "capital conservation buffer" in addition to its minimum risk-based capital requirements. This buffer is required to consist solely of CET1, but the buffer applies to all three risk-based measurements (CET1, Tier 1 and total capital). The capital conservation buffer was phased in incrementally over time, beginning January 1, 2016 at 0.625% and became fully effective on January 1, 2019. The capital conservation buffer consists of an additional amount of Tier 1 capital equal to 2.50% of risk-weighted assets, which was in effect for the year ended December 31, 2019.

Note 20. Capital Requirements and Regulatory Matters, Continued

As of December 31, 2019 and 2018, the most recent notification from the FDIC, the Bank was categorized as well capitalized under the regulatory framework for prompt corrective action. To remain categorized as well capitalized, the Bank will have to maintain minimum total risk-based, Tier 1 risk-based, and Tier 1 leverage ratios as disclosed in the table below. There are no conditions or events since the most recent notification that management believes have changed the Bank's prompt corrective action category.

The following table summarizes the capital ratios and the regulatory minimum requirements of the Bank.

(Dollars in thousands)	Actual		For Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Corrective Action Provisions	
December 31, 2019	**Amount**	**Ratio**	**Amount**	**Ratio**	**Amount**	**Ratio**
The Bank						
Total capital (to risk-weighted assets)	$ 18,778	14.19%	$ 10,590	8.00%	$ 13,238	10.00%
Tier 1 capital (to risk-weighted assets)	17,493	13.21%	7,943	6.00%	10,590	8.00%
Tier 1 capital (to average assets)	17,493	9.08%	7,709	4.00%	9,636	5.00%
Common Equity Tier 1 Capital (to risk-weighted assets)	17,493	13.21%	5,957	4.50%	8,605	6.50%
December 31, 2018						
The Bank						
Total capital (to risk-weighted assets)	$ 18,566	15.64%	$ 9,499	8.00%	$ 11,874	10.00%
Tier 1 capital (to risk-weighted assets)	17,273	14.55%	7,125	6.00%	9,499	8.00%
Tier 1 capital (to average assets)	17,273	10.04%	6,880	4.00%	8,600	5.00%
Common Equity Tier 1 Capital (to risk-weighted assets)	17,273	14.55%	5,343	4.50%	7,718	6.50%

Note 21. Sandhills Holding Company and Subsidiaries (Parent Company Only)

Following is condensed financial information of Sandhills Holding Company (Parent Company Only) as of and for the years ended December 31:

Condensed Balance Sheets

	December 31,	
	2019	2018
Assets		
Cash and due from banks	$ 134,466	$ 190,213
Investment in subsidiaries	20,208,175	20,139,554
Premises and equipment, net	106,780	152,174
Deferred tax asset	1,339,644	1,186,100
Other assets	23,649	23,373
Total assets	$ 21,812,714	$ 21,691,414
Liabilities and Shareholders' Equity		
Liabilities:		
Subordinated debt	$ 8,349,753	$ 8,322,843
Other liabilities	10,500	125,731
Total liabilities	8,360,253	8,448,574
Shareholders' equity	13,452,461	13,242,840
Total liabilities and shareholders' equity	$ 21,812,714	$ 21,691,414

Condensed Statements of Income

	For the years ended December 31,	
	2019	2018
Income:		
Dividends from Bank subsidiary before equity in undistributed net income of Bank subsidiary	$ 705,000	$ 700,000
Equity in undistributed earnings of subsidiaries	14,647	139,341
(Loss) gain on sale of other assets	(5,963)	47,242
Total income	713,684	886,583
Expense:		
Interest expense	651,719	651,719
Other expense	73,483	101,682
Total expense	725,202	753,401
(Loss) Income before income taxes	(11,518)	133,182
Income tax benefit	(157,396)	(148,294)
Net income	$ 145,878	$ 281,476

Note 21. Sandhills Holding Company and Subsidiaries (Parent Company Only), Continued

Condensed Statements of Cash Flows

	For the years ended December 31, 2019	2018
Operating activities		
Net income	$ 145,878	$ 281,476
Adjustments to reconcile net cash used in operating activities		
Depreciation	34,527	37,659
Equity in undistributed earnings of subsidiary	(719,647)	(839,341)
Amortization of subordinated debt issuance costs	26,910	26,910
Increase in deferred tax asset	(153,544)	(148,294)
Loss (gain) on sale of premises and equipment	5,963	(47,242)
Other, net	(115,507)	125,379
Net cash used in operating activities	(775,420)	(563,453)
Cash flows from investing activities		
Dividends received from subsidiary	705,000	700,000
Purchase of premises and equipment, net	-	(93,620)
Capital contribution to subsidiary	-	(2,605,800)
Proceeds from sale of premises and equipment	6,525	-
Net cash provided by (used in) investing activities	711,525	(1,999,420)
Cash flows from financing activities		
Proceeds from issuance of common stock	8,148	2,748,773
Net cash provided by financing activities	8,148	2,748,773
(Decrease) increase in cash	(55,747)	185,900
Cash and cash equivalents, beginning of year	190,213	4,313
Cash and cash equivalents, end of year	$ 134,466	$ 190,213

Note 22. Subsequent Events

Subsequent events are events or transactions that occur after the balance sheet date but before financial statements are issued. Recognized subsequent events are events or transactions that provide additional evidence about conditions that existed at the date of the balance sheet, including the estimates inherent in the process of preparing financial statements. Nonrecognized subsequent events are events that provide evidence about conditions that did not exist at the date of the balance sheet but arose after that date. Management has reviewed events occurring through March 6, 2020, the date the financial statements were available to be issued and no subsequent events occurred requiring accrual or disclosure.