UNITED STATES SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549
FORM 10-K

[X] Annual Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

or

[ ] Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the fiscal year ended December 31, 2008

Commission file number: 0-23090

Carrollton Bancorp
(Exact Name of Registrant as Specified in its Charter)

Maryland	52 1660951
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
344 N. Charles St. Baltimore, MD	21201
(Address of principal executive offices)	(Zip Code)
(410) 536 4600	
(Registrant's telephone number, including area code)	

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

None

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

Common Stock,
par value $1.00 per share

(Title of class)

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

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

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☒ No ☐

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K ☐.

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

Large accelerated filer ☐ Accelerated filer ☐ Non-accelerated filer ☐ (Do not check box if a smaller reporting company) Smaller reporting company ☒

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

The aggregate market value of the Common Stock, all of which has voting rights, held by non-affiliates of the registrant upon the closing price of such common equity as of the last business day of the most recently completed second fiscal quarter was approximately $30.3 million. For the purpose of this calculation, directors and executive officers of the registrant are considered affiliates.

At March 3, 2009, the Registrant had 2,564,988 shares of $1.00 par value common stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Proxy Statement for Annual Meeting of Shareholders to be held on May 12, 2009, are incorporated by reference in Part III of this Form 10-K.

TABLE OF CONTENTS

FORWARD-LOOKING STATEMENTS

This Annual Report on Form 10-K and certain information incorporated herein by reference contain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. All statements included or incorporated by reference in this Annual Report on Form 10-K, other than statements that are purely historical, are forward-looking statements. Statements that include the use of terminology such as "anticipates," "expects," "plans," "believes," "estimates" and similar expressions also identify forward-looking statements. The forward-looking statements are based on Carrollton Bancorp's current intent, belief and expectations. Forward-looking statements in this Annual Report on Form 10-K include, but are not limited to:

Part I. Item 3. Legal Proceedings:

Statement regarding the impact on the Company of routine legal proceedings.

Part II. Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations:

Statements regarding loan growth in real estate development and construction and commercial loan portfolios in 2009.

Statement regarding 2009 certificate of deposit pricing strategy.

Statement regarding challenges facing management in terms of interest rates, growth in net interest income and overall management of the net interest margin.

Statements regarding volatility in mortgage refinancing activity.

Part III. Item 7A. Quantitative and Qualitative Disclosures About Market Risk:

Statements regarding the Company's ability to limit exposure to interest rate risk.

Statements regarding factors that influence demand for real estate loans.

Statements regarding future revenue improvements.

Statements regarding the sufficiency of the Company's allowance for loan losses.

Part IV. Item 8. Note 3. Investments:

Statement regarding anticipated changes in the fair value of securities in relation to market rates.

These statements are not guarantees of future performance and are subject to certain risks and uncertainties that are difficult to predict. Actual results may differ materially from these forward-looking statements because of interest rate fluctuations, a deterioration of economic conditions in the Baltimore/ Washington metropolitan area, a downturn in the real estate market, losses from impaired loans, an increase in nonperforming assets, potential exposure to environmental laws, changes in federal and state bank laws and regulations, the highly competitive nature of the banking industry, a loss of key personnel, changes in accounting standards and other risks described in the Company's filings with the Securities and Exchange Commission. Existing and prospective investors are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date of this Report. Carrollton Bancorp undertakes no obligation to update or revise the information contained in this Annual Report whether as a result of new information, future events or circumstances, or otherwise. Past results of operations may not be indicative of future results.

PART I

ITEM 1: BUSINESS

General. – Carrollton Bancorp, a Maryland corporation (the "Company"), a bank holding company registered under the Bank Holding Company Act of 1956, as amended, was organized on January 11, 1990, and is headquartered in Baltimore, Maryland. Carrollton Bank (the "Bank") is a commercial bank and the principal subsidiary of the Company. The Bank was chartered by an act of the General Assembly of Maryland (Chapter 727) approved April 10, 1900. The Bank is engaged in a general commercial and retail banking business and, as of December 31, 2008, had a total of ten branch locations in Maryland with two branch locations in Baltimore City; three branch locations in Anne Arundel County; four branches in Baltimore County and one branch in Harford County. The Bank's wholly owned subsidiaries are Carrollton Mortgage Services, Inc. ("CMSI"), which is used primarily to originate and sell residential mortgage loans, Carrollton Financial Services, Inc. ("CFS"), which provides brokerage services, and Mulberry Street LLC ("MSLLC") which is used to dispose of other real estate owned. Carrollton Community Development Corporation ("CCDC") is a 96.4% owned subsidiary of the Bank which promotes, develops and improves the housing and economic conditions of people in Maryland, particularly the Metropolitan Baltimore area.

The Bank is an independent, community bank that seeks to provide personal attention and professional financial services to its customers while offering virtually all of the banking services of larger competitors. Our customers are primarily individuals and small and medium-sized businesses. The Bank's business philosophy includes offering informed and courteous service, local and timely decision-making, flexible and reasonable operating procedures and consistently applied credit policies.

On or around March 23, 2009, the executive offices of the Company and the principal office of the Bank will be relocated to 7151 Columbia Gateway Drive, Suite A, Columbia, Maryland 21046, telephone number (410) 312-5400. The Company files quarterly and annual reports with the Securities and Exchange Commission ("SEC") on forms 10-Q and 10-K, respectively, proxy materials on Schedule 14A and current reports on Form 8-K. The Company makes available, free of charge, all of these reports, as well as any amendments, through the Company's Internet site as soon as is reasonably practicable after they are filed electronically with the SEC. The address of that site is *http://www.carrolltonbank.com*. To access the SEC reports, click on *"About Us" —"SEC Filings"*. The SEC also maintains an internet site that contains reports, proxy materials and information statements at *http://sec.gov*. In addition, the Company will provide paper copies of filings free of charge upon written request.

Recent Market Developments. – In response to the financial crises affecting the banking system and financial markets and going concern threats to investment banks and other financial institutions, on October 3, 2008, the Emergency Economic Stabilization Act of 2008 (the "EESA") was signed into law. Pursuant to the EESA, the U.S. Treasury was given the authority to, among other things, purchase up to $700 billion of mortgages, mortgage-backed securities and certain other financial instruments from financial institutions for the purpose of stabilizing and providing liquidity to the U.S. financial markets.

On October 14, 2008, the Secretary of the Department of the Treasury announced that the Department of the Treasury will purchase equity stakes in a wide variety of banks and thrifts. Under the program, known as the Troubled Asset Relief Program Capital Purchase Program (the "TARP Capital Purchase Program"), from the $700 billion authorized by the EESA, the Treasury made $250 billion of capital available to U.S. financial institutions in the form of preferred stock. In conjunction with the purchase of preferred stock, the Treasury received, from participating financial institutions, warrants to purchase common stock with an aggregate market price equal to 15% of the preferred investment. Participating financial institutions were required to adopt the Treasury's standards for executive compensation and corporate governance for the period during which the Treasury holds equity issued under the TARP Capital Purchase Program. On February 13, 2009, the Company raised $9,201,000 through participation in the TARP Capital Purchase Program.

The Company issued 9,201 shares of Fixed Rate Cumulative Perpetual Preferred Stock, Series A, liquidation preference $1,000 per share (the "Series A Preferred Stock"), and a warrant to purchase 205,379 shares of the Company's common stock, par value $1.00 per share. The warrant is exercisable at $6.72 per share at any time on or before February 13, 2019. Treasury has agreed not to exercise voting power with respect to any shares of common stock issued upon exercise of the warrant.

On November 21, 2008, the Board of Directors of the Federal Deposit Insurance Corporation ("FDIC") adopted a final rule relating to the Temporary Liquidity Guarantee Program ("TLG Program"). The TLG Program was announced by the FDIC on October 14, 2008, preceded by the determination of systemic risk by the Secretary of the Department of Treasury (after consultation with the President), as an initiative to counter the system-wide crisis in the nation's financial sector. Under the TLG Program the FDIC will (i) guarantee, through the earlier of maturity or June 30, 2012, certain newly issued senior unsecured debt issued by participating institutions on or after October 14, 2008, and before June 30, 2009 and (ii) provide full FDIC deposit insurance coverage for non-interest bearing transaction deposit accounts, Negotiable Order of Withdrawal

(“NOW”) accounts paying less than 0.5% interest per annum and Interest on Lawyers Trust Accounts (“IOLTA”) accounts held at participating FDIC insured institutions through December 31, 2009. Coverage under the TLG Program was available for the first 30 days without charge. The fee assessment for coverage of senior unsecured debt ranges from 50 basis points to 100 basis points per annum, depending on the initial maturity of the debt. The fee assessment for deposit insurance coverage is 10 basis points per quarter on amounts in covered accounts exceeding $250,000. On November 25, 2008, the Company elected to participate in the deposit insurance coverage for non-interest bearing transaction deposit accounts. On December 10, 2008, the Company declined to participate in the senior unsecured debt program.

Description of Services. – The Bank provides a broad range of consumer and commercial banking products and services to individuals, businesses, professionals and governments. The services and products have been designed in such a manner as to appeal to consumers and business principals.

The following is a partial listing of the types of services and products that the Bank offers:

- Commercial loans for businesses, including those for working capital purposes, equipment purchases and accounts receivable and inventory financing.
- Commercial and residential real estate loans for acquisition, refinancing and construction.
- Consumer loans including automobile loans, home equity loans and lines of credit.
- Loans guaranteed by the United States Small Business Administration.
- Money market deposits, demand deposits, NOW accounts, savings accounts and certificates of deposit.
- Internet banking, including electronic bill payment.
- Letters of credit and remittance services.
- Credit and debit card services.
- Merchant credit card deposit servicing.
- Brokerage services for stocks, bonds, mutual funds and annuities.
- A 24-hour ATM network.
- After-hours depository services.
- Safe deposit boxes.
- Other services, such as direct deposit, traveler’s checks and IRAs.

Customer service hours for the Bank are competitive with other institutions in the market area. The Bank also acts as a reseller of services purchased from third party vendors for customers requiring services not offered directly by the Bank.

Lending Activities. – The Bank makes various types of loans to borrowers based on, among other things, an evaluation of the borrowers’ net asset value, cash flow, security and ability to repay. Loans to consumers include home mortgage loans, home equity lines of credit, home improvement loans, overdraft lines of credit, and installment loans for automobiles, boats and recreational vehicles. The Bank also makes loans secured by deposit accounts and common stocks. The Bank’s commercial loan product line includes commercial mortgage loans, time and demand loans, lines and letters of credit, and acquisition, development and construction financing. The Notes to the Consolidated Financial Statements contained in Part II, Item 8 report the classification by type of loan for the whole portfolio.

First and second residential mortgage loans, made principally through the Bank’s subsidiary, CMSI, enable customers to purchase or refinance residential properties. These loans are secured by liens on the residential property. All first mortgage loans with a loan to value ratio greater than 80% have private mortgage insurance coverage equal to or greater than the amount required under the Federal National Mortgage Association guidelines. Residential loans are considered comparatively low risk based on the type of collateral (residential property) and the underwriting standards used. The Bank experienced $423,687 of losses and $4,358 in recoveries on residential mortgage loans in 2008. The Bank experienced $76,426 of losses and no recoveries on residential mortgage loans in 2007. The Bank experienced no losses and no recoveries in 2006. There were approximately $877,000 of residential mortgage loans delinquent more than 90 days at December 31, 2008.

Home equity lines of credit are typically second mortgage loans (sometimes first mortgages) secured by the borrower’s primary residence structured as a revolving borrowing line with a maximum loan amount. Customers write checks to access the line. Generally, the Bank has a second lien on the property behind the first mortgage lien holder. The Bank has a number of different equity loan products that it offers. Borrowers can choose between fixed rate loans or loans tied to the prime rate with margins ranging from 0% to 1.5%. The Bank will finance up to 90% of the value of the home in combination with the first mortgage loan balance, depending on the rate and program. Home equity loans carry a higher level of risk than first mortgage residential loans because of the second lien position on the property, and because a higher loan to value ratio is used in the underwriting of the loan. However, the overall risk of loss on home equity loans is also considered comparatively low due to the underlying values of the collateral. The Bank experienced losses on home equity loans of $75,000 during 2008, $100,455 during 2007 and none during 2006. The Bank experienced no recoveries on home equity loans during 2008, 2007 and 2006. There were approximately $199,000 of home equity loans delinquent more than 90 days at December 31, 2008**.**

Commercial and investment mortgage loans are first mortgage loans made to individuals or to businesses to finance acquisitions of plant or earning assets, such as rental property. These loans are secured by a first mortgage lien on the commercial property, and may be further secured by other property or other assets depending on the value of the mortgaged property. In most instances, these loans are guaranteed personally by the principals. The Bank typically looks for cash flow from the business at least equal to 115% coverage of the business debt service, and for income-producing property to be self-supporting, generally, with a minimum debt service coverage ratio of 120% to 125%. Commercial mortgage loans carry more risk than residential real estate loans. Commercial mortgage loans tend to be larger in size, and the properties tend to exhibit more fluctuation in value. The repayment of the loan is primarily dependent on the success of the business itself, or the tenants in the case of income producing property. Economic cycles can affect the success of a business. The Bank experienced losses on commercial mortgage loans of $518,755 during 2008, $220,640 during 2007, and $59,120 during 2006. The Bank experienced recoveries on commercial and investment mortgages of $9,643 in 2008, $187 in 2007 and $6,290 in 2006. There were approximately $2.0 million commercial mortgage loans past due more than 90 days at December 31, 2008.

Construction and land development loans are loans to finance the acquisition and development of parcels of land and to construct residential housing or commercial property. The Bank typically will finance 70% to 80% of the discounted future value of these projects, or 80% of value or 90% of cost, whichever is less, on a single-family detached home. The loan is collateralized by the project or real estate itself, and other assets or guarantees of the principals in most cases. Repayment to the Bank is anticipated from the proceeds of sale of the final units, or permanent mortgage financing on a residential construction loan for a single borrower. These types of loans carry a higher degree of risk than a commercial mortgage loan. Interest rates, buyer preferences, and desired locations are all subject to change during the period from the time of the loan commitment to final delivery of the final unit, all of which can change the economics of the project. In addition, real estate developers to whom these loans are typically made are subject to the business risk of operating a business in a competitive environment. The Bank experienced $1.2 million of losses and $32,648 in recoveries on construction and land development loans during 2008. The Bank did not experience any losses or recoveries on construction and land development loans during 2007, and 2006. There were approximately $3.6 million in construction and land development loans past due more than 90 days at December 31, 2008.

Demand and time loans and lines of credit are loans to businesses for relatively short periods of time, usually not more than one year. These loans are made for any valid business purpose. These loans may be secured by assets of the borrower or guarantor, but may be unsecured based on the personal guarantee of the principal. If secured, loans may be made for up to 100% of the value of the collateral. The businesses to which these loans are made are subject to normal business risk, and cash flows of the business may be subject to economic cycles. In addition, the value of the collateral may fluctuate. If guaranteed by the principal, the net worth and assets of the principal may be dissipated by demands of the business, or due to other factors. The Bank had no losses or recoveries on demand and time loans in 2008, 2007 and 2006. There were $583,000 of demand and time and line of credit loans delinquent more than 90 days at December 31, 2008.

Home improvement loans are loans made to borrowers to complete improvements to their homes including such projects as room additions, swimming pool installations or new roofs. The Bank makes unsecured home improvement loans to a maximum amount of $15,000. Any loan above that limit is secured by a deed of trust. Borrowers are required to own their home, and to meet certain income and debt ratio requirements. The Bank also reviews the credit history of all applicants. Because they are unsecured or secured by a deed of trust, these loans are more risky than first mortgage residential lending. This risk is mitigated somewhat based on the fact that the loans are used to improve the borrower's home, typically a borrower's most significant asset. In addition, the debt-to-income ratio requirement helps determine the borrower's current ability to repay the loan. The Bank had charge-offs of home improvement loans of $0, $249, and $11,515 in 2008, 2007 and 2006, respectively. There were recoveries of $320, $608 and $0 in 2008, 2007, and 2006, respectively. There were approximately $3,000 of home improvement loans delinquent more than 90 days at December 31, 2008.

The remainder of the consumer loan portfolio is comprised of installment loans for automobiles, boats and recreational vehicles ("RV"), overdraft protection lines, and loans secured by deposit accounts or stocks. The largest portion of this group is installment loans for automobiles and other vehicles. The Bank will finance up to 90% of the cost of a new car purchase, or the maximum loan amount as determined by the National Automobile Dealers Association ("NADA") publication for used cars. The Bank will finance up to 85% of the cost of a new boat or RV, or the maximum loan amount determined by the NADA Boat/RV Guide for used Boats and RVs. These loans are secured by the vehicle purchased. Borrowers must meet certain income and debt ratio requirements, and a credit review is performed on each applicant. These types of loans are subject to the risk that the value of the vehicle will decline faster than the amount due on the loan. However, the income-to-debt ratio requirement helps determine the borrower's current ability to repay. The Bank had no losses on automobile loans in 2007 and $6,849 in 2006 and recoveries of $0, $5,598, and $1,251 in 2008, 2007 and 2006, respectively. There were no automobile or other vehicle loans past due more than 90 days at December 31, 2008.

Overdraft lines and other personal loans are unsecured lending arrangements. These loans or lines of credit are made to allow customers to easily make purchases of consumer goods. If the lines are handled as agreed, they will typically be automatically renewed each year. Because they are unsecured, these loans carry a higher level of risk than secured lending transactions. The Bank attempts to mitigate significant risk by establishing fairly low credit limits. Net charge-offs in 2008, 2007, and 2006 were $24,501, $2,916, and $11,662, respectively. There were $11,000 overdraft loans and other personal loans past due more than 90 days at December 31, 2008.

Loans secured by savings accounts and stock and bond certificates are secured lending arrangements. The Bank will advance funds for up to 95% of balances in savings or certificate of deposit accounts. The Bank will advance funds up to 60% of the market value of actively traded stock certificates and bonds or 50% of the market value of listed but not actively traded stocks and bonds. Loans secured by stocks and bonds are subject to margin calls to maintain the loan to value ratio. Collateral is not released until the loan is repaid, and the borrower is generally required to pay interest monthly. There were no losses on loans secured by savings accounts or stock and bond certificates during 2008, 2007, or 2006. Recoveries on loans secured by stocks and bonds were $0, $437, and $0 in 2008, 2007, and 2006 respectively. There were no loans secured by savings accounts or stock and bond certificates past due more than 90 days at December 31, 2008.

The Bank is the principal originator of the loans it makes, at this time. In prior periods, residential mortgage loans and home equity loans and lines of credit were predominantly purchased from a network of brokers or other types of originators with whom the Bank did business. The Bank has sold some loans in the secondary market and therefore derives a small amount of noninterest income from serviced loans. These income amounts are not significant to the amounts of noninterest income derived from other sources.

CMSI originates adjustable and fixed-rate residential mortgage loans at terms and conditions and with documentation that permit their sale in the secondary mortgage market. CMSI's practice is to immediately sell substantially all residential mortgage loans in the secondary market with servicing released.

CCDC was established in 1995 for the purpose of promoting, developing, and improving the housing and economic conditions of people in Maryland with particular emphasis in the Metropolitan Baltimore area. CCDC promotes through loans, investments, and other transactions, efforts to increase housing for low and moderate-income individuals.

MSLLC was established in 2004 for the purpose of disposing of real estate owned. At December 31, 2008, there were six properties with a fair market value of $1.7 million. There was no activity in MSLLC in 2007 and 2006.

Investment Activities. – The Company maintains a portfolio of investment securities to provide liquidity and income. The current portfolio amounts to about 17% of total assets, and is invested primarily in U.S. government agency securities, state and municipal bonds, corporate bonds, and mortgage-backed securities with maturities varying from 2009 to 2038, as well as equity securities.

Deposit Services. – The Bank offers a wide range of both personal and commercial types of deposit accounts and services as a means of gathering funds. Deposit accounts available include noninterest-bearing demand checking, interest-bearing checking (NOW accounts), savings, money market, certificates of deposit, and individual retirement accounts. Deposit accounts carry varying fee structures depending on the level of services desired by the customer. Interest rates vary depending on the balance in the account maintained by the customer. Commercial deposit customers may also choose an overnight investment account which automatically invests excess balances available in demand accounts on a daily basis in repurchase agreements. The Bank's customer base for deposits is primarily retail in nature. The Bank also offers certificates of deposit over $100,000 to its retail and commercial customers. The Bank has used deposit brokers in the past and may do so in the future to meet liquidity needs.

The Company offers Certificate of Deposit Registry Service ("CDARS") deposits to its customers. This is a program which allows customers to deposit more than would normally be covered by FDIC insurance. CDARS is a nationwide program that allows participating banks to "swap" customer deposits so that no customer has greater than the insurable maximum in one bank, but the customer only deals with his/her own bank.

In addition to traditional deposit services, the Bank offers telephone banking services, internet banking services and internet bill paying services to its customers. Also, the Bank offers remote deposit capture to its commercial customers.

Brokerage Activities. – CFS provides full service brokerage services for stocks, bonds, mutual funds and annuities. For 2008, commission income totaled $682,000 and net income was $158,000.

Market. – The Company considers its core markets to be the communities within the Baltimore Metropolitan Statistical Area ("Baltimore MSA"), particularly Baltimore City and the counties of Baltimore, Anne Arundel and Harford. Lending activities are broader and include areas outside of the Baltimore MSA. CMSI operates in Delaware, Pennsylvania, Virginia and West Virginia in addition to its core Maryland operations. All of the Company's revenue is generated within the United States.

Competition. – The Bank faces strong competition in all areas of its operations. This competition comes from entities operating in Baltimore City, Baltimore County, Anne Arundel County, Harford County, and Carroll County, and includes branches of some of the largest banks in Maryland. Its most direct competition for deposits historically has come from other commercial banks, savings banks, savings and loan associations and credit unions. The Bank also competes for deposits with money market funds, mutual funds and corporate and government securities. The Bank competes with the same banking entities for loans, as well as mortgage banking companies and other institutional lenders. The competition for loans varies from time to time depending on certain factors, including, among others, the general availability of lendable funds and credit, general and local economic conditions, current interest rate levels, conditions in the mortgage market and other factors which are not readily predictable. Some of the Bank's competitors have greater assets and operating capacity than the Bank.

Current federal law allows the acquisition of banks by bank holding companies nationwide. Further, federal and Maryland law permit interstate banking. Recent legislation has broadened the extent to which financial services companies, such as investment banks and insurance companies, may control commercial banks. As a consequence of these developments, competition in the Bank's principal market may increase, and a further consolidation of financial institutions in Maryland may occur.

Asset Management. – The Bank makes available several types of loan services to its customers as described above, depending on customer needs. Recent emphasis has been made on originating short-term (one year or less), variable rate commercial loans and variable rate home equity lines of credit, with the balance of its funds invested in consumer/installment loans and real estate loans, both commercial and residential. In addition, a portion of the Bank's assets is invested in high-grade securities and other investments in order to provide income, liquidity and safety. Such investments include U.S. government agency securities, corporate bonds, mortgage-backed securities and collateralized mortgage obligations, as well as advances of federal funds to other member banks of the Federal Reserve System. Subject to the effects of taxes, the Bank also invests in tax-exempt state and municipal securities with a minimum rating of "A" by a recognized ratings agency. The Bank's primary source of funds is customer deposits. The risk of non-repayment (or deferred payment) of loans is inherent in the business of commercial banking, regardless of the type of loan or borrower. The Bank's efforts to expand its loan portfolio to small and medium-sized businesses may result in the Bank undertaking certain lending risks which are somewhat different from those involved in loans made to larger businesses. The Bank's management evaluates all loan applications and seeks to minimize the exposure to credit risks through the use of thorough loan application, approval and monitoring procedures. However, there can be no assurance that such procedures significantly reduce all risks.

Employees. – As of December 31, 2008, the Bank and its subsidiaries had 137 full time equivalent employees, 28 of whom were officers. Each officer generally has responsibility for one or more loan, banking, customer contact, operations, or subsidiary functions. Non-officer employees are employed in a variety of administrative capacities. Management believes that it has a favorable relationship with its employees.

CRITICAL ACCOUNTING POLICIES

The Company's financial condition and results of operations are sensitive to accounting measurements and estimates of matters that are inherently uncertain. When applying accounting policies in areas that are subjective in nature, management must use its best judgment to arrive at the carrying value of certain assets. One of the most critical accounting policies applied is related to the valuation of the loan portfolio.

A variety of estimates impact the carrying value of the loan portfolio including the calculation of the allowance for loan losses, valuation of underlying collateral and the timing of loan charge-offs.

The allowance for loan losses is one of the most difficult and subjective judgments. The allowance is established and maintained at a level that management believes is adequate to cover losses resulting from the inability of borrowers to make required payments on loans. Estimates for loan losses are arrived at by analyzing risks associated with specific loans and the loan portfolio. Current trends in delinquencies and charge-offs, the views of Bank regulators, changes in the size and composition of the loan portfolio and peer comparisons are also factors. The analysis also requires consideration of the economic climate and direction and change in the interest rate environment, which may impact a borrower's ability to pay, legislation impacting the banking industry and economic conditions specific to the Bank's service area. Because the calculation of the allowance for loan losses relies on estimates and judgments relating to inherently uncertain events, results may differ from our estimates.

Another critical accounting policy is related to securities. Securities are evaluated periodically to determine whether a decline in their value is other than temporary. The term "other than temporary" is not intended to indicate a permanent decline in value. Rather, it means that the prospects for near term recovery of value are not necessarily favorable, or that there is a lack of evidence to support fair values equal to, or greater than, the carrying value of the investment. Management reviews criteria such as the magnitude and duration of the decline, as well as the reasons for the decline, to predict whether the loss in value is other than temporary. Once a decline in value is determined to be other than temporary, the value of the security is reduced and a corresponding charge to earnings is recognized.

SUPERVISION AND REGULATION

General. – The Company and Bank are extensively regulated under federal and state law. Generally, these laws and regulations are intended to protect depositors, not stockholders. The following is a summary description of certain provisions of certain laws, which affect the regulation of banks and holding companies. The discussion is qualified in its entirety by reference to applicable laws and regulations. Changes in these laws and regulations may have a material effect on the business and prospects of the Company and the Bank.

As a bank holding company, the Company is subject to the Bank Holding Company Act of 1956, as amended (the "BHCA"). The BHCA is administered by the Board of Governors of the Federal Reserve System (the "Board of Governors"), and the Company is required to file with the Board of Governors such reports and information as may be required pursuant to the BHCA. The Board of Governors also may examine the Company and any of its nonbank subsidiaries. The BCHA requires every bank holding company to obtain the prior approval of the Board of Governors before: (i) it or any of its subsidiaries (other than a bank) acquires substantially all of the assets of any bank; (ii) it acquires ownership or control of any voting shares of any bank if after such acquisition it would own or control, directly or indirectly, more than five percent of the voting shares of such bank; or (iii) it merges or consolidates with any other bank holding company.

Under the BHCA, a bank holding company is generally prohibited from engaging in, or acquiring direct or indirect control of more than five percent (5%) of the voting shares of any company engaged in non-banking activities. A major exception to this prohibition is for activities the Board of Governors finds, by order or regulation, to be so closely related to banking or managing or controlling banks. Some of the activities that the Board of Governors has determined by regulation to be properly incident to the business of a bank holding company are: making or servicing loans and certain types of leases; engaging in certain investment advisory and discount brokerage activities; performing certain data processing services; acting in certain circumstances as a fiduciary or as an investment or financial advisor; ownership of certain types of savings associations; engaging in certain insurance activities; and making investments in certain corporations or projects designed primarily to promote community welfare.

Federal and State Bank Regulation. The Bank is a Maryland state-chartered bank, with all the powers of a commercial bank, regulated and examined by the Office of the Maryland Commissioner of Financial Regulation (the "Commissioner') and the FDIC. The Commissioner and the FDIC have extensive enforcement authority over the institutions they regulate to prohibit or correct activities which violate law, regulations or written agreements with the regulator, or which are deemed to constitute unsafe or unsound practices. Enforcement actions may include the appointment of a conservator or receiver, the issuance of a cease and desist order, the termination of deposit insurance, the imposition of civil money penalties on the institution, its directors, officers, employees and institution-affiliated parties, and the enforcement of any such mechanisms through restraining orders or other court actions.

In its lending activities, the maximum legal rate of interest, fees and charges which a financial institution may charge on a particular loan depends on a variety of factors such as the type of borrower, the purpose of the loan, the amount of the loan and the date the loan is made. Other laws tie the maximum amount, which may be loaned to any one customer and its related interests to capital levels. The Bank is also subject to certain restrictions on extensions of credit to executive officers, directors, principal stockholders or any related interest of such persons which generally require that such credit extensions be made on substantially the same terms as are available to third persons dealing with the Bank and not involve more than the normal risk of repayment.

The Community Reinvestment Act ("CRA") requires that in connection with the examination of financial institutions within their jurisdictions, the FDIC evaluate the record of the financial institutions in meeting the credit needs of their local communities, including low and moderate-income neighborhoods, consistent with the safe and sound operation of these banks. The factors are also considered by all regulatory agencies in evaluating mergers, acquisitions and applications to open a branch or facility. As of the date of its most recent examination report, the Bank has a CRA rating of "Satisfactory."

Under the Federal Deposit Insurance Corporation Improvement Act of 1991("FDICIA"), each federal banking agency is required to prescribe, by regulation, non-capital safety and soundness standards for institutions under its authority. The federal banking agencies, including the FDIC, have adopted standards covering internal controls, information systems, internal audit systems, loan documentation, credit underwriting, interest rate exposure, asset growth, and compensation, fees and benefits. An institution that fails to meet those standards may be required by the agency to develop a plan acceptable to the agency, which specifies the steps that the institution will take to meet the standards. Failure to submit or implement such a plan may subject the institution to regulatory sanctions. The Bank believes that it meets substantially all standards which have been adopted. FDICIA also imposed new capital standards on insured depository institutions described under the caption, "Capital Requirements."

Before establishing new branch offices, the Bank must meet certain minimum capital stock and surplus requirements. Prior to establishment of the branch, the Bank must obtain Commissioner and FDIC approval.

Deposit Insurance. Congress has temporarily increased FDIC deposit insurance from $100,000 to $250,000 per depositor through December 31, 2009. On January 1, 2010, the standard coverage limit will return to $100,000 for all deposit categories except IRAs and Certain Retirement Accounts, which will be insured up to $250,000 per owner. The Company is participating in the FDIC's Temporary Liquidity Guarantee Program. Consequently, unlimited deposit insurance coverage is available through December 31, 2009 for non-interest bearing transaction accounts. As an FDIC insured institution, deposits of the Bank are currently insured through the Bank Insurance Fund ("BIF"). For traditional and ROTH IRA's, the federal deposit insurance limit is $250,000. The FDIC is required to establish the semi-annual assessments for BIF-insured depository institutions at a rate determined to be appropriate to maintain or increase the reserve ratio of the respective deposit insurance funds at or above 1.25 percent of estimated insured deposits or at such higher percentage that the FDIC determines to be justified for that year by circumstances raising significant risk of substantial future losses to the fund. The Bank paid a *de minimus* semi-annual assessment in 2008.

In an effort to restore capitalization levels and to ensure the BIF will adequately cover projected losses from future bank failures, the FDIC, in October 2008, proposed a rule to alter the way in which it differentiates for risk in the risk-based assessment system and to revise deposit insurance assessment rates, including base assessment rates. The FDIC proposed raising the current rates uniformly by 7 basis points for the assessment for the first quarter of 2009 resulting in annualized assessment rates for Risk Category 1 institutions ranging from 12 to 14 basis points. The proposal for first quarter 2009 assessment rates was adopted as a final rule in December 2008. The FDIC also proposed, effective April 1, 2009, initial base assessment rates for Risk Category 1 institutions of 10 to 14 basis points. After the effect of potential base-rate adjustments, the annualized assessment rate for Risk Category 1 institutions would range from 8 to 21 basis points. A final rule related to this proposal is expected to be issued during the first quarter of 2009. The Company cannot provide any assurance as to the amount of any proposed increase in its deposit insurance premium rate, should such an increase occur, as such changes are dependent upon a variety of factors, some of which are beyond the Company's control.

Limits on Dividends and Other Payment. Both federal and state laws impose restrictions on the ability of the Bank to pay dividends. The Federal Reserve Board ("FRB") has issued a policy statement, which provides that, as a general matter, insured banks may pay dividends only out of prior operating earnings. For a Maryland state-chartered bank, dividends may be paid out of undivided profits or, with the prior approval of the Commissioner, from surplus in excess of 100% of required capital stock. If, however, the surplus of a Maryland bank is less than 100% of its required capital stock, cash dividends may not be paid in excess of 90% of the net earnings. In addition to these specific restrictions, bank regulatory agencies, in general, also have the ability to prohibit proposed dividends by a financial institution, which would otherwise be permitted under applicable regulations if the regulatory body determines that such distribution would constitute an unsafe or unsound practice.

On February 13, 2009, the Company raised $9,201,000 through the sale of the Series A Preferred Stock which will qualify as Tier 1 capital. The Series A Preferred Stock will pay cumulative dividends at a rate of 5% per annum until February 15, 2014. Beginning February 16, 2014, the dividend rate will increase to 9% per annum. Dividends are payable quarterly. The Treasury's current consent shall be required for any increase in the common dividends per share until February 13, 2012 unless prior to such date, the Series A Preferred Stock is redeemed in whole or the Treasury has transferred all of the Series A Preferred Stock to third parties. For as long as the Series A Preferred Stock is outstanding, no dividend can be paid on the common stock unless all dividends on the Series A Preferred Stock have been paid.

On and after February 15, 2012, the Company may, at its option, redeem shares of Series A Preferred Stock, in whole or in part, at any time and from time to time, for cash at a per share amount equal to the sum of the liquidation preference per share plus any accrued and unpaid dividends to but excluding the redemption date. Prior to February 15, 2012, the Company may redeem shares of Series A Preferred Stock only if it has received aggregate gross proceeds of not less than $ 9,201,000 from one or more qualified equity offerings, and the aggregate redemption price may not exceed the net proceeds received by the Company from such offerings. The redemption of the Series A Preferred Stock requires prior regulatory approval.

The warrant is exercisable at $6.72 per share at any time on or before February 13, 2019. Treasury has agreed not to exercise voting power with respect to any shares of common stock issued upon exercise of the warrant.

The Series A Preferred Stock and the warrant were issued in a transaction exempt from registration pursuant to Section 4(2) of the Securities Act of 1933, as amended. The Company has agreed to register the Series A Preferred Stock, the warrant, and the shares of common stock underlying the warrant (the "warrant shares") as soon as practicable after the date of the issuance of the Series A Preferred Stock and the warrant. Neither the Series A Preferred Stock nor the warrant will be subject to any contractual restrictions on transfer, except that Treasury may not transfer a portion of the warrant with respect to, or exercise the warrant for, more than one-half of the warrant shares prior to the earlier of (a) the date on which the Company has received aggregate gross proceeds of not less than $9,201,000 from one or more qualified equity offerings and (b) December 31, 2009.

The Purchase Agreement also subjects the Company to certain of the executive compensation limitations included in the EESA. As a condition to the closing of the transaction, Robert A. Altieri, James M. Uveges, Gary M. Jewell, William D. Sherman, and Lola B. Stokes (the Company's Senior Executive Officers, as defined in the Purchase Agreement) each: (i) voluntarily waived any claim against the Treasury or the Company for any changes to such Senior Executive Officer's compensation or benefits that are required to comply with the regulation issued by the Treasury under the TARP Capital Purchase Program as published in the Federal Register on October 20, 2008 and acknowledging that the regulation may require modification of the compensation, bonus, incentive and other benefit plans, arrangements and policies and agreements (including so-called "golden parachute" agreements) as they relate to the period the Treasury holds any equity or debt securities of the Company acquired through the TARP Capital Purchase Program; and (ii) entered into an amendment to Messer's Altieri, Uveges, Jewell and Mrs. Stokes employment agreements that provide that any severance payments made to such officers will be reduced, as necessary, so as to comply with the requirements of the TARP Capital Purchase Program.

Capital Requirements. The FDIC adopted certain risk-based capital guidelines to assist in the assessment of the capital adequacy of a banking organization's operations for both transactions reported as assets on the balance sheet and transactions, such as letters of credit and recourse arrangements, which are recorded as off balance sheet items. Under these guidelines, nominal dollar amounts of assets and credit equivalent amounts of off balance sheet items are multiplied by one of several risk adjustment percentages, which range from 0% for assets with low credit risk, such as certain U.S. Treasury securities, to 100% for assets with relatively high credit risk, such as business loans.

A banking organization's risk-based capital ratios are obtained by dividing its qualifying capital by its total risk adjusted assets. The regulators measure risk-adjusted assets, which include off balance sheet items, against both total qualifying capital (the sum of Tier 1 capital and limited amounts of Tier 2 capital) and Tier 1 capital. "Tier 1," or core capital, includes common equity, perpetual preferred stock (excluding auction rate issues) and minority interest in equity accounts of consolidated subsidiaries, less goodwill and other intangibles, subject to certain exceptions. "Tier 2," or supplementary capital, includes, among other things, limited-life preferred stock, hybrid capital instruments, mandatory convertible securities, qualifying subordinated debt, and the allowance for loan losses, subject to certain limitations and less required deductions. The inclusion of elements of Tier 2 capital is subject to certain other requirements and limitations of the federal banking agencies. Banks subject to the risk-based capital guidelines are required to maintain a ratio of Tier 1 capital to risk-weighted assets of at least 4% and a ratio to total capital to risk-weighted assets of at least 8%. The appropriate regulatory authority may set higher capital requirements when particular circumstances warrant.

In August 1995 and May 1996, the federal banking agencies adopted final regulations specifying that the agencies will include, in their evaluations of a bank's capital adequacy, an assessment of the bank's interest rate risk ("IRR") exposure. The standards for measuring the adequacy and effectiveness of a banking organization's interest rate risk management include a measurement of board of director and senior management oversight, and a determination of whether a banking organization's procedures for comprehensive risk management are appropriate to the circumstances of the specific banking organization. The Bank has internal IRR models that are used to measure and monitor IRR. Additionally, the regulatory agencies have been assessing IRR on an informal basis for several years. For these reasons the addition of IRR evaluation to the agencies' capital guidelines has not resulted in significant changes in capital requirements for the Bank.

Failure to meet applicable capital guidelines could subject a banking organization to a variety of enforcement actions, including limitations on its ability to pay dividends, the issuance by the applicable regulatory authority of a capital directive to increase capital and, in the case of depository institutions, the termination of deposit insurance by the FDIC, as well as to the measures described under the caption, "Federal Deposit Insurance Corporation Improvement Act of 1991" below, as applicable to undercapitalized institutions. In addition, future changes in regulations or practices could further reduce the amount of capital recognized for purposes of capital adequacy. Such a change could affect the ability of the Bank to grow and could restrict the amount of profits, if any, available for the payment of dividends to the stockholders.

Federal Deposit Insurance Corporation Improvement Act of 1991. In December 1991, Congress enacted FDICIA, which substantially revised the bank regulatory and funding provisions of the Federal Deposit Insurance Act and made significant revisions to several other federal banking statutes. FDICIA provides for, among other things, (i) publicly available annual financial condition and management reports for financial institutions, including audits by independent accountants, (ii) the establishment of uniform accounting standards by federal banking agencies, (iii) the establishment of a "prompt corrective action" system of regulatory supervision and intervention, based on capitalization levels, with more scrutiny and restrictions placed on depository institutions with lower levels of capital, (iv) additional grounds for the appointment of a conservator or receiver, and (v) restrictions or prohibitions on accepting brokered deposits, except for institutions which significantly exceed minimum capital requirements. FDICIA also provides for increased funding of the FDIC insurance funds and the implementation of risk-based premiums, described further under the caption "Deposit Insurance."

A central feature of FDICIA is the requirement that the federal banking agencies take "prompt corrective action" with respect to depository institutions that do not meet minimum capital requirements. Pursuant to FDICIA, the federal bank regulatory authorities have adopted regulations setting forth a five-tiered system for measuring the capital adequacy of the depository institutions that they supervise. Under these regulations, a depository institution is classified in one of the following capital categories: “well capitalized,” “adequately capitalized,” “undercapitalized,” “significantly undercapitalized” and “critically undercapitalized.” An institution may be deemed by the regulators to be in a capitalization category that is lower than is indicated by its actual capital position if, among other things, it receives an unsatisfactory examination rating with respect to asset quality, management, earnings or liquidity. The Bank is currently “well capitalized.”

FDICIA generally prohibits a depository institution from making any capital distribution (including payment of a cash dividend) if the depository institution would thereafter be undercapitalized. Undercapitalized depository institutions are subject to growth limitations and are required to submit capital restoration plans. If a depository institution fails to submit an acceptable plan, it is treated as if it is significantly undercapitalized. Significantly undercapitalized depository institutions may be subject to a number of other requirements and restrictions, including orders to sell sufficient voting stock to become adequately capitalized, requirements to reduce total assets and stop accepting deposits from correspondent banks. Critically undercapitalized institutions are subject to the appointment of a receiver or conservator; generally within 90 days of the date such institution is determined to be critically undercapitalized.

FDICIA provides the federal banking agencies with significantly expanded powers to take enforcement action against institutions, which fail to comply with capital or other standards. Such action may include the termination of deposit insurance by the FDIC or the appointment of a receiver or conservator for the institution. FDICIA also limits the circumstances under which the FDIC is permitted to provide financial assistance to an insured institution before appointment of a conservator or receiver.

Financial Modernization. In November 1999, the Gramm-Leach-Bliley Act (“GLBA”) was signed into law. Effective in part on March 11, 2000, GLBA revised the BHCA and repealed the affiliation provisions for the Glass-Steagall Act of 1933, which, taken together, limited the securities, insurance and other non-banking activities of any company that controls a FDIC insured institution. Under GLBA, bank holding companies can elect, subject to certain qualifications, to become a “financial holding company.” GLBA provides that a financial holding company may engage in a full range of financial activities, including insurance and securities sales and underwriting activities, and real estate development, with the expedited notice procedures.

Maryland law generally permits Maryland state-chartered banks, including the Bank, to engage in the same activities, directly or through an affiliate, as national banks. GLBA permits certain qualified national banks to form financial subsidiaries, which have broad authority to engage in all financial activities except insurance underwriting, insurance investments, real estate investment or development, or merchant banking. Thus, GLBA has the effect of broadening the permitted activities of Maryland state-chartered banks.

THE PATRIOT ACT

The Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (the “PATRIOT Act”) requires financial institutions to develop a customer identification plan that includes procedures to:

- Collect identifying information about customers opening a deposit or loan account.
- Verify customer identity.
- Maintain records of the information used to verify the customer’s identity.
- Determine whether the customer appears on any list of suspected terrorists or terrorist organizations.

Under the provisions of the PATRIOT Act, the Bank is also required from time to time to search its customer data base for the names of known or suspected terrorists as provided by the government.

Due to the extensive regulation of the commercial banking business in the United States, the Company is particularly susceptible to changes in federal and state legislation and regulations.

Governmental Monetary Policies and Economic Controls

The Company is affected by monetary policies of regulatory agencies, including the FRB, which regulates the national money supply in order to mitigate recessionary and inflationary pressures. Among the techniques available to the FRB are: engaging in open market transactions in U.S. Government securities, changing the discount rate on bank borrowings, changing reserve requirements against bank deposits, prohibiting the payment of interest on demand deposits, and imposing conditions on time and savings deposits. These techniques are used in varying combinations to influence the overall growth of bank loans, investments and deposits. Their use may also affect interest rates charged on loans or paid on deposits. The effect of governmental policies on the earnings of the Company cannot be predicted. However, the Company’s earnings will be impacted by movement in interest rates, as discussed in Part II Item 7a., “Quantitative and Qualitative Disclosure About Market Risk.”

ITEM 1A: RISK FACTORS

The risks and uncertainties described below are not the only ones that we face. Additional risks and uncertainties that we are unaware of, or that we currently deem immaterial, also may become important factors that affect us and our business. If any of these risks were to occur, our business, financial condition or results of operations could be materially and adversely affected. Also, consider the other information in this Annual Report on Form 10-K, as well as the documents incorporated by reference.

The Company's Business May Be Adversely Affected by Conditions in the Financial Markets and Economic Conditions Generally

Since December 2007, the United States has been in a recession. Business activity across a wide range of industries and regions is greatly reduced and local governments and many businesses are facing extremely difficult operating conditions due to the lack of consumer spending and the lack of liquidity in the credit markets. Unemployment has increased significantly.

Since mid-2007, and particularly during the second half of 2008, the financial services industry and the securities markets generally were materially and adversely affected by significant declines in the values of nearly all asset classes and by a serious lack of liquidity. This was initially triggered by declines in home prices and the values of subprime mortgages, but spread to all mortgage and real estate asset classes, to leveraged bank loans and to nearly all asset classes, including equities. The global markets have been characterized by substantially increased volatility and short-selling and an overall loss of investor confidence, initially in financial institutions, but more recently in companies in a number of other industries and in the broader markets.

Market conditions have also led to the failure or merger of a number of prominent financial institutions. Financial institution failures or near-failures have resulted in further losses as a consequence of defaults on securities issued by them and defaults under contracts entered into with such entities as counterparties. Furthermore, declining asset values, defaults on mortgages and consumer loans, and the lack of market and investor confidence, as well as other factors, have all combined to increase credit default swap spreads, to cause rating agencies to lower credit ratings, and to otherwise increase the cost and decrease the availability of liquidity, despite very significant declines in Federal Reserve borrowing rates and other government actions. Some banks and other lenders have suffered significant losses and have become reluctant to lend, even on a secured basis, due to the increased risk of default and the impact of declining asset values on the value of collateral. The foregoing has significantly weakened the strength and liquidity of some financial institutions worldwide. In 2008, the U.S. government, the Federal Reserve and other regulators have taken numerous steps to increase liquidity and to restore investor confidence, including investing approximately $200 billion in the equity of other banking organizations, but asset values have continued to decline and access to liquidity continues to be very limited.

The Company's financial performance generally, and in particular the ability of borrowers to pay interest on and repay principal of outstanding loans and the value of collateral securing those loans, is highly dependent upon the business environment in the markets where the Company operates, in the State of Maryland and, in particular, the Baltimore, Washington metropolitan region. A favorable business environment is generally characterized by, among other factors, economic growth, declining unemployment, efficient capital markets, low inflation, high business and investor confidence, and strong business earnings. Unfavorable or uncertain economic and market conditions can be caused by: declines in economic growth, business activity or investor or business confidence; rising unemployment, limitations on the availability or increases in the cost of credit and capital; increases in inflation or interest rates; natural disasters; or a combination of these or other factors.

Overall, during 2008, the business environment has been adverse for many households and businesses in the United States and worldwide. The business environment in Maryland and the markets in which the Company operates has been less adverse than in the United States generally but continues to deteriorate. It is expected that the business environment in the State of Maryland, the United States and worldwide will continue to deteriorate for the foreseeable future. There can be no assurance that these conditions will improve in the near term. Such conditions could adversely affect the credit quality of the Company's loans, results of operations and financial condition.

The Company's Profitability Depends Significantly On Economic Conditions In The State Of Maryland

The Company's success depends primarily on the general economic conditions of the State of Maryland and the specific local markets in which the Company operates. Unlike larger national or other regional banks that are more geographically diversified, the Company provides banking and financial services to customers in the Baltimore, Washington metropolitan area. The local economic conditions in these areas have a significant impact on the demand for the Company's products and services as well as the ability of the Company's customers to repay loans, the value of the collateral securing loans and the stability of the Company's deposit funding sources. Although economic conditions in the State of Maryland have experienced less decline than in the United States generally, these conditions are declining and are expected to continue to decline in the future. A significant decline in general economic conditions, whether caused by recession, inflation, unemployment, changes in securities markets, acts of terrorism, outbreak of hostilities or other international or domestic occurrences or other factors could impact these local economic conditions and, in turn, have a material adverse effect on the Company's financial condition and results of operations.

Competition may decrease our growth or profits.

We face significant competition for banking services in our primary market in which we operate. Competition in the local banking industries may limit our ability to attract and retain customers. We may face competition now and in the future from the following: other local and regional banking institutions, including larger commercial banking organizations; savings banks; credit unions; other financial institutions; and non-bank financial services companies serving the area.

In particular, our competitors may possess greater resources that may afford them a marketplace advantage by enabling them to maintain numerous banking locations and mount extensive promotional and advertising campaigns. Additionally, banks and other financial institutions with larger capitalization and financial intermediaries not subject to bank regulatory restrictions have larger lending limits, which enable them to serve the credit needs of larger customers. We also face competition from out-of-state financial intermediaries that have opened low-end production offices or that solicit deposits in their respective market areas. If we are unable to attract and retain banking customers we may be unable to continue our loan growth and level of deposits and our results of operations and financial condition may otherwise be negatively affected.

In the past, we have expanded our operations into non-banking activities such as insurance-related products and brokerage services. We may have difficulty competing with more established providers of these products and services due to the intense competition in many of these industries. In addition, we may be unable to attract and retain non-banking customers due to a lack of market and product knowledge or other industry specific matters or an inability to attract and retain qualified, experienced employees. Our failure to attract and retain customers with respect to these non-banking activities could negatively impact our future earnings.

Changes in interest rates and other factors beyond our control may adversely affect our earnings and financial condition.

Our main source of income from operations is net interest income, which is equal to the difference between the interest income received on loans, investment securities and other interest-earning assets and the interest expense incurred in connection with deposits, borrowings and other interest-bearing liabilities. As a result, our net interest income can be affected by changes in market interest rates. These rates are highly sensitive to many factors beyond our control, including general economic conditions, both domestic and foreign, and the monetary and fiscal policies of various governmental and regulatory authorities. We have adopted asset and liability management policies to try to minimize the potential adverse effects of changes in interest rates on our net interest income, primarily by altering the mix and maturity of loans, investments and funding sources. However, even with these policies in place, we cannot provide assurance that changes in interest rates will not negatively impact our operating results.

An increase in interest rates also could have a negative impact on our business by reducing the ability of borrowers to repay their current loan obligations, which could not only result in increased loan defaults, foreclosures and write-offs, but also necessitate further increases to our allowance for loan losses. Increases in interest rates also may reduce the demand for loans and, as a result, the amount of loan and commitment fees. In addition, fluctuations in interest rates may result in disintermediation, which is the flow of funds away from depository institutions into direct investments that pay higher rates of return, and may affect the value of our investment securities and other interest-earning assets.

We originate and sell mortgage loans. Changes in interest rates affect demand for our loan products and the revenue realized on the sale of loans. A decrease in the volume of loans sold and lower gains on sales of mortgages can decrease our revenues and net income.

Our allowance for loan losses may not be adequate to cover our actual loan losses, which could adversely affect our earnings.

If our customers default on the repayment of their loans, our profitability could be adversely affected. A borrower's default on its obligations under one or more of our loans may result in lost principal and interest income and increased operating expenses as a result of the allocation of management time and resources to the collection and work-out of the loans. If collection efforts are unsuccessful or acceptable workout arrangements cannot be reached, we may have to write-off the loans in whole or in part. Although we may acquire any real estate or other assets that secure the defaulted loans through foreclosure or other similar remedies, the amount owed under the defaulted loans may exceed the value of the assets acquired.

Our management periodically makes a determination of our allowance for loan losses based on available information, including the quality of our loan portfolio, economic conditions, and the value of the underlying collateral and the level of our non-accruing loans. If our assumptions prove to be incorrect, our allowance may not be sufficient and future additions to the allowance may be necessary which will result in an expense for the period. If, as a result of general economic conditions or an increase in nonperforming loans, management determines that an increase in our allowance for loan losses is necessary, we may incur additional expenses.

In addition, as an integral part of their examination process, bank regulatory agencies periodically review our allowance for loan losses and the value we attribute to real estate acquired through foreclosure or other similar remedies. These regulatory agencies may require us to adjust our determination of the value for these items based on their judgment. These adjustments could negatively impact our results of operations or financial condition.

In the course of our business, we may acquire, through foreclosure, properties securing loans that are in default. Particularly in commercial real estate lending, there is a risk that hazardous substances could be discovered on these properties. In this event, we might be required to remove these substances from the affected properties at our sole cost and expense. The cost of this removal could substantially exceed the value of the affected properties. We may not have adequate remedies against the prior owners or other responsible parties and could find it difficult or impossible to sell the affected properties. The occurrence of one or more of these events could adversely affect our financial condition or operating results.

Changes in local economic conditions could adversely affect our business.

Because we serve primarily individuals and smaller businesses, the ability of our customers to repay their loans is impacted by the economic conditions in these areas. As of December 31, 2008, approximately 72% of our loan portfolio consisted of commercial loans, defined as commercial and industrial, municipal, multi-family, commercial real estate and construction loans. Thus, our results of operations, both in terms of the origination of new loans and the potential default of existing loans, is heavily dependent upon the strength of local businesses.

We have traditionally obtained funds principally through deposits and borrowings. As a general matter, deposits are a cheaper source of funds than borrowings, because interest rates paid for deposits are typically less than interest rates charged for borrowings. If, as a result of competitive pressures, market interest rates, general economic conditions or other events, the balance of our deposits decrease relative to our overall banking operations, we may have to rely more heavily on borrowings as a source of funds in the future. Such an increased reliance on borrowings could have a negative impact on our results of operations or financial condition.

Government regulation significantly affects our business.

Bank holding companies and state and federally chartered banks operate in a highly regulated environment and are subject to supervision and examination by federal and state regulatory agencies. We are subject to the BHCA, as amended, and to regulation and supervision by the Federal Deposit Insurance Corporation, or FDIC, and the Office of the Maryland Commissioner. The cost of compliance with regulatory requirements may adversely affect our results of operations or financial condition. Federal and state laws and regulations govern numerous matters including: changes in the ownership or control of banks and bank holding companies; maintenance of adequate capital and the financial condition of a financial institution; permissible types, amounts and terms of extensions of credit and investments; permissible non-banking activities; the level of reserves against deposits; and restrictions on dividend payments. Regulations affecting banks and financial services companies undergo continuous change, and we cannot predict the ultimate effect of these changes, which could have a material adverse effect on our profitability or financial condition. Federal economic and monetary policy may also affect our ability to attract deposits and other funding sources, make loans and investments, and achieve satisfactory interest spreads.

The FDIC, and state banking authorities possess cease and desist powers to prevent or remedy unsafe or unsound practices or violations of law by banks subject to their regulation, and the FRB possesses similar powers with respect to bank holding companies. These and other restrictions limit the manner in which we may conduct our business and obtain financing.

Furthermore, our banking business is affected not only by general economic conditions, but also by the monetary policies of the FRB. Changes in monetary or legislative policies may affect the interest rates we must offer to attract deposits and the interest rates we can charge on our loans, as well as the manner in which we offer deposits and make loans. These monetary policies have had, and are expected to continue to have, significant effects on the operating results of depository institutions, including our Bank.

Under regulatory capital adequacy guidelines and other regulatory requirements, we must meet guidelines that include quantitative measures of assets, liabilities, and certain off-balance sheet items, subject to qualitative judgments by regulators about components, risk weightings and other factors. If we fail to meet these minimum capital guidelines and other regulatory requirements, our financial condition would be materially and adversely affected. Our failure to maintain the status of “well capitalized” under our regulatory framework could affect the confidence of our customers in us, thus compromising our competitive position. In addition, failure to maintain the status of “well capitalized” under our regulatory framework or “well managed” under regulatory examination procedures could compromise our status as a bank holding company and related eligibility for a streamlined review process for acquisition proposals.

Changes in the Federal and State tax laws may negatively impact the financial performance of the Company.

The Company is subject to changes in tax law that could increase the effective tax rate payable to the state or federal government. These law changes may be retroactive to previous periods and as a result, could negatively affect the current and future performance of the Company.

Technology failure could adversely affect our operations and profits.

We rely heavily on communications and information systems to conduct our business. Any failure or interruptions or breach in security of these systems could result in failures or disruptions in our customer relationship management, general ledger, deposits, and servicing or loan origination systems. The occurrence of any failures or interruptions could result in a loss of customer business and have a material adverse effect on our results of operations and financial condition.

The Company is subject to litigation risk.

In the normal course of business, the Corporation may become involved in litigation, the outcome of which may have a direct material impact on our financial position and daily operations. Please see Note 16, "Contingencies" for the current status of existing and threatened litigation.

Changes in accounting standards or interpretation in new or existing standards could materially affect the results of the Company.

From time to time the Financial Accounting Standards Board ("FASB") and the SEC change accounting regulations and reporting standards that govern the preparation of the Company's financial statements. In addition, the FASB, SEC, bank regulators and the outside independent auditors may revise their previous interpretations regarding existing accounting and regulations and the application of these accounting standards. These revisions in their interpretations are out of the Company's control and may have a material impact on the Company's financial results of operations.

Our ability to pay dividends is limited by law and contract.

Our ability to pay dividends to our shareholders largely depends on the Company's receipt of dividends from the Bank. The amount of dividends that the Bank may pay to the Company is limited by federal laws and regulations. We also may decide to limit the payment of dividends even when we have the legal ability to pay them in order to maintain earnings for use in our business.

The market price for our common stock may be volatile.

The market price for our common stock has fluctuated, ranging between $5.50 and $15.08 per share during the 12 months ended December 31, 2008. The overall market and the price of our common stock may continue to be volatile. There may be a significant impact on the market share of our common stock due to, among other things:

- Variations in our anticipated or actual operating results or the results of our competitors;
- Changes in investors' or analysts' perceptions of the risks and conditions of business;
- The size of the public float of our common stock;
- Regulatory developments;
- The announcement of acquisitions or new branch locations by us or our competitors;
- Market conditions; and
- General economic conditions.

Additionally, the average daily trading volume for our common stock is low and on various days throughout the year, there is no activity on the stock. There can be no assurance that a more active or consistent trading market will develop. As a result, relatively small trades could have a significant impact on the price of our stock.

ITEM 2: PROPERTIES

The Company owned the following properties, which had a book value of $2.3 million at December 31, 2008:

Location	*Description*
1740 East Joppa Road Towson, MD 21234	Full service branch with drive thru, Electronic Banking offices, Auditing offices and leased office space
427 Crain Highway Glen Burnie, MD 21061	Full service branch with drive-thru
531 South Conkling Street Baltimore, MD 21224	Full service branch with drive-thru

344 N. Charles Street Baltimore, MD 21201 (1)	Full service branch with Executive offices, Lending offices and Finance offices

The Company leased the following facilities at an aggregate annual rental of approximately $1.2 million as of December 31, 2008:

Location	*Description*	*Lease Expiration Date**
1066-70 Maiden Choice Lane Arbutus, MD 21229	Full service branch	April 30, 2031
4738 Shelbourne Road Baltimore, MD 21229	Detached drive-thru	April 30, 2031
Suites 101-103 & 120-122 1589 Sulphur Spring Road Baltimore, MD 21227 (1)	Administrative and operational offices	April 30, 2009
2637-A Old Annapolis Road Hanover, MD 21076	Full service branch	October 1, 2014
Northway Shopping Center 684 Old Mill Road Millersville, MD 21108	Full service branch	August 31, 2014
602 Hoagie Drive Bel Air, MD 21014	Full service branch	November 30, 2044
10301 York Road Cockeysville, MD 21030	Full service branch	December 1, 2047
4040 Schroeder Avenue Perry Hall, MD 21128	Full service branch opened January 7, 2008. Relocated from White Marsh, Maryland	August 13, 2047
2300 York Road Timonium, MD 21093	Mortgage subsidiary offices	January 14, 2010
208 Hickory Avenue Bel Air, MD 21014	Mortgage subsidiary office closed	March 31, 2010
8905 Harford Road Baltimore, MD 21234	Mortgage subsidiary offices	June 30, 2009
1 Center Square, Suite 201 Hanover, PA 17331	Mortgage subsidiary offices	July 31, 2009
7151 Columbia Gateway Drive Suite A Columbia, MD 21046 (1)	Executive, administrative and operational offices	April 30, 2029

* Expiration date, assuming the Company exercises all extension options.

(1) On or around March 23, 2009, the Executive, Lending and Finance offices at 344 N. Charles Street and the administrative and operational offices at 1589 Sulphur Spring Road will move to 7151 Columbia Gateway Drive, Suite A, Columbia, Maryland 21046.

ITEM 3: LEGAL PROCEEDINGS

The Company is involved in various routine legal actions arising from normal business activities. In management's opinion, the outcome of these matters, individually or in the aggregate, will not have a material adverse impact on the results of operation or financial position of the Company.

ITEM 4: SUBMISSION OF MATTERS TO A VOTE OF SECURITY-HOLDERS

There were no matters submitted to a vote of the shareholders during the quarter ended December 31, 2008.

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

TRADING AND DIVIDENDS

As of December 31, 2008, there were 372 shareholders of record of the Company. The Company's Common Stock has traded on the National Association of Security Dealers' Automated Quotation System ("NASDAQ") National Market Tier of The NASDAQ Stock Market under the symbol "CRRB". Currently, there are two broker-dealers who make a market in the Common Stock.

As a depository institution whose deposits are insured by the FDIC, the Bank may not pay dividends or distribute any of its capital assets while it remains in default on any assessment due to the FDIC. The Bank currently is not in default under any of its obligations to the FDIC. As a commercial bank under the Maryland Financial Institution Law, the Bank may declare cash dividends from undivided profits or, with the prior approval of the Commissioner of Financial Regulation, out of surplus in excess of 100% of its required capital stock, and after providing for due or accrued expenses, losses, interest and taxes.

The Company and the Bank, in declaring and paying dividends, are also limited insofar as minimum capital requirements of regulatory authorities must be maintained. The Company and the Bank currently comply with such capital requirements.

Dividends declared per share on the Company's common stock were $0.48 in 2008 and 2007, and $0.45 in 2006, representing a payout ratio of 137.23% in 2008, 63.88% in 2007, and 48.98% in 2006. The dividend payout ratio is the result of dividing the amount of dividends paid by net income.

The Company implemented a Dividend Reinvestment Plan that provides automatic reinvestment of dividends in additional shares of Company common stock.

During 2008, the Company repurchased and retired 276,137 shares of common stock at an average price of $14.07. During 2007, the Company repurchased and retired 16,015 shares of common stock at a price of $16.50 per share. In 2006, the Company repurchased and retired 7,518 shares of common stock at a price of $17.14 per share.

The following table sets forth the high and low sales price and dividends per share of the Company's common stock for the periods indicated.

Period	*Price Per Share*				*Cash Dividends Paid Per Share*	
	2008		*2007*		*2008*	*2007*
	Low	*High*	*Low*	*High*		
4th Quarter	$ 5.50	$ 9.34	$11.25	$14.85	$ 0.12	$0.12
3rd Quarter	8.00	14.00	12.00	16.73	0.12	0.12
2nd Quarter	11.75	14.99	15.55	18.40	0.12	0.12
1st Quarter	12.00	15.08	16.40	18.00	0.12	0.12
					$ 0.48	$0.48

As of December 31, 2008, there were 372 common shareholders of record holding an aggregate of 2,564,988 shares. The Company believes there to be in excess of 540 beneficial owners of the Company's Common Stock.

The ability of the Company to pay dividends in the future will be dependent on the earnings, if any, financial condition and business of the Company, as well as other relevant factors, such as regulatory requirements. No assurance can be given either that the Company's future earnings, if any, will be sufficient to enable it to pay dividends, or that if such earnings are sufficient, that the Company will not decide to retain such earnings for general working capital and other funding needs. In addition, the Company is highly dependent on dividends received from the Bank to enable it to pay dividends to shareholders. No assurance can be given that the Bank will continue to generate sufficient earnings to enable it to pay dividends to the Company, or that it will continue to meet regulatory capital requirements which, if not met, could prohibit payment of dividends to the Company.

On February 13, 2009, as part of the TARP Capital Purchase Program, the Company entered into a Letter Agreement, and the related Securities Purchase Agreement - Standard Terms (collectively, the "Purchase Agreement"), with the United States

Department of the Treasury (“Treasury”), pursuant to which the Company issued (i) 9,201 shares of Fixed Rate Cumulative Perpetual Preferred Stock, Series A, liquidation preference $1,000 per share (the “Series A Preferred Stock”), and (ii) a warrant to purchase 205,379 shares of the Company’s common stock, par value $1.00 per share, for an aggregate purchase price of $1,380,147 in cash (the “Warrant”).

The Series A Preferred Stock will qualify as Tier 1 capital and will pay cumulative dividends at a rate of 5% per annum until February 15, 2014. Beginning February 16, 2014, the dividend rate will increase to 9% per annum. On and after February 15, 2012, the Company may, at its option, redeem shares of Series A Preferred Stock, in whole or in part, at any time and from time to time, for cash at a per share amount equal to the sum of the liquidation preference per share plus any accrued and unpaid dividends to but excluding the redemption date. Prior to February 15, 2012, the Company may redeem shares of Series A Preferred Stock only if it has received aggregate gross proceeds of not less than $9,201,000 from one or more qualified equity offerings, and the aggregate redemption price may not exceed the net proceeds received by the Company from such offerings. The redemption of the Series A Preferred Stock requires prior regulatory approval.

The Warrant is exercisable in whole or in part, from time to time, at $6.72 per share at any time on or before February 13, 2019. The number of shares of common stock issuable upon exercise of the Warrant and the exercise price per share will be adjusted if specific events occur. Treasury has agreed not to exercise voting power with respect to any shares of common stock issued upon exercise of the Warrant.

Pursuant to the terms of the Purchase Agreement, prior to the earlier of (i) February 13, 2012 or (ii) the date on which the Series A Preferred Stock has been redeemed in full or Treasury has transferred all of the Series A Preferred Stock to non-affiliates, the Company cannot increase its quarterly cash dividend above $0.08 or repurchase any shares of its common stock or other capital stock or equity securities or trust preferred securities without the consent of Treasury.

In addition, pursuant to the Articles Supplementary relating to the Series A Preferred Stock, so long as any shares of Series A Preferred Stock remain outstanding, the Company may not declare or pay any dividends or distributions on the Company’s common stock or any class or series of the Company’s equity securities ranking junior, as to dividends and upon liquidation, to the Series A Preferred Stock (“Junior Stock”) (other than dividends payable solely in shares of common stock) or on any other class or series of the Company’s equity securities ranking, as to dividends and upon liquidation, on a parity with the Series A Preferred Stock (“Parity Stock”), and may not repurchase or redeem any common stock, Junior Stock or Parity Stock, unless all accrued and unpaid dividends for past dividend periods, including the latest completed dividend period, have been paid or have been declared and a sufficient sum has been set aside for the benefit of the holders of the Series A Preferred Stock.

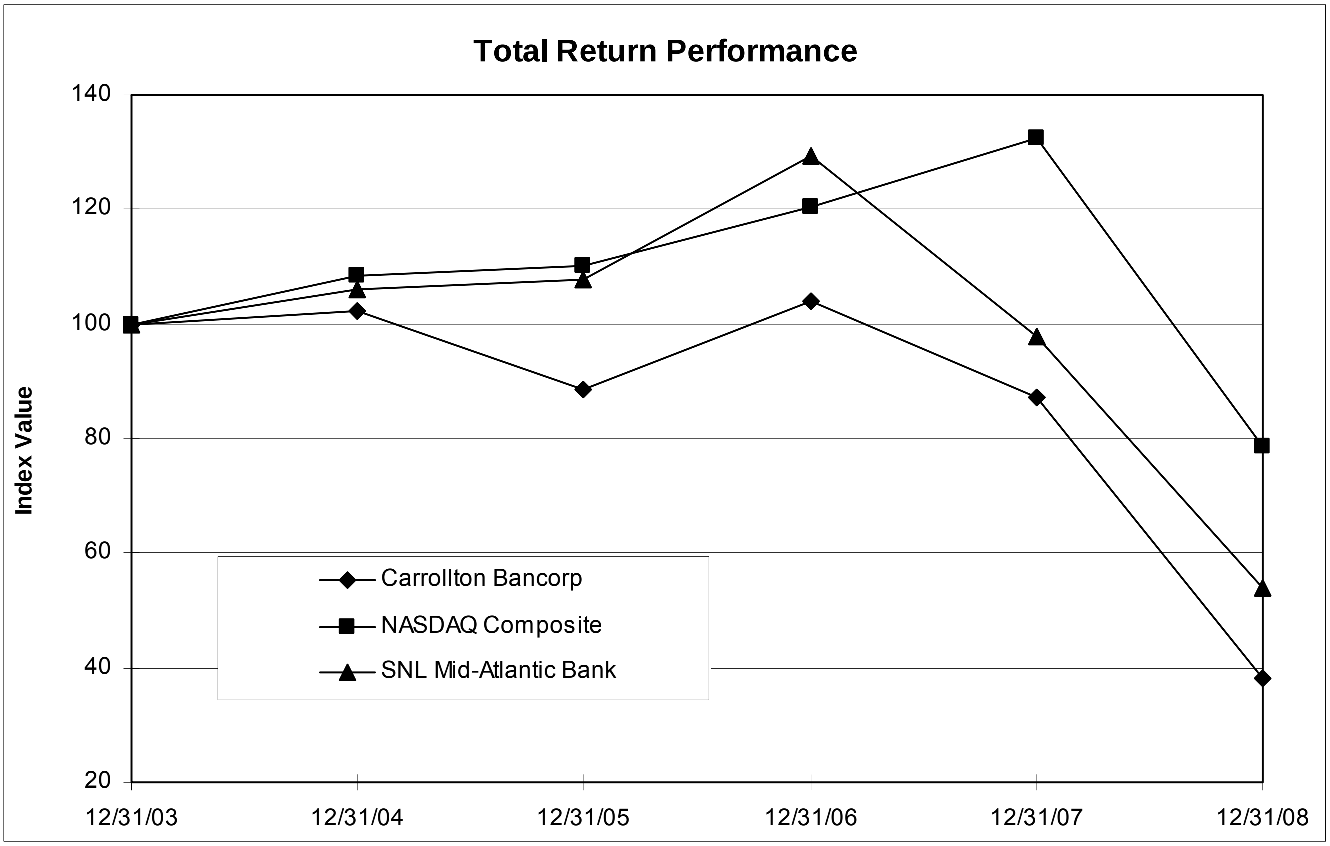
The repurchase restrictions described above do not apply in certain limited circumstances, including the repurchase of common stock in connection with the administration of any employee benefit plan in the ordinary course of business and consistent with past practice, but only to offset the increase in the number of diluted shares outstanding resulting from the grant, vesting or exercise of equity-based compensation.

STOCK PERFORMANCE TABLE

The Company is required by the SEC to provide a five-year comparison of the cumulative total shareholder return on our common stock compared with that of a broad equity market index, and either a published industry index or a constructed peer group index of the Company.

The following chart compares the cumulative shareholder return on the Company's common stock from December 31, 2003, to December 31, 2008, with the cumulative total of the NASDAQ Composite (U.S.), the NASDAQ Bank and SNL Mid-Atlantic Indices. The comparison assumes $100 was invested on December 31, 2003, in the Company's common stock and in each of the foregoing indices. It also assumes reinvestment of any dividends.

The Company does not make, nor does it endorse, any predictions as to future stock performance.



	Period Ending					
Index	*12/31/03*	*12/31/04*	*12/31/05*	*12/31/06*	*12/31/07*	*12/31/08*
Carrollton Bancorp	100.00	102.17	88.54	104.06	87.36	38.03
NASDAQ Composite	100.00	108.59	110.08	120.56	132.39	78.72
SNL Mid-Atlantic Bank	100.00	105.91	107.79	129.37	97.83	53.89

The following table provides information about the Company's equity securities that may be issued under all of the Company's equity compensation plans as of the end of the most recently completed fiscal year:

EQUITY COMPENSATION PLAN

Plan Category	*Number of securities to be issued upon exercise of outstanding options, warrants and rights (a)*	*Weighted-average exercise price of outstanding options, warrants and rights (b)*	*Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) (c)*
Equity compensation plans approved by security holders	156,385	$14.23	492,800
Equity compensation plans not approved by security holders	N/A	N/A	N/A
Total	156,385	$14.23	492,800

ITEM 6: SELECTED FINANCIAL DATA

	2008	2007	2006	2005	2004
CONSOLIDATED INCOME STATEMENT DATA:					
Interest income	$ 22,406,600	$ 23,676,360	$ 23,127,504	$ 19,071,379	$ 15,500,323
Interest expense	8,457,182	9,762,324	8,737,450	7,375,083	5,321,622
Net interest income	13,949,418	13,914,036	14,390,054	11,696,296	10,178,701
Provision for loan losses	2,096,000	536,000	—	—	—
Net interest income after provision for loan losses	11,853,418	13,378,036	14,390,054	11,696,296	10,178,701
Noninterest income	6,585,694	6,274,142	8,898,996	10,718,636	8,781,151
Noninterest expenses	17,468,064	16,475,141	19,381,003	18,634,124	17,751,000
Income before income taxes	971,048	3,177,037	3,908,047	3,780,808	1,208,852
Income taxes	124,197	1,050,774	1,323,268	1,322,371	320,488
Net income	$ 846,851	$ 2,126,263	$ 2,584,779	$ 2,458,437	$ 888,364
CONSOLIDATED BALANCE SHEET DATA, AT YEAR END					
Assets	$404,181,184	$352,848,570	$349,824,752	$360,467,146	$319,123,132
Gross loans	283,693,156	261,623,833	260,001,314	247,943,073	219,726,294
Deposits	292,353,276	285,638,625	277,903,801	271,626,503	225,846,145
Shareholders' equity	27,390,693	35,931,300	34,711,378	34,640,165	34,215,280
PER SHARE DATA:					
Number of shares of Common Stock outstanding, at year-end	2,564,988	2,834,975	2,806,705	2,809,698	2,834,823
Net income:					
Basic	$ 0.32	$ 0.75	$ 0.92	$ 0.87	$ 0.31
Diluted	0.32	0.75	0.90	0.87	0.31
Cash dividends declared	0.48	0.48	0.45	0.40	0.38
Book value, at year end	10.68	12.67	12.37	12.33	12.07
Performance and capital ratios:					
Return on average assets	0.22 %	0.61 %	0.75 %	0.72 %	0.29 %
Return on average shareholders' equity	2.62 %	5.97 %	7.55 %	7.12 %	2.61 %
Net interest margin (a)	3.93 %	4.34 %	4.57 %	3.89 %	3.81 %
Average shareholders' equity to average total assets	8.54 %	10.22 %	9.91 %	10.13 %	11.11 %
Year-end capital to year-end risk-weighted assets:					
Tier 1	9.84 %	12.35 %	11.92 %	11.63 %	11.52 %
Total	10.91 %	13.63 %	13.20 %	13.51 %	12.74 %
Year-end Tier 1 leverage ratio	6.78 %	10.03 %	9.74 %	8.96 %	9.41 %
Cash dividends declared to net income	147.46 %	63.88 %	48.98 %	45.97 %	121.17 %
ASSET QUALITY RATIOS:					
Allowance for loan losses, at year-end to:					
Gross loans	1.12 %	1.25 %	1.20 %	1.35 %	1.59 %
Nonperforming, restructured and past-due loans	39.67 %	55.28 %	54.93 %	209.50 %	132.05 %
Net charge-offs to average gross loans	0.82 %	0.15 %	0.08 %	0.06 %	0.08 %
Nonperforming assets as a percent of period-end gross loans and foreclosed real estate	3.42 %	2.26 %	2.19 %	0.64 %	1.20 %

(a) Net interest margin is the ratio of net interest income, determined on a fully taxable equivalent basis (a non-GAAP financial measure), to total average interest earning assets.

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

FORWARD-LOOKING STATEMENTS

This Annual Report on Form 10-K and certain information incorporated herein by reference contain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. All statements included or incorporated by reference in this Annual Report on Form 10-K, other than statements that are purely historical, are forward-looking statements. Statements that include the use of terminology such as "anticipates," "expects," "intends," "plans," "believes," "estimates" and similar expressions also identify forward-looking statements. The forward-looking statements are based on the Company's current intent, belief and expectations. Forward-looking statements in this Annual Report on Form 10-K include, but are not limited to statements of the Company's plans, strategies, objectives, intentions, including, among other statements, statements involving the Company's projected loan and deposit growth, loan collateral values, collectibility of loans, anticipated changes in other operating income, payroll and branching expenses, branch, office and product expansion of the Company and its subsidiary, and liquidity and capital levels.

These statements are not guarantees of future performance and are subject to certain risks and uncertainties that are difficult to predict. Actual results may differ materially from these forward-looking statements because of interest rate fluctuations, a deterioration of economic conditions in the Baltimore-Washington metropolitan area, a downturn in the real estate market, losses from impaired loans, an increase in nonperforming assets, potential exposure to environmental laws, changes in federal and state bank laws and regulations, the highly competitive nature of the banking industry, a loss of key personnel, changes in accounting standards and other risks described in the Company's filings with the SEC. Existing and prospective investors are cautioned not to place undue reliance on these forward-looking statements, which speak only as of today's date. The Company undertakes no obligation to update or revise the information contained in this Annual Report whether as a result of new information, future events or circumstances or otherwise. Past results of operations may not be indicative of future results. Readers should carefully review the risk factors described in other documents the Company files from time to time with the SEC, including the Quarterly Reports on Form 10-Q to be filed by the Company in 2009**.**

BUSINESS AND OVERVIEW

The Company is a bank holding company headquartered in Baltimore, Maryland with one wholly-owned subsidiary, the Bank. The Bank has four subsidiaries, CMSI, CFS, and MSLLC which are wholly owned, and CCDC, which is 96.4% owned.

The Bank is engaged in a general commercial and retail banking business with ten branch locations. CMSI is in the business of originating residential mortgage loans and has two branch locations. CFS provides brokerage services to customers and MSLLC manages and disposes of real estate acquired through foreclosures. CCDC promotes, develops and improves the housing and economic conditions of people in Maryland.

Total assets for the year ended December 31, 2008 compared to December 31, 2007 reflect a 15% increase to $404.2 million. Gross loans, including loans held for sale, increased 13% or $36.2 million from $269.2 million at December 31, 2007, to $305.4 million at December 31, 2008. Investments increased 26% or $14.0 million to $66.8 million at December 31, 2008. Total deposits increased 2% or $6.7 million to $292.4 million while borrowings increased 168% or $49.9 million. During the same period, stockholders' equity decreased $8.5 million or 24% to $27.4 million or 6.78% of total assets compared to 10.2% at December 31, 2007. The decrease was due primarily to the repurchase of 276,137 shares for $3.9 million, dividends paid of $1.2 million, and a decrease in accumulated other comprehensive income of $4.3 million, all of which was partially offset by net income of $847,000.

Net income for the year ended December 31, 2008, totaled $847,000 compared to $2.1 million for the prior year, a $1.3 million or 60% decrease. The decrease was due to the $1.6 million increase in the provision for loan losses and the $538,000 pretax charge to close the Wilkens Plaza drive thru branch. The increase in the provision for loan losses was due to an increase in the level of nonperforming assets, which required additional allocations to the allowance for credit losses.

Net income for the year ended December 31, 2007, totaled $2.1 million compared to $2.6 million for the prior year, an 18% decrease. The Company's earnings performance for the year ended December 31, 2007, was impacted by the decision to stop servicing money service businesses (MSB) as of September 2006, hiring consultants to assist in documenting internal controls for compliance with Sarbanes-Oxley Act of 2002 ("SOX"), the increase in the provision for loan losses, and legal fees and related expenses for non-accrual loans.

The earnings for the year ended December 31, 2006, included a before tax charge of approximately $1.8 million ($1.2 million after tax) representing the loss from a check kiting scheme by one of the Bank's commercial customers. The earnings also included a charge of approximately $2.3 million representing a prepayment penalty for restructuring a $35 million FHLBA advance at a fixed rate of 6.84% maturing February 2, 2010. This charge was substantially offset by a gain of approximately $2.3 million from the sale of equity securities.

Comparing the year ended December 31, 2008, and 2007, net interest income remained relatively flat at $13.0 million. The reduction in rates by the Federal Reserve during the year contributed to the reduction in the Company's net interest margin from 4.34% for the year ended December 31, 2007 to 3.93% for the year ended December 31, 2008. The 41 basis points decrease in the net interest margin was substantially offset by the $34.2 million increase in average earning assets.

The Company recorded a provision for loan losses of $2.1 million for the year ended December 31, 2008, compared to $536,000 in 2007. The increase in the provision for loan losses was due to the increase in nonperforming loans and other loan risk factors. Nonperforming assets increased from $5.9 million at December 31, 2007 to $9.8 million at December 31, 2009. The allowance for loan losses represented 1.12% of outstanding loans at December 31, 2008.

For the year ended December 31, 2008, noninterest income was $6.6 million compared to $6.3 million for the year ended December 31, 2007, an increase of $312,000 or 5%. The increase was due to the $244,000 gain on the sale and call of securities purchased at a discount partially offset by the write down of equity securities, and a $263,000 or 12% increase in the fees and commissions earned by CMSI. These increases were partially offset by a $126,000 or 13% decrease in service charges, a $53,000 or 3% decrease in Point of Sale revenue and ATM fees and a $21,000 or 4% decrease in other fees and commissions.

Noninterest expenses were $17.5 million for the year ended December 31, 2008, compared to $16.5 million for the year ended December 31, 2007, a $993,000 or 6% increase. The increase resulted from a one-time pre-tax charge of $538,000 to close the Wilkens Plaza drive thru branch, a $238,000 increase in OREO expenses, a $257,000 increase in occupancy expense caused by opening of our new Cockeysville branch and relocating our White Marsh branch to Perry Hall and normal lease escalation charges, and a $506,000 or 37% increase in employee benefits, in particular medical expenses. These increases in expenses were offset by a $281,000 reduction in salary expenses due to fewer employees and a $159,000 or 15% decrease in professional services related to consulting fees for compliance with SOX in 2007.

The Company paid dividends of $0.48 per share to shareholders during 2008.

RESULTS OF OPERATIONS

SUMMARY

The Company reported net income for 2008 of $847,000 or $0.32 per diluted share, representing a 60.2% decrease from 2007 net income of $2.1 million or $0.75 per share.

Loans held for sale increased $14.1 million or 186.3% due to the increase in refinancings of residential mortgages due to the reduction in rates by the Federal Reserve during the year.

The loan portfolio net of the Allowance for Loan Losses increased 8.6% to $280.5 million as a result of the Company's continuing efforts to align the loan portfolio to be in line with typical commercial banks. Interest income on loans, including loans held for sale, decreased 9.8% due to the reduction in the yield on average loans, including loans held for sale, from 7.66% for the year ended December 31, 2007 to 6.64% for the year ended December 31, 2008. The 102 basis points decrease in the yield was partially offset by the $11.3 million increase in average gross loans and loans held for sale.

The deposit portfolio increased 2.4% to $292.4 million, with the majority of the growth derived from certificates of deposit. Partially affecting these increases were decreases in noninterest bearing deposits, money market accounts and savings accounts. Borrowings from the Federal Home Loan Bank of Atlanta ("FHLBA") increased $50.2 million to fund the growth in loans and investments. Total interest expense decreased during 2008 due to the reduction in the yield on total interest bearing liabilities from 3.73% for the year ended December 31, 2007, to 2.86% for the year ended December 31, 2008. The 87 basis point decrease in the yield was partially offset by the $33.4 million increase in average total interest bearing liabilities. Noninterest income increased 5.0% or $312,000 in 2008 compared to 2007. The increase was due to the $224,000 gain in the sale and call of securities purchased at a discount partially offset by the write down of equity securities, and a $263,000 or 11.5% increase in the fees and commissions earned by CMSI. These increases were partially offset by a $126,000 or 13.3% decrease in service charges, a $53,000 or 2.8% decrease in Point of Sale revenue and ATM fees and a $21,000 or 4.3% decrease in other fees and commissions.

Noninterest expense increased 6.0% or $993,000 in 2008 compared to 2007. The increase resulted from a one-time pre-tax charge of $538,000 to close the Wilkens Plaza drive thru branch, a $238,000 increase in OREO expenses, a $257,000 increase in occupancy expense caused by opening of our new Cockeysville branch and relocating of our White Marsh branch to Perry Hall and normal lease escalation charges, and a $506,000 or 37.1% increase in employee benefits, in particular medical expenses. These increases in expenses were offset by a $281,000 or 3.9% reduction in salary expenses due to fewer employees and a $159,000 or 14.8% decrease in professional services related to consulting fees for compliance with SOX in 2007.

The Company reported net income for 2007 of $2.1 million or $0.75 per diluted share, representing an 18% decrease from 2006 net income of $2.6 million or $0.90 per share.

The loan portfolio net of the Allowance for Loan Losses and including loans held for sale increased 0.6% to $265.9 million as a result of the Company's continuing efforts to align the loan portfolio to be in line with typical commercial banks. Loans held for sale were substantially the same at $7.5 million due to the slow down in the residential housing market. Interest income on loans, including loans held for sale, increased 3.2% due to average loans, including loans held for sale, increasing $10.6 million and partially offset by loans repricing to lower rates in the fourth quarter of 2007.

The deposit portfolio increased 2.8% to $285.6 million, with the majority of the growth derived from money market accounts and certificates of deposit. Partially affecting these increases were decreases in noninterest bearing deposits and savings accounts. Interest expense increased during 2007, due to an $8.3 million increase in average interest-bearing deposits and the yield on interest-bearing deposits increasing 44 basis points.

Noninterest income decreased 29.5% or $2.6 million in 2007 compared to 2006, due primarily to a $2.2 million gain on the sale of securities in 2006, a 15.3% or $171,000 decrease in service charges, a 7.3% or $181,000 decrease in the fees and commissions earned by CMSI and an 8.1% or $166,000 decrease on Point of Sale revenue and ATM fees.

Noninterest expense decreased 15.0% or $2.9 million in 2007 compared to 2006. The decrease was due to the $1.8 million charge from the check kiting scheme by one of the Bank's commercial customers and the $2.3 million prepayment penalty for restructuring a FHLBA advance in 2006 partially offset by the $225,000 or 3% increase in salaries, the $269,000 or 15% increase in occupancy costs and the $855,000 or 20% increase in other operating expenses. The $225,000 increase in salaries was due to additional personnel for the new branch opened in May 2007 and normal salary increases partially offset by the elimination of personnel. The $269,000 increase in occupancy costs was due to normal lease escalation charges, the new branch rent started in March 2007, and a significant increase in a 30-year branch lease that renewed in April 2006. The $855,000 increase was due to $202,000 in consulting fees for compliance with SOX, increased legal fees and related costs due to a significant commercial loan to one borrower and increased nonaccrual loans and a $155,000 write down and cost to dispose of a real estate owned property in 2007 compared to a recovery of legal fees and related expenses on the payoff of a delinquent loan in 2006.

NET INTEREST INCOME

Net interest income, the amount by which interest income on interest-earning assets exceeds interest expense on interest-bearing liabilities, is the most significant component of the Company's earnings. Net interest income is a function of several factors, including changes in the volume and mix of interest-earning assets and funding sources, and market interest rates. While management policies influence these factors, external forces, including customer needs and demands, competition, the economic policies of the federal government and the monetary policies of the FRB, are also important.

The following table sets forth, for the periods indicated, information regarding the average balances of interest-earning assets and interest-bearing liabilities, the amount of interest income and interest expense and the resulting yields on average interest-earning assets and rates paid on average interest-bearing liabilities. Average balances are also provided for noninterest-earning assets and noninterest-bearing liabilities.

AVERAGE BALANCES, INTEREST, AND YIELDS

	2008			2007			2006		
	Average Balance	*Interest*	*Yield*	*Average Balance*	*Interest*	*Yield*	*Average Balance*	*Interest*	*Yield*
ASSETS									
Federal funds sold, Federal Reserve Bank and Federal Home Loan Bank deposit	$ 7,511,540	$ 65,861	0.88%	$ 3,737,413	$ 181,635	4.86%	$ 7,839,525	$ 382,625	4.88%
Federal Home Loan Bank stock	2,968,299	108,686	3.66	1,544,464	99,223	6.42	1,742,153	99,046	5.69
Investment securities: (a)									
U.S. government agency	23,311,111	1,317,296	5.65	16,043,046	902,454	5.63	15,316,293	788,538	5.15
State and municipal	8,543,619	525,509	6.15	9,233,678	572,591	6.20	8,734,211	544,815	6.24
Mortgage-backed securities	27,211,120	1,495,541	5.50	19,650,335	1,067,144	5.43	21,554,754	1,170,089	5.43
Corporate bonds	9,033,034	423,755	4.69	5,877,246	391,199	6.66	4,089,963	270,840	6.62
Other	1,512,580	74,775	4.94	1,140,856	53,199	4.66	1,154,060	49,212	4.26
	69,611,464	3,836,876	5.51	51,945,161	2,986,587	5.75	50,849,281	2,823,494	5.55
Loans:									
Demand and time	66,488,316	3,972,570	5.97	73,606,674	5,844,340	7.94	73,339,911	5,862,743	7.99
Residential mortgage (b)	90,110,476	5,874,216	6.52	77,543,499	5,704,170	7.36	72,131,409	3,926,413	5.44
Commercial mortgage and construction	123,220,972	8,712,560	7.07	116,904,123	8,988,319	7.69	110,899,759	8,544,541	7.70
Installment	1,236,740	89,834	7.26	1,238,724	100,692	8.13	1,504,253	80,978	5.38
Lease financing	147,300	8,761	5.95	595,593	39,494	6.63	1,429,551	80,889	5.66
	281,203,804	18,657,941	6.64	269,888,613	20,677,015	7.66	259,304,883	20,044,135	7.73
Total interest-earning assets	361,295,107	22,669,364	6.27	327,115,651	23,944,460	7.32	319,735,842	23,349,301	7.30
Noninterest-bearing cash	3,116,830			8,649,236			14,651,700		
Premises and equipment	7,223,167			6,533,050			5,432,452		
Other assets	10,382,790			8,170,747			7,993,335		
Allowance for loan losses	(3,161,028)			(3,108,760)			(3,287,376		
Unrealized gains (losses) on available for sale securities, net	(827,068)			1,133,365			1,065,683		
	$378,029,798			$348,493,289			$345,591,636		
LIABILITIES AND SHAREHOLDERS' EQUITY									
Interest-bearing deposits:									
Savings and NOW	$52,315,578	122,459	0.23%	$ 55,719,609	131,760	0.24%	$ 62,309,713	147,770	0.24%
Money market	46,737,845	1,021,124	2.18	56,986,611	2,248,253	3.95	51,303,354	1,936,266	3.77
Certificates of deposit	130,592,612	5,472,535	4.19	117,106,699	5,700,452	4.87	101,071,899	4,521,369	4.47
	229,646,035	6,616,118	2.88	229,812,919	8,080,465	3.52	214,684,966	6,605,404	3.08
Borrowed funds	65,789,689	1,841,064	2.80	32,222,600	1,681,860	5.22	38,900,240	2,132,046	5.48
Total interest-bearing liabilities	295,435,724	8,457,182	2.86	262,035,519	9,762,325	3.73	253,585,206	8,737,451	3.45
Noninterest-bearing deposits	48,754,626			49,584,706			56,441,180		
Other liabilities	1,569,676			1,261,192			1,312,259		
Shareholders' equity	32,269,772			35,611,872			34,252,991		
Total liabilities and shareholders' equity	$378,029,798			$348,493,289			$345,591,636		
Net interest margin	$361,295,107	$14,212,182	3.93%	$327,115,651	$14,182,135	4.34%	$319,735,842	$14,611,850	4.57%

(a) Interest on investments and loans is presented on a fully taxable equivalent basis (a non-GAAP financial measure), using the federal income tax rates of 34% and, where applicable, the state rate of 8.25% for 2008 and 7% for 2007 and 2006 (or a combined federal and state rate of 39.445% for 2008 and 38.62% for 2007 and 2006) to increase tax exempt interest income to a taxable equivalent basis. This is a non-GAAP measure that management believes is useful when comparing annual results,

(b) Loans held for sale are included in residential mortgage loans.

(c) Net interest margin is the ratio of net interest income, determined on a fully taxable-equivalent basis, to total average interest earning assets.

Net interest income on a tax-equivalent basis was substantially the same at $14.2 million for the years ended December 31, 2008, and 2007. The decrease in the net interest margin of 41 basis points from 4.34% for the year ended December 31, 2007, to 3.93% for the year ended December 31, 2008, was partially offset by a $34.2 million increase in average interest-earning assets during 2008 compared to 2007.

The $11.3 million or 4.2% increase in average loans outstanding is attributed to the Company's active business development efforts in its residential, commercial real estate, and construction and land development loan portfolio and general economic conditions of the Company's primary service market. The yield on loans decreased to 6.64% in 2008 compared to 7.66% for 2007 as the Federal Open Market Committee ("FOMC") lowered rates in 2008. The yield on investment securities decreased to 5.51% in 2008 from 5.75% in 2007. Total interest-earning assets increased $34.2 million or 10.4% while the yield decreased 105 basis points. Total interest-bearing liabilities increased $33.4 million or 12.7% while the yield decreased 87 basis points. Interest-bearing deposits were substantially the same at $229.6 million while borrowings increased $33.6 million or 104.2% to fund loan and investment growth. The net impact was a slight increase in tax-equivalent net interest income for the year ended December 31, 2008, compared to 2007.

Net interest income on a tax-equivalent basis decreased to $14.2 million for the year ended December 31, 2007, compared to $14.6 million for 2006. The decrease in tax-equivalent net interest income during 2007 was due to the decrease in the net interest margin of 23 basis points partially offset by a $10.6 million increase in average interest-earning assets during 2007 compared to 2006.

The $10.6 million or 4.1% increase in average loans outstanding is attributed to the Company's active business development efforts in its residential and construction and land development loan portfolio and general economic conditions of the Company's primary service market. The yield on loans decreased to 7.66% in 2007 compared to 7.73% for 2006 as the FOMC began lowering rates in September 2007. The yield on investment securities increased to 5.75% in 2007 from 5.55% in 2006. The net impact was a $430,000 or 2.9% decrease in tax-equivalent interest income for the year ended December 31, 2007, compared to 2006.

Interest expense increased $1.0 million to $9.8 million in 2007 from $8.7 million in 2006. Interest expense on deposits increased primarily due to a change in the deposit mix, with an increase in the amount of interest-bearing deposits and the cost of interest-bearing deposits increased from 3.08% in 2006 to 3.52% in 2007. Interest expense on borrowed funds decreased due to a $6.7 million decrease in average borrowed funds and the cost of average borrowed funds decreasing to 5.22% for the year ended December 31, 2007, compared to 5.48% for the same period in 2006.

The following table and the related discussions of interest income and interest expense provide further analysis of the changes in net interest income during 2008 and 2007:

	2008 Compared to 2007			2007 Compared to 2006		
	Change Due to Variance In			*Change Due to Variance In*		
	Rate(b)	*Volume(b)*	*Total*	*Rates(b)*	*Volume(b)*	*Total*
INTEREST INCOME						
Federal funds sold and interest-bearing deposits with other banks	$ (299,194)	$ 183,419	$ (115,775)	$ (778)	$ (200,213)	$ (200,991)
Investment securities and FHLB stock	(241,556)	1,101,308	859,752	113,357	49,913	163,270
Loans (a)	(2,885,965)	866,892	(2,019,073)	(185,237)	818,117	632,880
TOTAL INTEREST EARNED	(3,426,715)	2,151,619	(1,275,096)	(72,658)	667,817	595,159
INTEREST EXPENSE						
Deposits	(1,458,479)	(5,868)	(1,464,347)	1,009,606	465,455	1,475,061
Borrowings	(1,592,830)	1,752,034	159,204	(84,198)	(365,989)	(450,187)
TOTAL INTEREST EXPENSE	(3,051,309)	1,746,166	(1,305,143)	925,408	99,466	1,024,874
NET INTEREST INCOME	$ (375,406)	$ 405,453	$ 30,047	$ (998,066)	$ 568,351	$ (429,715)

(a) Interest on investments and loans is presented on a fully taxable equivalent basis (a non-GAAP financial measure), using regular income tax rates.

(b) The change in interest income and expense due to variance in both rate and volume has been allocated to the change due to variance in rate.

PROVISION FOR LOAN LOSSES

On a monthly basis, management of the Company reviews all loan portfolios to determine trends and monitor asset quality. For consumer loan portfolios, this review generally consists of reviewing delinquency levels on an aggregate basis with timely follow-up on accounts that become delinquent. In commercial loan portfolios, delinquency information is monitored and periodic reviews of business and property leasing operations are performed on an individual loan basis to determine potential collection and repayment problems.

Due to the slow down in the housing and real estate market and the unprecedented state of the economy, the Company has experienced an increase in its delinquency rate and charge off rate. The Company recorded a provision for loan losses of $2.1 million in 2008, $536,000 in 2007, and none for the year ended December 31, 2006. Nonaccrual, restructured and delinquent loans over 90 days to total loans increased to 3.42% at the end of 2008 compared to 2.26% in 2007. The ratio of net loan losses to average loans increased in 2008 to 0.74% compared to 0.15% for 2007. Nonaccrual, restructured, and delinquent loans over 90 days to total loans increased to 2.26% at the end of 2007 compared to 2.19% in 2006. The ratio of net loan losses to average loans increased in 2007 to 0.15% compared to 0.08% for 2006.

NONINTEREST INCOME

Noninterest income increased from $6.3 million during 2007 to $6.6 million in 2008, an increase of $312,000 or 5.0%. The increase was due to the $244,000 gain on the sale and call of securities purchased at a discount partially offset by the write down of equity securities, and a $263,000 or 11.5% increase in the fees and commissions earned by CMSI. These increases were partially offset by a $126,000 or 13.3% decrease in service charges, a $53,000 or 2.8% decrease in Point of Sale revenue and ATM fees and a $21,000 or 4.3% decrease in other fees and commissions.

Noninterest income decreased from $8.9 million during 2006 to $6.3 million in 2007 due primarily to the $2.2 million gain on the sale of securities in 2006. The $181,000 decrease in net gains and fees on sales of mortgage loans corresponded to a decrease in the fees received on mortgage loans sold during the year due to a slow down in the residential housing market. The $166,000 decrease in electronic banking was due to a reduction in the number of Point of Sale transactions in 2007 compared to 2006. The $171,000 decrease in service charges was due to the decision to stop servicing money service businesses (MSB) as of September 2006, and was partially offset by fee increases effective January 2007. In 2006, sales of available-for-sale securities generated $2.2 million in gains compared to $840,000 in 2005.

Electronic banking income is comprised of three sources: national point of sale (“POS”) sponsorships, ATM fees, and check card fees. The fees from the ATMs represent approximately 4% of total electronic banking revenue in 2007. The Company sponsors merchants who accept ATM cards for purchases within various networks (i.e. STAR, PULSE, and NYCE). This national POS sponsorship income represents approximately 82% of total electronic banking revenue. Fees from check cards comprise the remaining 14% of electronic banking revenue.

The Company offers a variety of financial planning and investment options to customers, through its subsidiary, CFS, and recognizes commission income as these services are provided.

NONINTEREST EXPENSES

Noninterest expense consists primarily of costs associated with personnel, occupancy and equipment, data processing, marketing and professional fees. Noninterest expenses were $17.5 million for the year ended December 31, 2008 compared to $16.5 million for the year ended December 31, 2007, a $993,000 or 6.0% increase. The increase resulted from a one-time pre-tax charge of $538,000 to close the Wilkens Plaza drive thru branch, a $238,000 increase in OREO expenses, a $257,000 or 12.4% increase in occupancy expense resulting from the opening of our new Cockeysville branch and relocating of our White Marsh branch to Perry Hall and normal lease escalation charges, and a $506,000 or 37.1% increase in employee benefits, in particular medical expenses. These increases in expenses were offset by a $281,000 or 3.9% reduction in salary expenses due to fewer employees and a $159,000 or 14.8% decrease in professional services related to consulting fees for compliance with SOX in 2007.

Noninterest expenses were $16.5 million for the year ended December 31, 2007 compared to $19.4 million for the year ended December 31, 2006, a $2.9 million or 15% decrease. The decrease was due to the $1.8 million charge from the check kiting scheme in 2006, the $2.3 million prepayment penalty for restructuring the FHLB advance in 2006. These decreases were partially offset by the $225,000 or 3% increase in salaries, the $269,000 or 15% increase in occupancy costs, the $671,000 or 129% increase in professional fees, and the $183,000 or 5% increase in other operating expenses. The $225,000 increase in salaries was due to additional personnel for the new branch opened in May 2007 and normal salary increases partially offset by the elimination of personnel. The $269,000 increase in occupancy costs was due to normal lease escalation charges, the new branch rent started in March 2007, and a significant increase in a 30-year branch lease that expired April 2006. The $671,000 increase in professional fees was due to $202,000 in consulting fees for compliance with SOX, increased legal fees and related costs due to a significant commercial loan to one borrower and increased nonaccrual loans. The $183,000 increase in other operating expenses was due primarily to a $155,000 write down and cost to dispose of a real estate owned property in 2007 compared to a recovery of legal fess and related expenses on the payoff of a delinquent loan in 2006.

INCOME TAX PROVISION

Income tax expense was $124,000 in 2008, $1.1 million in 2007 and $1.3 million in 2006. The effective tax rate was 12.8% in 2008, 33.1% in 2007, and 33.9% in 2006. The effective tax rates fluctuate from year to year due to changes in the mix of tax-exempt loans, investments and life insurance policies as a percentage of total loans and investments. In 2008, tax exempt interest was a substantial percentage of income before income taxes which resulted in a significantly lower effective tax rate. During 2007 and 2006, the Company purchased additional tax exempt securities, which reduced the effective tax rates.

FINANCIAL CONDITION

SUMMARY

Total assets of the Company increased by 14.6% to $404.2 million at December 31, 2008 from $352.8 million at December 31, 2007. Investment securities increased 26.5% to $66.8 million at December 31, 2008. Gross loans, excluding loans held for sale, increased by 8.4% to $283.7 million at December 31, 2008 compared to $261.6 million at the end of 2007. Interest-earning assets increased $53.3 million to $383.2 million and were 94.8% of total assets at December 31, 2008.

INVESTMENT SECURITIES

The investment portfolio consists of investment securities held to maturity and securities available for sale. Investment securities held to maturity are those securities that the Company has the positive intent and ability to hold to maturity and are carried at amortized cost. Securities available for sale are those securities that the Company intends to hold for an indefinite period of time but not necessarily until maturity. These securities are carried at fair value and may be sold as part of an asset/liability management strategy, liquidity management, interest rate risk management, regulatory capital management or other similar factors.

The components of the investment portfolio were as follows at December 31:

	2008	*2007*	*2006*	*2005*	*2004*
AVAILABLE FOR SALE					
U.S. Government agency	$18,334,178	$11,688,457	$ 9,637,760	$10,740,335	$19,913,790
Mortgage-backed securities	24,969,846	11,441,115	12,725,553	8,490,125	8,447,886
State and municipal bonds	6,890,713	4,904,648	5,724,959	3,689,859	4,137,433
Corporate bonds	4,133,642	4,788,589	5,621,529	1,514,471	3,036,920
Subtotal	54,328,379	32,822,809	33,709,801	24,434,790	35,536,029
Equity securities	2,065,486	1,966,123	2,224,846	4,660,213	6,952,463
Total available for sale	56,393,865	34,788,932	35,934,647	29,095,003	42,488,492
HELD TO MATURITY					
U.S. Government agency	—	6,460,305	6,456,069	5,000,000	—
Mortgage-backed securities	5,966,091	7,130,202	8,761,200	9,575,713	—
State and municipal bonds	3,912,836	3,912,769	3,912,704	3,912,692	—
Equity securities	495,361	500,000	—	—	—
Total held to maturity	10,374,288	18,003,276	19,129,973	18,488,405	—
Total investment securities	$66,768,153	$52,792,208	$55,064,620	$47,583,408	$42,488,492

Note: Investments classified as available for sale are carried at fair value whereas investments classified as held to maturity are carried at amortized cost.

The following table shows the maturity of the investment portfolio at December 31, 2008:

	Available for Sale			Held to Maturity		
Maturing	*Amortized Cost*	*Fair Value*	*Yield*	*Amortized Cost*	*Fair Value*	*Yield*
Within one year	$ 867,126	$ 875,152	3.49%	$ —	$ —	—%
Over one to five years	4,625,219	4,534,807	6.19	—	—	—
Over five to ten years	5,346,104	5,356,638	5.16	3,912,836	3,892,560	5.53
Over ten years	23,962,298	18,591,936	4.78	495,361	130,745	3.05
	34,800,747	29,358,533		4,408,197	4,023,305	
Mortgage-backed securities	24,688,564	24,969,846	5.81	5,966,091	6,108,552	4.73
Equity securities	1,608,495	2,065,486	3.31	—	—	—
	$61,097,806	$56,393,865		$10,374,288	$10,131,857	

The investment portfolio consists primarily of U. S. Government agency securities, mortgage-backed securities, corporate bonds, state and municipal obligations, and equity securities. The income from state and municipal obligations is exempt from federal income tax. Certain agency securities are exempt from state income taxes. The Company uses its investment portfolio as a source of both liquidity and earnings.

Investment securities increased $14.0 million to $66.8 million at December 31, 2008 compared to $52.8 million at December 31, 2007.

LOANS

The following table represents a breakdown of loan balances at December 31:

	2008	*2007*	*2006*	*2005*	*2004*
Real Estate:					
Residential	$ 77,278,004	$ 66,259,210	$ 55,057,625	$ 53,148,211	$ 55,242,018
Commercial	136,006,919	111,474,356	120,397,988	97,909,115	94,858,597
Construction and land development	30,955,304	35,206,622	29,996,306	37,415,478	17,774,874
Demand and time	37,691,638	46,406,977	51,549,802	56,118,527	46,168,587
Lease financing	29,772	287,519	969,113	1,936,482	3,598,003
Installment	1,731,519	1,989,149	2,030,480	1,415,260	2,084,215
	283,693,156	261,623,833	260,001,314	247,943,073	219,726,294
Allowance for loan losses	(3,179,741)	(3,270,425)	(3,131,021)	(3,337,163)	(3,485,076)
Loans, net	$280,513,415	$258,353,408	$256,870,293	$244,605,910	$216,241,218

Gross loans, excluding loans held for sale, increased $22.1 million or 8.4% from $261.6 million at December 31, 2007 to $283.7 million at December 31, 2008. The increase was in residential lending and commercial real estate lending while construction and land development and demand and time loans decreased. Commercial loans amounted to $204.7 million at December 31, 2008 and were 72% of total loans. Consumer loans amounted to $79.0 million and were 28% of total loans.

The following table shows the contractual maturities and interest rate sensitivities of the Company's loans at December 31, 2008. Some loans may include contractual installment payments that are not reflected in the table until final maturity. In addition, the Company's experience indicates that a significant number of loans will be extended or repaid prior to contractual maturity. Consequently, the table is not intended to be a forecast of future cash repayments.

	Maturing						
	In one year or less		*After 1 through 5 years*		*After 5 years*		
	Fixed	*Variable*	*Fixed*	*Variable*	*Fixed*	*Variable*	*Total*
Real Estate:							
Residential	$1,172,069	$26,457,598	$1,689,138	$5,226,649	$38,215,532	$4,517,018	$77,278,004
Commercial	16,316,296	15,158,345	62,372,217	9,660,125	31,003,845	1,496,091	136,006,919
Construction and land development	8,365,351	13,725,235	4,602,797	2,432,179	1,829,742	—	30,955,304
Demand and time	3,100,464	25,581,635	7,513,265	399,577	1,096,697	—	37,691,638
Lease financing	29,772	—	—	—	—	—	29,772
Installment	490,596	656,583	222,767	—	173,789	187,784	1,731,519
	$29,474,548	$81,579,396	$76,400,184	$17,718,530	$72,319,605	$6,200,893	$283,693,156

The following table provides information concerning nonperforming assets and past due loans at December 31, 2008:

	2008	*2007*	*2006*	*2005*	*2004*
Nonaccrual loans (a)	$5,027,767	$4,819,139	$3,699,397	$1,413,925	$ 615,394
Restructured loans	771,216	178,003	180,686	—	455,864
Foreclosed real estate	1,736,018	—	1,383,163	—	—
	$7,535,001	$4,997,142	$5,263,246	$1,413,925	$1,071,258
Accruing loans past-due 90 days or more	$2,216,728	$ 918,986	$ 436,599	$ 179,012	$1,567,919

(a) Loans are placed in nonaccrual status when they are past-due 90 days as to either principal or interest or when, in the opinion of management, the collection of all interest and/or principal is in doubt. A loan remains in nonaccrual status until the loan is current as to payment of both principal and interest and the borrower demonstrated the ability to pay and remain current. Management may grant a waiver from nonaccrual status for a 90-day past-due loan that is both well secured and in the process of collection.

ALLOWANCE FOR LOAN LOSSES

An allowance for loan losses is maintained to absorb losses in the existing loan portfolio. The allowance is a function of specific loan allowances, general loan allowances based on historical loan loss experience and current trends, and allowances based on general economic conditions that affect the collectibility of the loan portfolio. These can include, but are not limited to exposure to an industry experiencing problems, changes in the nature or volume of the portfolio and delinquency and nonaccrual trends. The portfolio review and calculation of the allowance is performed by management on a continuing basis.

The specific allowance is based on regular analysis of the loan portfolio and is determined by analysis of collateral value, cash flow and guarantor capacity, as applicable. The specific allowance was $290,127, $901,582, and $534,639 as of December 31, 2008, 2007 and 2006, respectively.

The general allowance is calculated using internal loan grading results and appropriate allowance factors on approximately ten classes of loans. This process is reviewed on a regular basis. The allowance factors may be revised whenever necessary to address current credit quality trends or risks associated with particular loan types. Historic trend analysis is utilized to obtain the factors to be applied. The general allowance was $1.6 million, $1.4 million, and $2.0 million as of December 31, 2008, 2007 and 2006, respectively.

Allocation of a portion of the allowance does not preclude its availability to absorb losses in other categories. An unallocated reserve is maintained to recognize the imprecision in estimating and measuring loss when evaluating the allowance for individual loans or pools of loans.

During the years ended December 31, 2004 through 2008, the unallocated portion of the allowance for loan losses has fluctuated with the specific and general allowances so that the total allowance for loan losses would be at a level that management believes is the best estimate of probable future loan losses at the balance sheet date. The specific allowance may fluctuate from period to period if the balance of what management considers problem loans changes. The general allowance will fluctuate with changes in the mix of the Company's loan portfolio, economic conditions, or specific industry conditions. The requirements of the Company's federal regulators are a consideration in determining the required total allowance. Due to the level of the unallocated allowance, management did not make any provision for loan losses in 2006 and 2005.

Management believes that it has adequately assessed the risk of loss in the loan portfolios based on a subjective evaluation and has provided an allowance which is appropriate based on that assessment. Because the allowance is an estimate based on current conditions, any change in the economic conditions of the Company's market area or change within a borrower's business could result in a revised evaluation, which could alter the Company's earnings.

The following charts show the level of loan losses recorded by the Company for the past five years, management's allocation of the allowance for loan losses by type of loan as of the end of each year, and other statistical information. The allocation of the allowance reflects management's analysis of economic risk potential by type of loan, and is not intended as a forecast of loan losses.

	Years ended December 31				
Description	*2008*	*2007*	*2006*	*2005*	*2004*
Balance at beginning of year	$3,270,425	$3,131,021	$3,337,163	$3,485,076	$3,648,245
Charge-offs:					
Demand and time	—	—	—	123,578	192,440
Lease financing	73,821	25,778	154,747	168,823	—
Real estate:					
Residential	498,687	176,881	—	—	7,746
Commercial	518,755	220,640	59,120	—	—
Construction	1,174,879	—	—	—	—
Installment	2,335	19,153	41,967	22,640	76,936
	2,268,477	442,452	255,834	315,041	277,122
Recoveries:					
Demand and time	—	—	—	130,904	67,111
Lease financing	8,309	14,138	16,530	3,980	—
Real estate:					
Residential	4,358	—	—	14,874	8,087
Commercial	9,643	187	6,290	—	—
Construction	32,648	—	—	—	—
Installment	26,835	31,531	26,872	17,370	38,755
	81,793	45,856	49,692	167,128	113,953
Net charge-offs	2,186,684	396,596	206,142	147,913	163,169
Provision charged to operations	2,096,000	536,000	—	—	—
Balance at end of the year	$3,179,741	$3,270,425	$3,131,021	$3,337,163	$3,485,076
Ratio of net charge-offs to average loans outstanding	0.82%	0.15%	0.08%	0.06%	0.08%

A breakdown of the allowance for loan losses is provided in the table below; however, management does not believe that the allowance can be segregated by category with precision. The breakdown of the allowance is based primarily on those factors discussed previously in evaluating the allowance as a whole. Since all of those factors are subject to change, the breakdown is not necessarily indicative of the category of actual or realized credit losses.

Portfolio	2008	2007	2006	2005	2004
Demand and time and lease financing	$ 235,573	$ 807,582	$ 922,612	$ 474,059	$ 589,053
Real estate:					
Residential	702,297	1,258,314	409,684	718,028	587,292
Commercial	1,100,933	687,797	923,453	679,002	1,034,546
Construction and land development	193,471	217,225	230,072	382,204	342,114
Installment	81,642	39,164	49,399	143,318	149,271
Unallocated	865,640	260,343	595,801	940,552	782,800
	$ 3,179,741	$ 3,270,425	$ 3,131,021	$ 3,337,163	$ 3,485,076

The table below provides a percentage breakdown of the loan portfolio by category to total loans at December 31:

Portfolio	*2008*	*2007*	*2006*	*2005*	*2004*
Demand and time and lease financing	13.3%	17.8%	20.2%	23.4%	22.7%
Real estate:					
Residential	27.2	25.3	21.2	21.4	25.1
Commercial	48.0	42.6	46.3	39.6	43.2
Construction and land development	10.9	13.5	11.5	15.1	8.1
Installment	0.6	0.8	0.8	0.5	0.9
	100.0%	100.0%	100.0%	100.0%	100.0%

All loan allowances are subject to regulatory examinations and determinations as to the appropriateness of the methodology and adequacy on an annual basis.

At December 31, 2008 the allowance for loan losses was $3.2 million, a 2.8% decrease from the end of 2007. The ratio of the allowance to total loans was 1.12% at December 31, 2008 and 1.25% at December 31, 2007. The ratio of net loan losses to average loans outstanding for 2008 was 0.82% compared to 0.15% for 2007. The ratio of nonaccrual loans, restructured loans and loans delinquent more than 90 days to total loans and foreclosed real estate increased to 3.42% at December 31, 2008 from 2.26% at the end of 2007. The ratio of real estate loans to total loans increased to 86.1% at the end of 2008 from 81.4% at the end of 2007.

FUNDING SOURCES

DEPOSITS

The following table sets forth the average deposit balances and average rates paid on deposits during the years ended December 31:

	2008		2007		2006	
	Average Balance	*Average Rate*	*Average Balance*	*Average Rate*	*Average Balance*	*Average Rate*
Noninterest-bearing deposits	$ 48,754,626	—%	$ 49,584,706	—%	$ 56,441,180	—%
Interest-bearing deposits:						
NOW accounts	26,840,775	.21	29,273,381	0.21	32,038,917	0.21
Savings accounts	25,474,803	.26	26,446,228	0.27	30,270,796	0.27
Money market accounts	46,737,845	2.18	56,986,611	3.95	51,303,354	3.77
Certificates of deposit	130,592,612	4.19	117,106,699	4.87	101,071,899	4.47
	$278,400,661	2.38%	$279,397,625	2.89%	$271,126,146	2.44%

The following table provides the maturities of certificates of deposit of the Company in amounts of $100,000 or more at December 31, 2008:

Maturing in:	
3 months or less	$ 6,642,951
Over 3 months through 6 months	3,154,269
Over 6 months through 12 months	23,366,570
Over 12 months	14,120,612
	$47,284,402

Total deposits at December 31, 2008 increased by $6.7 million to $292.4 million from the end of 2007. Interest bearing accounts increased by $11 million and noninterest-bearing deposits decreased by $4.3 million.

The Company began offering CDARS deposits to its customers during 2004. This program allows for customers who wish to invest more than the amounts that would normally be covered by FDIC insurance with the Bank. The program is nationwide and allows participating banks to “swap” customer deposits so that no customer has greater than the insurable maximum in one bank, but the customer only deals with his/her own bank. As of December 31, 2008, the Bank had approximately $21.5 million in CDARS deposits, an increase of $7.9 million from December 31, 2007.

BORROWED FUNDS

Borrowed funds consist of securities sold under repurchase agreements, federal funds purchased and borrowings from the FHLB. Securities sold under repurchase agreements are securities sold to the Bank's customers under a continuing "roll-over" contract and mature in one business day. The underlying securities sold are federal agency securities that are segregated from the Company's other investment securities. Federal funds purchased are unsecured, overnight borrowings from other financial institutions.

Information with respect to borrowings is as follows at and for the years ended December 31:

December 31:	*2008*	*2007*	*2006*
Due 2007, 5.50% to 5.51%	$ —	$ —	$17,000,000
Due 2008, 5.19% to 5.51%	—	15,000,000	5,000,000
Due 2009, 0.48% to 2.33%.	21,600,000	—	—
Due 2010, 0.59% to 3.57%	15,500,000	—	—
Due 2011, 3.00% to 4.04%	15,900,000	—	—
Due 2012, 3.18% to 3.52%	9,000,000	—	—
Due 2013, 3.26% to 4.33%	3,230,000	—	—
	$65,230,000	$15,000,000	$22,000,000
Federal funds purchased and securities sold under repurchase agreements	$14,210,755	$14,589,152	$13,405,463
Weighted average interest rate at year-end:			
Advances from the FHLB	2.30%	5.03%	5.43%
Federal funds purchased and securities sold under repurchase agreements	0.003%	4.03%	4.86%
Maximum outstanding at any month-end:			
Advances from the FHLB	$82,550,000	$30,000,000	$40,000,000
Federal funds purchased and securities sold under repurchase agreements	$15,697,045	19,427,144	13,405,463
Average balance outstanding during the year:			
Advances from the FHLB	$51,812,650	$19,753,973	$24,603,287
Federal funds purchased and securities sold under repurchase agreements	$13,404,970	11,914,984	9,040,071
Weighted average interest rate during the year:			
Advances from the FHLB	3.07%	5.58%	5.38%
Federal funds purchased and securities sold under repurchase agreements	1.76%	4.67%	4.66%

Debt retirement expense of $2.3 million was incurred in 2006 due to the restructuring of a $35.0 million FHLBA advance that had a maturity date of February 2, 2010 and an interest rate of 6.84%.

The Company may borrow under available unsecured federal funds line of credit of $5 million and a secured federal funds line of credit of $10 million with other institutions. There was no balance outstanding under these lines at December 31, 2008 and 2007. These lines bear interest at the current federal funds rate of the correspondent bank.

CAPITAL

Bank holding companies and banks are required by the FRB and FDIC to maintain minimum levels of Tier 1 (or Core) and Tier 2 capital measured as a percentage of assets on a risk-weighted basis. Capital is primarily represented by shareholders' equity, adjusted for the allowance for loan losses and certain issues of preferred stock, convertible securities, and subordinated debt, depending on the capital level being measured. Assets and certain off-balance sheet transactions are assigned to one of five different risk-weighting factors for purposes of determining the risk-adjusted asset base. The minimum levels of Tier 1 and Tier 2 capital to risk-adjusted assets are 4% and 8%, respectively, under the regulations.

In addition, the FRB and the FDIC require that bank holding companies and banks maintain a minimum level of Tier 1 (or Core) capital to average total assets excluding intangibles for the current quarter. This measure is known as the leverage ratio. The current regulatory minimum for the leverage ratio for institutions to be considered adequately capitalized is 4%, but could be required to be maintained at a higher level based on the regulator's assessment of an institution's risk profile. The following chart shows the regulatory capital levels for the Company and Bank at December 31, 2008 and 2007. The Company's subsidiary bank also exceeded the FDIC required minimum capital levels at those dates by a substantial margin. Based on the levels of capital, the Company and the Bank are well capitalized.

The following table shows the Company's and the Bank's capital ratios as of December 31:

		Carrollton Bancorp	Carrollton Bank	Carrollton Bancorp	Carrollton Bank
	Minimum	*2008*	*2008*	*2007*	*2007*
Leverage ratio	4%	8.17%	7.37%	10.03%	9.72%
Risk-based capital:					
Tier 1 (Core)	4%	9.84%	9.41%	12.35%	12.20%
Total	8%	10.91%	10.45%	13.63%	13.31%

Total shareholders' equity decreased 23.8% or $8.5 million to $27.4 million at December 31, 2008. The decrease was due primarily to the repurchase of 276,137 shares for $3.9 million, dividends paid of $1.2 million, and a decrease in accumulated other comprehensive income of $4.3 million, all of which was partially offset by net income of $847,000. The decrease in accumulated other comprehensive income was due to the decrease in the fair market value of the available for sale securities, the loss on the frozen defined benefit pension plan partially offset by the increase in the fair market value of the effective cash flow hedge. Under regulatory requirements, amounts reported as accumulated other comprehensive income/loss related to these items do not increase or reduce regulatory capital and are not included in the calculation of risk-based capital and leverage ratios.

LIQUIDITY AND CAPITAL EXPENDITURES

LIQUIDITY

Liquidity describes the ability of the Company to meet financial obligations, including lending commitments and contingencies that arise during the normal course of business. Liquidity is primarily needed to meet the borrowing and deposit withdrawal requirements of the customers of the Company, as well as to meet current and planned expenditures.

The Company's liquidity is derived primarily from its deposit base and equity capital. Liquidity is provided through the Company's portfolios of cash and interest-bearing deposits in other banks, federal funds sold, loans held for sale, unpledged investment securities held to maturity due within one year, and unpledged securities available for sale. Such assets totaled $37.3 million or 9.2% of total assets at December 31, 2008.

The borrowing requirements of customers include commitments to extend credit and the unused portion of lines of credit, which totaled $111.0 million at December 31, 2008. Of this total, management places a high probability of required funding within one year on approximately $60.5 million. The amount remaining is unused home equity lines and other consumer lines on which management places low probability of funding.

The Company also has external sources of funds through the Federal Reserve Bank ("FRB") and FHLB, which can be drawn upon when required. There is a line of credit totaling approximately $64 million with the Federal Home Loan Bank of Atlanta (the "FHLB") based on qualifying loans pledged as collateral. Also the Company can pledge securities at the FRB and FHLB and borrow approximately 97% of the fair market value of the securities. In addition, the Company had $33.7 million of securities pledged at the FHLB under which the Company's subsidiary, Carrollton Bank, could have borrowed approximately $32.7 million. Also, Carrollton Bank has $8.2 million of securities pledged at FRB under which it could have borrowed approximately $8.0 million. Approximately $2.6 million of securities have not been pledged against any borrowings. Outstanding borrowings at the FHLB were $65.2 million at December 31, 2008. Additionally, the Company has an unsecured federal funds line of credit of $5.0 million and a $10.0 secured federal funds line of credit with other institutions. The secured federal funds line of credit with another institution would require Carrollton Bank to transfer securities pledged at the FHLB or FRB to this institution before Carrollton Bank could borrow against this line. There was no balance outstanding under these lines at December 31, 2008. These lines bear interest at the current federal funds rate of the correspondent bank.

CAPITAL EXPENDITURES

Capital expenditures were approximately $489,000 in 2008, $2.3 million in 2007 and $801,000 in 2006. The capital expenditures in 2008 related to renovations at a couple of branches and purchases of equipment, including computer equipment. The capital expenditures in 2007 were principally due to completing the construction of the Cockeysville branch and construction of a new branch in Perry Hall which opened in January 2008. Capital expenditures in 2006 were due to renovations at a couple of branches and partial construction of a new branch in Cockeysville expected to open in the second quarter of 2007.

Capital expenditures are projected to be approximately $1.2 million for fiscal year 2009 for renovations at one of the Company's branch locations, purchases of several ATM's, purchase of hardware, software, cubicles, filing cabinets and storage for the new corporate headquarters.

MARKET RISK AND INTEREST RATE SENSITIVITY

The Company's interest rate risk represents the level of exposure it has to fluctuations in interest rates and is primarily measured as the change in earnings and the theoretical market value of equity that results from changes in interest rates. The Asset/Liability Management Committee of the Board of Directors (the "ALCO") oversees the Company's management of interest rate risk. The objective of the management of interest rate risk is to optimize net interest income during volatile as well as stable interest rate environments while maintaining a balance between the maturity and repricing characteristics of assets and liabilities that is consistent with the Company's liquidity, asset and earnings growth, and capital adequacy goals.

Due to changes in interest rates, the level of income for a financial institution can be affected by the repricing characteristics of its assets and liabilities. At December 31, 2008, the Company is in an asset sensitive position. Management continuously takes steps to reduce higher costing fixed rate funding instruments, while increasing assets that are more fluid in their repricing. An asset sensitive position, theoretically, is favorable in a rising rate environment since more assets than liabilities will reprice in a given time frame as interest rates rise. Management works to maintain a consistent spread between yields on assets and costs of deposits and borrowings, regardless of the direction of interest rates.

In order to partially offset a reduction in interest income in a declining interest rate environment, on December 14, 2005, the Bank purchased a $10.0 million notional amount interest rate Floor with a minimum interest rate (strike rate) of 7.0% based on the U.S. prime rate. The term of the Floor is five years. The Floor will reduce the variability of cash flow from a pool of variable rate loans should the rate index of the loans fall below the predetermined strike rate of the hedge (7%).

The following chart shows the static gap position for interest sensitive assets and liabilities of the Company as of December 31, 2008. The chart is as of a point in time, and reflects only the contractual terms of the loan or deposit accounts in assigning assets and liabilities to the various repricing periods except that deposit accounts with no contractual maturity, such as money market, NOW and savings accounts, have been allocated evenly over a five-year period. In addition, the maturities of investments shown in the gap table will differ from contractual maturities due to anticipated calls of certain securities based on current interest rates. While this chart indicates the opportunity to reprice assets and liabilities within certain time frames, it does not reflect the fact that interest rate changes occur in disproportionate increments for various assets and liabilities.

Period from December 31, 2008 in which assets and liabilities reprice:

(Dollars in thousands)	*0 to 90 days*	*91 to 365 days*	*1 to 2 years*	*3 to 5 years*	*> 5 years*
ASSETS:					
Short term investments	$ 3,665	$ —	$ —	$ —	$ —
Investment securities	2,987	19,924	31,220	8,659	3,978
Loans held for sale	21,701	—	—	—	—
Loans:					
Residential real estate	17,649	42,767	10,739	4,552	1,571
Commercial real estate	16,463	44,031	24,218	40,883	10,412
Construction and land development	7,032	15,020	1,947	4,562	2,394
Demand and time	4,729	24,969	2,190	4,724	1,080
Lease financing	28	2	—	—	—
Installment	103	864	98	65	602
	$ 74,357	$147,577	$ 70,412	$ 63,445	$ 20,037
LIABILITIES:					
Deposits	$ 66,059	$ 81,577	$ 42,396	$ 4,293	$ 98,028
Borrowings	40,311	500	10,500	28,130	—
	$ 106,370	$ 82,077	$ 52,896	$ 32,423	$ 98,028
Gap position					
Period	$ (32,013)	$ 65,500	$ 17,516	$ 31,022	$ (77,991)
% of assets	(7.92%)	16.21%	4.33%	7.68%	(19.30%)
Cumulative	$ (32,013)	$ 33.487	$ 51,003	$ 82,025	$ 4,034
% of assets	(7.92%)	8.29%	12.62%	20.29%	1.00%
Cumulative risk sensitive assets to risk sensitive liabilities	69.91%	117.77%	121.13%	129.96%	101.09%

INFLATION

Inflation may be expected to have an impact on the Company's operating costs and thus on net income. A prolonged period of inflation could cause interest rates, wages, and other costs to increase and could adversely affect the Company's results of operations unless the fees charged by the Company could be increased correspondingly. However, the Company believes that the impact of inflation was not material for 2008, 2007, and 2006.

OFF-BALANCE SHEET ARRANGEMENTS

The Company enters into off-balance sheet arrangements in the normal course of business. These arrangements consist primarily of commitments to extend credit, lines of credit and letters of credit. In addition, the Company has certain operating lease obligations.

Credit commitments are agreements to lend to a customer as long as there is no violation of any condition to the contract. Loan commitments generally have interest rates fixed at current market amounts, fixed expiration dates, and may require payment of a fee. Lines of credit generally have variable interest rates. Such lines do not represent future cash requirements because it is unlikely that all customers will draw upon their lines in full at any time. Letters of credit are commitments issued to guarantee the performance of a customer to a third party.

The Company's exposure to credit loss in the event of nonperformance by the borrower is the contract amount of the commitment. Loan commitments, lines of credit, and letters of credit are made on the same terms, including collateral, as outstanding loans. The Company is not aware of any accounting loss it would incur by funding its commitments.

Outstanding loan commitments, unused lines of credit and letters of credit were as follows at December 31, 2008**:**

Loan commitments	$ 31,395,464
Unused lines of credit	79,654,394
Letters of credit	2,604,489

CONTRACTUAL OBLIGATIONS

The Company enters into contractual obligations in the normal course of business. Among these obligations are short and long-term FHLBA advances, operating leases related to branch and administrative facilities, a long term contract with a data processing provider and purchase contracts related to construction of a new branch office. Payments required under these obligations are set forth in the table below as of December 31, 2008.

Contractual Obligations (Dollars in thousands)	*Total*	*Less than 1 year*	*One to three years*	*Three to five years*	*More than five years*
Federal Home Loan Bank	$ 65,230	$ 21,600	$ 40,400	$ 3,230	—
Federal fund purchased and securities sold under agreement to repurchase	14,211	14,211	—	—	—
Operating lease obligations	13,430	1,179	2,154	1,835	8,262
Purchase obligations(1)	4,942	569	1,190	1,262	1,921
Total	$ 97,813	$ 37,559	$ 43,744	$ 6,327	$10,183

(1) Represents payments required under contract, based on average monthly charges for 2008 and assuming a growth rate of 3%, with the Company's current data processing service provider that expires in October 2016.

NEW ACCOUNTING PRONOUNCEMENTS

In May 2008, the Financial Accounting Standards Board, or FASB, issued FSP APB14-1, *Accounting for Convertible Debt Instruments That May Be Settled In Cash upon Conversion (Including Partial Cash Settlement*), which applies to all convertible debt instruments that have a "net settlement feature", which means instruments that by their terms may be settled either wholly or partially in cash upon conversion. Under FSP APB 14-1, the liability and equity components of convertible debt instruments that may be settled wholly or partially in cash upon conversion must be accounted for separately in a manner reflective of their issuer's nonconvertible debt borrowing rate. Previous guidance provided for accounting of this type of convertible debt instruments entirely as debt. FSP APB 14-1 is effective for financial statements issued for fiscal years beginning after December 15, 2008 and interim periods within those fiscal years. The adoption of this statement will have no affect on the Company's financial statements.

SFAS No. 160, *Noncontrolling Interest in Consolidated Financial Statements*, an amendment of ARB Statement No. 51. SFAS 160 amends Accounting Research Bulletin ("ARB") No. 51, *Consolidated Financial Statements*, to establish accounting and reporting standards for the non-controlling interest in a subsidiary and for the deconsolidation of a subsidiary. SFAS 160 clarifies that a non-controlling interest in a subsidiary, which is sometimes referred to as minority interest, is an ownership interest in the consolidated entity that should be reported as a component of equity in the consolidated financial statements. Among other requirements, SFAS 160 requires consolidated net income to be reported at amounts that include the amounts attributable to both the parent and the non-controlling interest. It also requires disclosure, on the face of the consolidated income statement, of the amounts of consolidated net income attributable to the parent and to the non-controlling interest. SFAS 160 is effective for the Company on January 1, 2009 and is not expected to have a significant impact on the Company's financial statements.

In March 2008, the FASB issued SFAS 161, Disclosures about Derivative Instruments and Hedging Activities, an amendment of FASB Statement No. 133, which enhances the disclosure requirements related to derivative instruments and hedging activity to provide greater transparency about (i) how and why an entity uses derivative instruments, (ii) how derivative instruments and related hedge items are accounted for under SFAS 133 and its related interpretations, and (iii) how derivative instruments and related hedged items affect an entity's financial position, results of operations and cash flows. To meet those objectives, SFAS 161 requires qualitative disclosures about objectives and strategies for using derivatives, quantitative disclosures about fair value amounts of gains and losses on derivative instruments and disclosures about credit-risk-related contingent features in derivative agreements. SFAS 161 is effective for the Company on January 1, 2009 and is not expected to have a significant impact on the Company's financial statements.

SFAS No. 162, "The Hierarchy of Generally Accepted Accounting Principles." SFAS 162 identifies the sources of accounting principles and the framework for selecting the principles to be used in the preparation of financial statements of nongovernmental entities that are presented in conformity with generally accepted accounting principles ("GAAP") in the United States (the GAAP hierarchy). The hierarchical guidance provided by SFAS 162 did not have a significant impact on the Company's financial statements.

FSP No. 132(R)-1 "Employers' Disclosures about Postretirement Benefit Plan Assets." FSP 132(R)-1 provides guidance related to an employer's disclosures about plan assets of defined benefit pension or other post- retirement benefit plans. Under FSP 132(R)-1, disclosures should provide users of financial statements with an understanding of how investment allocation decisions are made, the factors that are pertinent to an understanding of investment policies and strategies, the major categories of plan assets, the inputs and valuation techniques used to measure the fair value of plan assets, the effect of fair value measurements using significant unobservable inputs on changes in plan assets for the period and significant concentrations of risk within plan assets. The disclosures required by FSP 132(R)-1 will be included in the Company's financial statements beginning with the financial statements for the year-ending December 31, 2009.

ITEM 7A: QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

For information regarding the market risk of the Company's financial instruments, see "Market Risk and Interest Rate Sensitivity" in Management's Discussion and Analysis of Financial Condition and Results of Operations in Item 7.

ITEM 8: FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders
Carrollton Bancorp
Baltimore, Maryland

We have audited the accompanying consolidated balance sheets of Carrollton Bancorp and Subsidiary as of December 31, 2008 and 2007, and the related consolidated statements of income, changes in shareholders' equity, and cash flows for each of the three years in the three year period ended December 31, 2008. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with standards of the Public Company Accounting Oversight Board in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform an audit of the Company's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Carrollton Bancorp and Subsidiary as of December 31, 2008 and 2007, and the results of their operations and their cash flows for each of the three years ended December 31, 2008, in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 1 to the financial statements, effective January 1, 2006, the Bank adopted the provisions of Statement of Financial Accounting Standard No. 123R, *Share Based Payment,* and effective December 31, 2006, Statement of Financial Accounting Standards, No. 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans — an amendment of FASB Statement No. 87, 88, 106, and 132(R).*

Rowles & Company, LLP, Certified Public Accountants

Rowles & Company, LLP

Baltimore, Maryland
March 3, 2009

CONSOLIDATED BALANCE SHEETS

	December 31, 2008	December 31, 2007
ASSETS		
Cash and due from banks	$ 6,110,122	$ 9,382,800
Federal funds sold and Federal Home Loan Bank deposit	4,052,166	7,544,181
Federal Home Loan Bank stock, at cost	3,575,700	1,305,100
Investment securities		
Available for sale	56,393,865	34,788,932
Held to maturity	10,374,288	18,003,276
Loans held for sale	21,701,287	7,579,765
Loans, less allowance for loan losses of $3,179,741 and $3,270,425	280,513,415	258,353,408
Premises and equipment	7,012,193	7,198,208
Accrued interest receivable	1,797,241	1,733,672
Bank owned life insurance	4,593,182	4,435,024
Deferred income taxes	3,416,895	762,606
Other real estate owned	1,736,018	—
Other assets	2,904,812	1,762,083
	$404,181,184	$352,849,055
LIABILITIES AND SHAREHOLDERS' EQUITY		
Deposits		
Noninterest-bearing	$ 45,324,537	$ 49,619,610
Interest-bearing	247,028,739	236,019,015
Total deposits	292,353,276	285,638,625
Federal funds purchased and securities sold under agreements to repurchase	14,210,755	14,589,152
Advances from the Federal Home Loan Bank	65,230,000	15,000,000
Accrued interest payable	288,410	221,285
Accrued pension plan	1,968,896	—
Other liabilities	2,739,154	1,468,693
	376,790,491	316,917,755
Shareholders' equity		
Common stock, par $1.00 per share; authorized 10,000,000 shares; issued and outstanding 2,564,988 in 2008 and 2,834,975 in 2007	2,564,988	2,834,975
Additional paid-in capital	15,255,971	18,781,650
Retained earnings	13,252,272	13,654,180
Accumulated other comprehensive income (loss)	(3,682,538)	660,495
	27,390,693	35,931,300
	$404,181,184	$352,849,055

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

CONSOLIDATED STATEMENTS OF INCOME

	Years Ended December 31,		
	2008	2007	2006
INTEREST INCOME			
Interest and fees on loans	$18,657,887	$20,676,380	$20,041,704
Interest and dividends on securities			
Taxable interest income	3,163,838	2,297,626	2,197,049
Nontaxable interest income	345,093	376,199	357,867
Dividends	174,494	145,477	148,259
Interest on federal funds sold and other interest income	65,288	180,678	382,625
Total interest income	22,406,600	23,676,360	23,127,504
INTEREST EXPENSE			
Deposits	6,628,576	8,102,417	6,624,327
Borrowings	1,828,606	1,659,907	2,113,123
Total interest expense	8,457,182	9,762,324	8,737,450
Net interest income	13,949,418	13,914,036	14,390,054
PROVISION FOR LOAN LOSSES	2,096,000	536,000	—
Net interest income after provision for loan losses	11,853,418	13,378,036	14,390,054
NONINTEREST INCOME			
Service charges on deposit accounts	823,978	950,217	1,121,271
Brokerage commissions	681,658	677,647	647,301
Electronic Banking fees	1,826,574	1,879,650	2,045,618
Mortgage banking fees and gains	2,548,417	2,284,988	2,465,814
Other fees and commissions	461,031	481,640	461,841
Gains on security sales	244,036	—	2,157,151
Total noninterest income	6,585,694	6,274,142	8,898,996
NONINTEREST EXPENSES			
Salaries	6,946,000	7,226,753	7,001,847
Employee benefits	1,869,560	1,363,985	1,500,820
Occupancy	2,320,978	2,064,352	1,794,873
Furniture and equipment	636,784	600,654	633,004
Professional services	910,521	1,192,628	521,231
Lease buyout - branch	538,000	—	—
Prepayment penalty	—	—	2,251,971
Check kiting loss	—	—	1,833,733
(Recovery) Impairment of ATM network	—	—	(106,221)
Other noninterest expenses	4,246,221	4,026,769	3,949,745
Total noninterest expenses	17,468,064	16,475,141	19,381,003
Income before income taxes	971,048	3,177,037	3,908,047
INCOME TAXES	124,197	1,050,774	1,323,268
NET INCOME	$ 846,851	$ 2,126,263	$ 2,584,779
NET INCOME PER SHARE — BASIC	$ 0.32	$ 0.75	$ 0.92
NET INCOME PER SHARE — DILUTED	$ 0.32	$ 0.75	$ 0.90

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

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
YEARS ENDED DECEMBER 31, 2008, 2007 AND 2006

	Common Stock	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income(Loss)	Comprehensive Income(Loss)
BALANCE, DECEMBER 31, 2005	$2,809,698	$18,425,528	$11,567,531	$1,837,408	
Net Income	—	—	2,584,779	—	$ 2,584,779
Changes in net unrealized gains (losses) on available for sale securities, net of tax	—	—	—	(1,156,725)	(1,156,725)
Adjustment to initially apply SFAS 158, net of tax effects of $306	—	—	—	484	484
Cash flow hedging derivative	—	—	—	(35,092)	(35,092)
Comprehensive income					$ 1,393,446
Shares acquired and cancelled	(7,518)	(121,332)	—	—	
Stock options exercised including tax benefit of $7,014	4,525	54,708	—	—	
Stock based compensation	—	13,447	—	—	
Cash dividends $0.45 per share	—	—	(1,266,063)	—	
BALANCE, DECEMBER 31, 2006	2,806,705	18,372,351	12,886,247	646,075	
Net Income	—	—	2,126,263	—	$ 2,126,263
Changes in net unrealized gains (losses) on available for sale securities, net of tax	—	—	—	(121,312)	(121,312)
SFAS 158, net of tax effects of $17,785	—	—	—	26,819	26,819
Cash flow hedging derivative	—	—	—	108,913	108,913
Comprehensive income					$ 2,140,683
Shares acquired and cancelled	(16,015)	(248,256)	—	—	
Stock options exercised including tax benefit of $32,790	40,685	584,814	—	—	
Issuance of stock under 2007 Equity Plan	3,600	54,900	—	—	
Stock based compensation	—	17,841	—	—	
Cash dividends, $0.48 per share	—	—	(1,358,330)	—	
BALANCE, DECEMBER 31, 2007	2,834,975	18,781,650	13,654,180	660,495	
Net Income	—	—	846,851	—	$ 846,851
Changes in net unrealized gains (losses) on available for sale securities, net of tax	—	—	—	(3,407,842)	(3,407,842)
SFAS 158, net of tax effects of $776,631	—	—	—	(1,219,569)	(1,219.569)
Cash flow hedging derivative	—	—	—	284,378	284,378
Comprehensive income (loss)					$(3,496,182)
Shares acquired and cancelled	(276,137)	(3,607,733)	—	—	
Stock options exercised including tax benefit of $1,833	2,550	27,939	—	—	
Issuance of stock under 2007 Equity Plan	3,600	46,800	—	—	
Stock based compensation	—	7,315			
Cash dividends, $0.48 per share			(1,248,759)		
BALANCE, DECEMBER 31, 2008	$2,564,988	$15,255,971	$13,252,272	$(3,682,538)	

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

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Years Ended December 31, 2008	2007	2006
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net income	$ 846,851	$ 2,126,263	$ 2,584,779
ADJUSTMENTS TO RECONCILE NET INCOME TO NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES:			
Provision for loan losses	2,096,000	536,000	—
Deprecation and amortization	869,301	847,924	763,749
Deferred income taxes	(1,382,057)	139,538	60,631
Amortization of premiums and discounts	(98,525)	(57,828)	(57,411)
Gains on disposal of securities	(348,318)	—	(2,157,176)
Write down of equity securities	104,282	—	—
(Recovery) impairment of ATM network	—	—	(106,221)
Loans held for sale made, net of principal sold	(14,121,522)	(90,475)	6,277,819
Gains on sale of premises and equipment	—	(5,592)	—
Write down of foreclosed real estate	167,000	—	—
(Gain) loss on sale of foreclosed real estate	(18,981)	127,906	—
Stock based compensation expense	7,315	17,841	13,447
Stock issued under 2007 Equity Plan	50,400	58,500	—
(Increase) decrease in:			
Accrued interest receivable	(63,569)	(20,019)	(294,824)
Prepaid income taxes	(649,190)	—	256,482
Cash surrender value of bank owned life insurance	(158,158)	(155,194)	(156,286)
Other assets	(751,410)	(478,693)	226,026
Increase (decrease) in:			
Accrued interest payable	67,125	6,720	(367,298)
Deferred loan origination fees	(88,255)	(184,808)	(33,566)
Income taxes payable	—	(154,935)	—
Accrued pension plan liability	1,968,896	—	—
Other liabilities	1,344,650	34,083	1,313
Net cash provided by (used in) operating activities	(10,158,165)	2,747,231	7,011,464
CASH FLOWS FROM INVESTING ACTIVITIES:			
Proceeds from sales of securities available for sale	5,369,929	—	2,766,852
Proceeds from maturities of securities available for sale	2,772,957	6,973,048	3,554,884
Proceeds from maturities of securities held to maturity	7,689,223	1,159,552	1,353,243
Redemption (purchase) of Federal Home Loan Bank stock, net	(2,270,600)	399,400	727,100
Purchase of securities available for sale	(35,080,758)	(6,000,000)	(15,030,741)
Purchase of securities held to maturity	—	—	(1,952,570)
Loans made, net of principal collected	(25,412,696)	(579,049)	(12,230,817)
Purchase of premises and equipment	(499.605)	(2,338,287)	(801,823)
Purchase of foreclosed real estate	(922,573)	—	—
Proceeds from sale of premises and equipment	—	20,909	—
Proceeds from sale of foreclosed real estate	283,481	—	—
Net cash (used in) investing activities	(48,070.642)	(364,427)	(21,613,872)
CASH FLOWS FROM FINANCING ACTIVITIES:			
Net increase (decrease) in time deposits	23,356,996	13,519,929	25,486,897
Net increase (decrease) in other deposits	(16,642,345)	(5,785,105)	(19,209,599)
Advances (payment) of Federal Home Loan Bank advance	50,230,000	(7,000,000)	(18,000,000)
Net increase (decrease) in other borrowed funds	(378,397)	1,183,689	2,192,991
Common stock repurchase and retirement	(3,883,870)	(264,271)	(128,850)
Stock options exercised	28,606	592,709	52,219
Income tax benefit from exercise of stock options	1,883	32,790	7,014
Dividends paid	(1,248,759)	(1,358,330)	(1,266,063)
Net cash provided by (used in) financing activities	51,464,114	921,411	(10,865,391)
Net increase (decrease) in cash and cash equivalents	(6,764,693)	3,304,215	(25,467,799)
Cash and cash equivalents at beginning of year	16,926,981	13,622,766	39,090,565
Cash and cash equivalents at end of year	$ 10,162,288	$ 16,926,981	$ 13,622,766
SUPPLEMENTAL INFORMATION:			
Interest paid on deposits and borrowings	$ 8,390,057	$ 9,755,604	$ 9,104,758
Income taxes paid	$ 872,387	$ 1,205,709	$ 837,661
NONCASH ACTIVITY:			
Transfer of loans to foreclosed real estate	$ 1,244,945	$ —	$ 1,383,163
Foreclosed real estate financed	$ —	$ 1,327,175	$ —

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting and reporting policies of Carrollton Bancorp and subsidiary (the "Company") conform to U.S. generally accepted accounting principles. The following is a description of the more significant of these policies.

Organization

The Company was formed January 11, 1990 and is a Maryland corporation chartered as a bank holding company. The Company holds all the issued and outstanding shares of common stock of Carrollton Bank (the "Bank"). The Bank is a Maryland company that engages in general commercial banking operations. Deposits in the Bank are insured, subject to regulatory limitations, by the Federal Deposit Insurance Corporation (the "FDIC").

The Bank provides commercial and brokerage services to individuals and small and medium-sized businesses. Services offered by the Bank include a variety of loans and a broad spectrum of commercial and consumer financial services.

Basis of Presentation

The consolidated financial statements are prepared in conformity with U.S. generally accepted accounting principles and include all accounts of the Company and its wholly-owned subsidiary, Carrollton Bank. All significant intercompany accounts and transactions have been eliminated in the consolidated financial statements. Certain amounts for prior years have been reclassified to conform to the presentation for 2008. These reclassifications have no effect on stockholders' equity or net income as previously reported.

Use of Estimates

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

Material estimates that are particularly susceptible to significant change in the near-term relate to the determination of the allowance for loan losses (the "Allowance"), and other than temporary impairment of investment securities. In connection with the determination of the Allowance, management prepares fair value analyses and obtains independent appraisals as necessary. Management believes that the Allowance is sufficient to address the losses inherent in the current loan portfolio. While management uses available information to recognize losses on loans, future additions to the Allowance may be necessary based on changes in economic conditions. In addition, various regulatory agencies, as an integral part of their examination processes, periodically review the Bank's Allowance. Such agencies may require the Bank to recognize additions to the Allowance based on their judgments about information available to them at the time of their examinations.

Securities are evaluated periodically to determine whether a decline in their value is other than temporary. The term "other than temporary" is not intended to indicate a permanent decline in value. Rather, it means that the prospects for near term recovery of value are not necessarily favorable, or that there is a lack of evidence to support fair values equal to, or greater than, the carrying value of the investment. Management reviews criteria such as the magnitude and duration of the decline, as well as the reasons for the decline, to predict whether the loss in value is other than temporary. Once a decline in value is determined to be other than temporary, the value of the security is reduced and a corresponding charge to earnings is recognized.

Fair Value

Effective January 1, 2008, the Company adopted Statement of Financial Accounting Standard No. 157, Fair Value Measurements, or SFAS 157, which establishes a framework for measuring fair value and requires enhanced disclosures about fair value measurements. In accordance with Financial Accounting Standards Board Staff Position ("FSP") No. SFAS 157-2, "Effective Date of FASB Statement No. 157," the Company will delay application of SFAS 157 for non-financial assets and non-financial liabilities, until January 1, 2009. SFAS 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles and expands disclosures about fair value measurements. The application of SFAS 157 in situations where the market for a financial asset is not active was clarified by the issuance of FSP No. SFAS 157-3, "Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active," in October 2008. FSP No. SFAS 157-3 became effective immediately and required the use of level 3 inputs for the five TRUP CDOs securities.

SFAS 157 clarifies that fair value is an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. SFAS 157 also requires disclosure about how fair value is determined for assets and liabilities and establishes a hierarchy for which these assets and liabilities must be grouped, based on significant levels of inputs. See Note 20 for more information, including a listing of our assets and liabilities required to be measured at fair value on a recurring basis and where they are classified within the hierarchy as of December 31, 2008.

In February 2007, the FASB issued Statement No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities." The standard provides companies with an option to report selected financial assets and liabilities at fair value and establishes presentation and disclosure requirements designed to facilitate comparisons between companies that choose different measurement attributes for similar types of assets and liabilities. The new standard was effective for the Company on January 1, 2008. The Company did not elect the fair value option for any financial assets or financial liabilities as of January 1, 2008.

Cash and Cash Equivalents

For purposes of the Consolidated Statements of Cash Flows, cash and cash equivalents include cash and due from banks, federal funds sold and interest-bearing deposits with banks.

Federal funds sold are carried at cost, which approximates fair value, and are generally sold for one-day periods.

Federal Home Loan Bank Stock

Federal Home Loan Bank stock is carried at cost, which approximates fair value.

Investment Securities Available for Sale

Securities available for sale are acquired as part of the Company's asset/liability management strategy and may be sold in response to changes in interest rates, loan demand, changes in prepayment risk and other factors. Securities available for sale are recorded at their fair value. Unrealized holding gains or losses, net of the related tax effect, are excluded from earnings and reported as an item of other comprehensive income until realized. The carrying values of securities available for sale are adjusted for premium amortization to the earlier of the maturity or expected call date and discount accretion to the maturity date. Realized gains and losses, using the specific identification method, are included as a separate component of noninterest income. Related interest and dividends are included in interest income. Declines in the fair value of individual available for sale securities below their cost that are other than temporary result in write-downs of the individual securities to their fair value. Factors affecting the determination of whether an other-than-temporary impairment has occurred include a downgrading of the security by a rating agency, a significant deterioration in the financial condition of the issuer, or that management would not have the intent and ability to hold a security for a period of time sufficient to allow for any anticipated recovery in fair value.

Equity securities represent the stock of various financial institutions.

Investment Securities Held to Maturity

Investment securities held to maturity are those securities which the Company has the ability and positive intent to hold until maturity. Securities so classified at the time of purchase are recorded at cost. Carrying values of securities held to maturity are adjusted for premium amortization to the earlier of the maturity or expected call date and discount accretion to the maturity date. Declines in the fair value of individual held to maturity securities below their cost, that are other than temporary, result in write-downs of the individual securities to their fair value. Factors affecting the determination of whether an other-than-temporary impairment has occurred include a downgrading of the security by the rating agency, a significant deterioration in the financial condition of the issuer, or that management would not have the ability to hold a security for a period of time sufficient to allow for any anticipated recovery in fair value.

Loans Held for Sale

Residential mortgage loans originated for sale are carried at the lower of cost or market, which may be indicated by the committed sale price, determined on an individual basis.

Loans Receivable

Loans are stated at the amount of unpaid principal adjusted for deferred origination fees and costs and the allowance for loan losses. Deferred origination fees and costs are recognized as an adjustment of the related loan yield using the interest method. The Company determines the delinquency status of loans based on contractual loan terms. Loans are generally placed in nonaccrual status when they are past-due 90 days as to either principal or interest or when, in the opinion of management, the collection of all interest and/or principal is in doubt. A loan remains in nonaccrual status until the loan is current as to payment of both principal and interest and the borrower demonstrates the ability to pay and remain current. Management may grant a waiver from nonaccrual status for a 90-day past-due loan that is both well secured and in the process of collection.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

A loan is considered to be impaired when, based on current information and events, it is probable that the Company will be unable to collect all amounts due according to the contractual terms of the loan agreement. A loan is not considered impaired during a period of delay in payment if the Company expects to collect all amounts due, including interest past-due. The Company generally considers a period of delay in payment to include delinquency up to 90 days.

In accordance with Statement of Financial Accounting Standards ("SFAS") No. 114, *Accounting by Creditors for Impairment of a Loan*, the Company measures impaired loans: (i) at the present value of expected cash flows discounted at the loan's effective interest rate; (ii) at the observable market price; or (iii) at the fair value of the collateral if the loan is collateral dependent. If the measure of the impaired loan is less than the recorded investment in the loan, an impairment is recognized through a valuation allowance and corresponding provision for loan losses.

SFAS 114 does not apply to larger groups of smaller-balance homogeneous loans such as consumer installment loans. These loans are collectively evaluated for impairment. The Company's impaired loans are, therefore, comprised primarily of commercial loans, including commercial mortgage loans, and real estate development and construction loans. In addition, impaired loans are generally loans which management has placed in nonaccrual status. The Company recognizes interest income for impaired loans consistent with its method for nonaccrual loans. Specifically, interest payments received are normally applied to principal. An impaired loan is charged off when the loan, or a portion thereof, is considered uncollectible.

The Company provides for loan losses through the establishment of the Allowance by provisions charged against earnings. The Company's objective is to ensure that the Allowance is adequate to cover probable loan losses inherent in the loan portfolio at the date of each balance sheet. Management considers a number of factors in estimating the required level of the Allowance. These factors include: historical loss experience in the loan portfolios; the levels and trends in past-due and nonaccrual loans; the status of nonaccrual loans and other loans identified as having the potential for further deterioration; credit risk and industry concentrations; trends in loan volume; the effects of any changes in lending policies and procedures or underwriting standards; and, a continuing evaluation of the economic environment. The Company's estimate of the required allowance is subject to revision as these factors change and is sensitive to the effects of the economic and market conditions on borrowers. Loan losses are charged against the Allowance when management believes the uncollectibility of the loan is confirmed. Subsequent recoveries, if any, are credited to the Allowance.

Other Real Estate Owned (OREO)

OREO is comprised of properties acquired in partial or total satisfaction of problem loans. The properties are recorded at the lower of cost or estimated fair value less selling costs. Losses incurred at the time of acquisition of the property are charged to the allowance for loan losses. Subsequent write-downs are included in noninterest expense along with operating income and expenses of such properties and gains or losses realized upon disposition.

Premises and Equipment

Premises and equipment are stated at cost less accumulated depreciation and amortization. Depreciation and amortization are charged to noninterest expenses. Depreciation generally is computed on the straight-line basis over the estimated useful lives of the assets, which generally range from three to ten years for furniture and equipment, three to five years for computer software and hardware, and ten to forty years for buildings and leasehold improvements. Leasehold improvements are generally amortized over the terms of the related leases or the lives of the assets, whichever is shorter. The costs of significant purchases, renewals and betterments are capitalized, while the costs of ordinary maintenance and repairs are expensed as incurred and included in noninterest expense.

Bank Owned Life Insurance

The Company purchased insurance on the lives of certain groups of employees. The policies accumulate asset values to meet future liabilities. Increases in the cash surrender value are recorded in noninterest income in the Consolidated Statements of Income.

Income Taxes

The Company and its subsidiary file a consolidated federal income tax return. Deferred income taxes are recognized for the tax consequences of temporary differences between financial statement carrying amounts and the tax basis of assets and liabilities based on enacted tax rates expected to be in effect when such amounts are realized or settled.

Intangible Assets

A deposit intangible asset of $1,847,700, relating to a branch acquisition, is being amortized using the straight-line method over 15 years. The remaining unamortized balance at December 31, 2008 and 2007 was $184,761 and $307,936, respectively. Amortization expense was $123,170 for 2008, 2007, and 2006, respectively.

The Company capitalizes the value of loan servicing retained on loan sales, and amortizes the value over the estimated life of the portfolio of loans serviced.

Intangible assets are included in “Other assets” on the Consolidated Balance Sheets. Management evaluates intangible assets for impairment quarterly.

Derivative Instruments and Hedging Activities

The Company accounts for derivative instruments and hedging activities utilizing guidelines established in the Financial Accounting Standards Board (“FASB”) Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities*, as amended. The Company recognizes all derivatives as either assets or liabilities on the balance sheet and measures those instruments at fair value. Changes in fair value of derivatives designated and accounted for as cash flow hedges, to the extent they are effective as hedges, are recorded in “Other Comprehensive Income,” net of deferred taxes. Any hedge ineffectiveness would be recognized in the income statement line item pertaining to the hedged item.

Management periodically reviews contracts from various functional areas of the Company to identify potential derivatives embedded within selected contracts. Management has identified potential embedded derivatives in certain loan commitments for residential mortgages where the Company has intent to sell to an outside investor. Due to the short-term nature of these loan commitments and the minimal historical dollar amount of commitments outstanding, the corresponding impact on the Company’s financial condition and results of operation has not been material.

The Company entered into an interest rate Floor transaction on December 14, 2005. The Floor has a notional amount of $10.0 million with a minimum interest rate of 7.00% based on U.S. prime rate and was initiated to hedge exposure to the variability in the future cash flows derived from adjustable rate home equity loans in a declining interest rate environment. The Floor has a term of five years. This interest rate Floor is designated a cash flow hedge, as it is designed to reduce variation in overall changes in cash flow below the above designated strike level associated with the first Prime based interest payments received each period on its then existing loans. The interest rate of these loans will change whenever the repricing index changes, plus or minus a credit spread (based on each loan’s underlying credit characteristics), until the maturity of the interest rate Floor. Should the Prime rate index fall below the strike level of the Floor prior to maturity, the Floor’s counterparty will pay the Bank the difference between the strike rate and the rate index multiplied by the notional value of the Floor multiplied by the number of days in the period divided by 360 days. The fair value of the Floor will be recorded as “Other Assets” and changes in the fair value will be recorded as “Other Comprehensive Income” a component of shareholders’ equity.

Per Share Data

Basic net income per share is determined by dividing net income by the weighted average number of common shares outstanding giving retroactive effect to any stock dividends and splits declared. Diluted earnings per share is determined by adjusting average shares of common stock outstanding by the potentially dilutive effects of stock options outstanding. The dilutive effects of stock options are computed using the treasury stock method.

Comprehensive Income

Comprehensive income includes all changes in shareholders’ equity during a period, except those relating to investments by and distributions to shareholders. The Company’s comprehensive income consists of net earnings, unrealized gains and losses on securities available for sale, changes in the fair value of the Floor and the adjustment from the adoption of SFAS No. 158, *Employees Accounting for Defined Benefit Pension and Other Post Retirement Plans* as of December 31, 2006, and is presented in the statements of shareholders’ equity. Accumulated other comprehensive income is displayed as a separate component of shareholders’ equity.

Stock-based Compensation

At the Company’s annual shareholders meeting on May 15, 2007, the 2007 Equity Plan was approved. This Plan provides for the issuance of stock options, stock appreciation rights (SARs), restricted stock, restricted performance stock, unrestricted Company stock and performance unit awards to directors, officers and other eligible employees and makes available 500,000 shares for issuance. The Plan provides for automatic annual grants of 300 shares of unrestricted stock of the Company to each non-employee director. Also, in accordance with the 2007 Equity Plan, 300 shares of unrestricted Common Stock were issued to each non-employee director in May 2008 and 2007. No new grants will be made under the 1998 Long Term Incentive Plan. However, incentive stock options issued under the 1998 plan will remain outstanding until exercised or until the tenth anniversary of the grant date of such options.

On January 1, 2006, the Company adopted the provisions of FASB Statement No. 123 (R), *Share-Based Payment,* which requires companies to recognize expense related to the fair value of stock-based compensation. Prior to January 1, 2006, the Company accounted for stock-based compensation under the recognition and measurement provisions of Accounting

Principles Board ("APB") Opinion No. 25, Accounting for Stock Issued to Employees, and related Interpretations, as permitted by FASB Statement No. 123, Accounting for Stock-Based Compensation. In accordance with APB No. 25, no compensation cost was required to be recognized for options granted that had an exercise price equal to the market value of the underlying common stock on the date of the grant.

The Company adopted SFAS 123 (R) using the modified prospective transition method. Under this transition method, compensation cost recognized for the year ended December 31, 2006 includes: a) compensation cost for all share-based compensation granted prior to, but not vested as of January 1, 2006, based on the grant-date fair value estimated in accordance with the original provisions of SFAS 123, and b) compensation cost for all share-based compensation granted subsequent to January 1, 2006, based on the grant-date fair value estimated in accordance with the provisions of SFAS 123 (R). Prior to January 1, 2006, no compensation expense was recognized for stock option grants, as all such grants had an exercise price equal to the fair market value on the date of the grant.

In December 2005, the Company authorized the grant of 42,000 options to officers and the immediate vesting of such options. All outstanding options to officers where the exercise price of the option exceeded the fair market value of the Company's stock were also approved for accelerated vesting. This resulted in 75,500 options becoming vested in 2005 that would have otherwise vested in future years.

As a result of adopting SFAS 123R on January 1, 2006, incremental stock-based compensation expense recognized was $7,315 and $17,841 during 2008 and 2007. As of December 31, 2008, there was $2,123 of unrecognized compensation expense related to nonvested stock options, which will be recognized over the remaining vesting period.

2. CASH AND DUE FROM BANKS

The Bank is required by the Federal Reserve System to maintain certain reserve balances based principally on deposit liabilities. At December 31, 2008 and 2007, the required reserve balances were $1.6 million and $1.2 million, respectively. The Company sells federal funds on an unsecured basis to its correspondent banks. Average balances sold were $2.5 million in 2008 and $3.5 million in 2007.

3. INVESTMENT SECURITIES

Investment securities are summarized as follows:

	Amortized cost	*Unrealized gains*	*Unrealized losses*	*Fair value*
December 31, 2008				
AVAILABLE FOR SALE				
U.S. government agency	$18,103,498	$ 230,681	$ —	$18,334,178
Mortgage-backed securities	24,688,564	859,292	578,010	24,969,846
State and municipal	7,033,219	20,282	162,788	6,890,713
Corporate bonds	9,664,031	—	5,530,389	4,133,642
	59,489,312	1,110,255	6,271,187	54,328,379
Equity securities	1,608,495	539,982	82,991	2,065,486
	$61,097,807	$1,650,237	$6,354,178	$56,393,865
HELD TO MATURITY				
U.S. government agency	$ —	$ —	$ —	$ —
Mortgage-backed securities	5,966,091	144,174	1,714	6,108,552
State and municipal	3,912,836	—	20,277	3,892,560
Corporate bonds	495,361	—	364,616	130,745
	$10,374,288	$ 144,174	$ 386,607	$10,131,857

3. Investment Securities *(Continued)*

	Amortized cost	*Unrealized gains*	*Unrealized losses*	*Fair value*
December 31, 2007				
AVAILABLE FOR SALE				
U.S. government agency	$11,293,966	$ 394,491	$ —	$11,688,457
Mortgage-backed securities	11,324,751	160,986	(44,622)	11,441,115
State and municipal	4,874,900	34,250	(4,502)	4,904,648
Corporate bonds	5,243,111	—	(454,522)	4,788,589
	32,736,728	589,727	(503,646)	32,822,809
Equity securities	1,140,856	864,905	(39,638)	1,966,123
	$33,877,584	$1,454,632	$(543,284)	$34,788,932
HELD TO MATURITY				
U.S. government agency	$ 6,460,305	$ 40,160	$ —	$ 6,500,465
Mortgage-backed securities	7,130,202	13,678	(36,908)	7,106,972
State and municipal	3,912,769	33,641	—	3,946,010
Corporate bonds	500,000	—	(56,250)	443,750
	$18,003,276	$ 87,479	$ (93,158)	$17,997,197

Information related to unrealized losses in the portfolio as of December 31, 2008 follows:

	Less than 12 months		12 months or longer		Total	
	Fair Value	*Unrealized Losses*	*Fair Value*	*Unrealized Losses*	*Fair Value*	*Unrealized Losses*
Mortgage-backed securities	$2,816,406	$ (481,503)	$ 2,684,751	$ (98,221)	$ 5,501,157	$ (579,724)
State and municipal	—	—	8,991,576	(183,065)	8,991,576	(183,065)
Corporate bonds	2,594,407	$ (5,769,254)	1,669,980	(125,751)	4,264,387	(5,895,005)
Equity securities	—	—	396,816	(82,991)	396,816	(82,991)
	$5,410,813	$ (6,250,757)	$13,743,123	$(490,028)	$19,153,936	$(6,740,785)

Contractual maturities of debt securities at December 31, 2008 and 2007 are shown below. Actual maturities may differ from contractual maturities because borrowers have the right to call or prepay obligations with or without call or prepayment penalties.

	December 31, 2008			
	Available for sale		Held to maturity	
Maturing	*Amortized Cost*	*Fair Value*	*Amortized Cost*	*Fair Value*
Within one year	$ 867,126	$ 875,152	$ —	$ —
Over one to five years	4,625,219	4,534,807	—	—
Over five to ten years	5,346,104	5,356,638	3,912,836	3,892,560
Over ten years	23,962,298	18,591,936	495,361	130,745
Mortgage-backed securities	24,688,564	24,969,846	5,966,091	6,108,552
	$59,489,312	$54,328,379	$10,374,288	$10,131,857

	December 31, 2007			
	Available for sale		Held to maturity	
Maturing	*Amortized Cost*	*Fair Value*	*Amortized Cost*	*Fair Value*
Within one year	$ 5,503,111	$ 5,050,273	$ 500,000	$ 443,750
Over one to five years	2,984,706	3,010,030	—	—
Over five to ten years	3,435,926	3,575,687	9,962,551	10,031,598
Over ten years	9,488,234	9,745,704	410,523	415,278
Mortgage-backed securities	11,324,751	11,441,115	7,130,202	7,106,972
	$32,736,728	$32,822,809	$18,003,276	$17,997,598

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.

At December 31, 2008, the Company owned five collateralized debt obligation securities that are backed by trust preferred securities issued by banks, thrifts, and insurance companies ("TRUP CDOs"). The market for these securities at December 31, 2008 was not active and markets for similar securities were also not active. The inactivity was evidenced first by a significant widening of the bid-ask spread in the brokered markets in which TRUP CDOs trade and then by a significant decrease in the volume of trades relative to historical levels. The new issue market is also inactive as no new TRUP CDOs have been issued since 2007. There are currently very few market participants who are willing or able to transact for these securities.

The market values for these securities (and any securities other than those issued or guaranteed by the U.S. Treasury) are very depressed relative to historical levels. For example, the yield on spreads for the broad market of investment grade and high yield corporate bonds reached all time wide levels versus U.S. Treasuries at the end of November 2008 and remain near those levels today. Thus, in today's market, a low market price for a particular bond may only provide evidence of stress in the credit markets in general versus being an indicator of credit problems with a particular issuer.

Given conditions in the debt markets today and the absence of observable transactions in the secondary and new issue markets, we determined:

- The few observable transactions and market quotations that are available are not reliable for purposes of determining fair value at December, 31, 2008;
- An income valuation approach technique (present value technique) that maximizes the use of relevant observable inputs and minimizes the use of unobservable inputs will be equally or more representative of fair value than the market approach valuation technique used at prior measurement dates; and
- Our TRUP CDOs will be classified within Level 3 of the fair value hierarchy because we determined that significant adjustments are required to determine fair value at the measurement date.

Our TRUP CDO valuations were prepared by an independent third party. Their approach to determining fair value involved these steps:

1. The credit quality of the collateral is estimated using average probability of default values for each issuer (adjusted for rating levels).
2. The default probabilities also considered the potential for correlation among issuers within the same industry (e.g. banks with other banks).
3. The loss given default was assumed to be 95% (i.e. a 5% recovery).
4. The cash flows were forecast for the underlying collateral and applied to each CDO tranche to determine the resulting distribution among the securities.
5. The expected cash flows were discounted to calculate the present value of the security.
6. The calculations were modeled in several thousand scenarios using a Monte Carlo engine and the average price was used for valuation purposes.

3. INVESTMENT SECURITIES *(CONTINUED)*

7. The effective discount rates on an overall basis range from 7% to 31% and are highly dependent upon the credit quality of the collateral, the relative position of the tranche in the capital structure of the TRUP CDO and the prepayment assumptions.

During 2008, the Company wrote down two equity securities for $104,282. At December 31, 2008, seven marketable equity securities had unrealized losses of approximately $83,000 from the Company's cost basis. At December 31, 2007, five marketable equity securities had unrealized losses of approximately $40,000 from the Company's cost basis. No credit issues in the remaining equity securities have been identified that cause management to believe the decline in market value is other than temporary. In analyzing the issuer's financial condition, management considers industry analysis reports, financial performance and projected target prices of investment analysts within a one-year time frame. Unrealized losses on marketable equity securities that are in excess of 50% of cost, and that have been sustained for more than 24 months, are generally recognized by management as being other than temporary and charged to earnings, unless evidence exists to support a realizable value equal to or greater than the Company's carrying value of the investment.

All unrealized losses on U.S. government agency, mortgage-backed securities, state and municipal securities and corporate bonds as of December 31, 2008 are considered to be temporary losses, because each security will be redeemed at face value at, or prior to maturity. In most cases, the temporary impairment in value is caused by market interest rate fluctuations.

At December 31, 2008 and 2007, securities with an amortized cost of $64.5 million (fair value of $59.7 million) and $16.6 million (fair value of $16.5 million), respectively, were pledged as collateral for government deposits, securities sold under repurchase agreements, advances from the Federal Home Loan Bank, and borrowings from the FRB. At December 31, 2008, there were no borrowings against the securities pledged at the FRB.

In 2008, the Company realized gross gains on sales of or call of securities purchased at a discount of $347,510. These gains were partially offset by the $104,282 write down of equity securities. There were no sales of securities in 2007. In 2006 the Company realized gross gains on sales of securities of $2.2 million. There were no realized losses in 2006. Income taxes on net security gains in 2008 and 2006 were $31,000 and $730,000, respectively.

4. LOANS

Major classifications of loans at December 31 are as follows:

	2008	*2007*
Real estate:		
Residential	$77,278,004	$ 66,259,210
Commercial	136,006,919	111,474,356
Construction and land development	30,955,304	35,206,622
Demand and time	37,691,638	46,406,977
Lease financing	29,772	287,519
Installment	1,731,519	1,989,149
	283,693,156	261,623,833
Allowance for loan losses	(3,179,741)	(3,270,425)
Loans, net	$280,513,415	$258,353,408

The Bank makes loans to customers located in Maryland, Virginia, Pennsylvania and Delaware. Although the loan portfolio is diversified, its performance will be influenced by the regional economy.

The maturity and rate repricing distribution of the loan portfolio at December 31 is as follows:

	2008	*2007*
Repricing or maturing within one year	$111,053,944	$111,657,455
Maturing over one to five years	94,118,714	84,060,030
Maturing over five years	78,520,498	65,906,348
	$283,693,156	$261,623,833

4. Loans (Continued)

Loan balances have been adjusted by the following deferred amounts as of December 31:

	2008	*2007*
Deferred origination costs and premiums	$904,499	$738,614
Deferred origination fees and unearned discounts	(947,080)	(869,450)
Net deferred fees	$(42,581)	$(130,836)

Transactions in the allowance for loan losses for the years ended December 31 were as follows:

	2008	*2007*	*2006*
Beginning balance	$3,270,425	$3,131,021	$3,337,163
Provision charged to operations	2,096,000	536,000	—
Recoveries	81,793	45,856	49,692
	5,448,218	3,712,877	3,386,855
Loans charged off	2,268,477	442,452	255,834
Ending balance	$3,179,741	$3,270,425	$3,131,021

Nonperforming assets and loans past-due 90 days or more but accruing interest were as follows at December 31:

	2008	*2007*	*2006*
Nonaccrual loans	$5,027,767	$4,819,139	$3,699,397
Restructured loans	771,216	178,003	180,686
Foreclosed real estate	1,736,018	—	1,383,163
Total nonperforming assets	$7,535,001	$4,997,142	$5,263,246
Accruing loans past-due 90 days or more	$2,216,728	$ 918,986	$ 436,599
Unrecorded interest on nonaccrual loans	$ 296,553	$ 458,797	$ 76,044
Interest income recognized on nonaccrual loans	$ 281,237	$ 88,384	$ 300,650

At December 31, 2008, the Company had eleven impaired loans totaling approximately $1,554,000, all of which had been classified as non-accrual. The valuation allowance for impaired loans was $290,127 at December 31, 2008.

The average balance of impaired loans amounted to approximately $3.6 million in 2008. During 2008, the Company received total payments on impaired loans of $1.9 million. Of this amount, $133,000 was recorded as interest income for 2008. The remainder was applied to reduce principal.

At December 31, 2007, the Company had nine impaired loans totaling approximately $3,640,000, all of which had been classified as non-accrual. The valuation allowance for impaired loans was $901,652 at December 31, 2007.

The average balance of impaired loans amounted to approximately $3.9 million in 2007. During 2007, the Company received total payments on impaired loans of $669,083. Of this amount, $52,454 was recorded as interest income for 2007. The remainder was applied to reduce principal.

At December 31, 2006 there were no impaired loans.

Loans with a balance of approximately $109.9 million and $97.3 million were pledged as collateral to the Federal Home Loan Bank of Atlanta as of December 31, 2008 and 2007, respectively. At December 31, 2008 and 2007, the Company serviced loans for others totaling $498,000 and $727,000, respectively.

5. Credit Commitments

Outstanding loan commitments, unused lines of credit, and letters of credit were as follows as of December 31:

	2008	*2007*	*2006*
LOAN COMMITMENTS			
Mortgage loans	$ 4,847,310	$ 4,347,755	$ 4,122,697
Construction and land development	23,864,454	17,688,330	29,501,299
Commercial loans	2,683,700	21,303,360	6,840,000
	$31,395,464	$43,339,445	$40,463,996
UNUSED LINES OF CREDIT			
Home equity lines	$40,965,247	$43,371,236	$46,199,911
Commercial lines	37,517,960	39,801,481	44,279,428
Unsecured consumer lines	1,171,187	1,144,641	1,084,048
	$79,654,394	$84,317,358	$91,563,387
LETTERS OF CREDIT	$ 2,604,489	$ 2,546,445	$ 2,223,755

Loan commitments and lines of credit are agreements to lend to a customer as long as there is no violation of any condition to the contract. Loan commitments generally have interest rates fixed at current market amounts, fixed expiration dates, and may require payment of a fee. Lines of credit generally have variable interest rates. Such lines do not represent future cash requirements because it is unlikely that all customers will draw upon their lines in full at any time. Letters of credit are commitments issued to guarantee the performance of a customer to a third party.

The Company's exposure to credit loss in the event of nonperformance by the borrower is the contract amount of the commitment. Loan commitments, lines of credit, and letters of credit are made on the same terms, including collateral, as outstanding loans. The Company is not aware of any accounting loss it would incur by funding the above commitments.

6. Related Party Transactions

The Company's executive officers and directors, or other entities, to which they are related, enter into loan transactions with the Bank in the ordinary course of business. The terms of these transactions are similar to the terms provided to other borrowers entering into similar loan transactions and do not involve more than normal risk of collectibility. During the years ended December 31, 2008, 2007 and 2006, transactions in related party loans were as follows:

	2008	*2007*	*2006*
Beginning balance	$4,423,636	$ 7,976,614	$ 1,894,784
Additions	693,468	629,259	7,918,876
Repayments	(2,328,636)	(4,182,237)	(1,837,046)
Ending balance	$2,788,468	$ 4,423,636	$ 7,976,614

A director of the Company is a partner in a law firm that provides legal services to the Company and the Bank. During the years ended December 31, 2008, 2007, and 2006, amounts paid to the law firm in connection with those services were approximately $381,000, $358,000, and $195,000, respectively.

A director of the Company is President of an insurance brokerage through which the Company and the Bank place various insurance policies. During the years ended December 31, 2008, 2007, and 2006, amounts paid to the insurance brokerage for insurance premiums were approximately $214,000, $112,000, and $282,000, respectively.

A director of the Company is President of an electrical company through which the Company and the Bank may contract for electrical services. No such services were performed in 2008, 2007 or 2006.

A director of the Company is the Executive Vice President for a commercial real estate services company, through which the Company and the Bank contracted for appraisal and management services. In late 2006 and 2007, contracts for the construction of two branches were awarded on a competitive bid basis to a related party. Contract payments totaling approximately $126,562 in 2008, $1.5 million in 2007, and $356,000 in 2006 were paid to the related party.

The Bank routinely enters into deposit relationships with its directors, officers and employees in the normal course of business. These deposits bear the same terms and conditions of those prevailing at the time for comparable transactions with

6. Related Party Transactions (Continued)

unrelated parties. Balances of executive officers and directors on deposits as of December 31, 2008 and 2007 were $2.7 million and $2.0 million, respectively.

7. Premises and Equipment

A summary of premises and equipment is as follows as of December 31:

	2008	*2007*
Land and improvements	$ 909,544	$ 909,544
Buildings	4,671,416	4,607,893
Leasehold improvements	3,494,431	3,686,903
Equipment and fixtures	4,938,751	4,939,409
	14,014,142	14,143,749
Accumulated depreciation and amortization	(7,001,949)	(6,945,541)
	$7,012,193	$ 7,198,208

Depreciation and amortization of premises and equipment was $675,409, $663,135, and $611,658, for 2008, 2007, and 2006, respectively. Amortization of software was $60,507, $61,616, and $108,364 for 2008, 2007, and 2006, respectively.

8. Deposits

Major classifications of interest-bearing deposits are as follows as of December 31:

	2008	*2007*
NOW and Super NOW	$ 27,887,068	$ 27,832,670
Money market	42,314,448	54,090,422
Savings	24,909,807	25,535,502
Certificates of deposit of $100,000 or more	47,284,402	36,865,359
Other time deposits	104,633,014	91,695,062
	$247,028,739	$236,019,015

Time deposits mature as follows:

	December 31,	
	2008	*2007*
Maturing within one year	$104,464,421	$109,844,363
Maturing over one to two years	39,495,278	12,620,414
Maturing over two to three years	5,281,316	4,313,494
Maturing over three to four years	1,595,778	801,961
Maturing over four to five years	1,080,623	980,189
	$151,917,416	$128,560,421

9. Borrowed Funds

Borrowed funds consist of securities sold under repurchase agreements, federal funds purchased, and borrowings from the FHLB. Securities sold under repurchase agreements are securities sold to the Bank’s customers under a continuing “roll-over” contract and mature in one business day. The underlying securities sold are federal agency securities that are segregated from the Company’s other investment securities. Federal funds purchased are unsecured, overnight borrowings from other financial institutions.

9. BORROWED FUNDS *(CONTINUED)*

Information with respect to borrowings is as follows at and for the years ended December 31:

Federal Home Loan Bank Borrowings

December 31,	*2008*	*2007*
Due 2008, 5.19% to 5.51%	$ —	$15,000,000
Due 2009, 0.48% to 2.33%	21,600,000	—
Due 2010, 0.59% to 3.57%	15,500,000	—
Due 2011, 3.00% to 4.04%	15,900,000	—
Due 2012, 3.18% to 3.52%	9,000,000	—
Due 2013, 3.26% to 4.33%	3,230,000	—
	$65,230,000	$15,000,000
Federal funds purchased and securities sold under repurchase agreements	$14,210,755	$14,589,152
Weighted average interest rate at year-end:		
Advances from the FHLB	2.30%	5.03%
Federal funds purchased and securities sold under repurchase agreements	0.003%	4.03%
Maximum outstanding at any month-end:		
Advances from the FHLB	$82,550,000	$30,000,000
Federal funds purchased and securities sold under repurchase agreements	$15,697,045	$19,427,144
Average balance outstanding during the year:		
Advances from the FHLB	$51,812,650	$19,753,973
Federal funds purchased and securities sold under repurchase agreements	$13,404,970	$11,914,984
Weighted average interest rate during the year:		
Advances from the FHLB	3.07%	5.58%
Federal funds purchased and securities sold under repurchase agreements	1.76%	4.67%

Debt retirement expense of $2.3 million was incurred in 2006 due to the restructuring of a $35.0 million FHLB advance that had a maturity date of February 2, 2010 and an interest rate of 6.84%.

The Company also has external sources of funds through the Federal Reserve Bank (“FRB”) and FHLB, which can be drawn upon when required. There is a line of credit totaling approximately $64 million with the Federal Home Loan Bank of Atlanta (the “FHLB”) based on qualifying loans pledged as collateral. Also the Company can pledge securities at the FRB and FHLB and borrow approximately 97% of the fair market value of the securities. In addition, the Company had $33.7 million of securities pledged at the FHLB under which the Company’s subsidiary, Carrollton Bank, could have borrowed approximately $32.7 million. Also, Carrollton Bank has $8.2 million of securities pledged at FRB under which it could have borrowed approximately $8.0 million. Approximately $2.6 million of securities have not been pledged against any borrowings. Outstanding borrowings at the FHLB were $65.2 million at December 31, 2008. Additionally, the Company has an unsecured federal funds line of credit of $5.0 million and a $10.0 secured federal funds line of credit with other institutions. The secured federal funds line of credit with the another institution would require Carrollton Bank to transfer securities pledged at the FHLB or FRB to this institution before Carrollton Bank could borrow against the line. There was no balance outstanding under these lines at December 31, 2008. These lines bear interest at the current federal funds rate of the correspondent bank.

10. Other Noninterest Expenses

Other noninterest expenses include the following for the years ended December 31:

	2008	*2007*	*2006*
Data processing services	$ 853,868	$ 847,231	$ 815,056
Loan expenses	438,591	290,286	195,844
Marketing	340,514	320,916	303,903
Directors' fees	307,850	352,550	238,850
Employee-related expenses	305,074	412,885	384,128
Loss on the sale of other real estate owned and related expenses	268,743	—	—
Liability insurance	158,687	172,041	205,516
Printing, stationary, and supplies	157,830	166,373	202,541
Software maintenance	144,120	110,455	51,306
Telephone	141,536	125,558	162,808
Carrier service	134,957	196,240	210,703
Deposit premium amortization	123,174	123,174	123,180
Postage and freight	118,684	141,918	164,606
FDIC Assessment	92,424	32,557	33,013
Contributions	88,348	30,358	59,324
ATM services	81,069	63,959	77,704
Shareholder expense	76,527	94,974	111,768
Software amortization	60,507	61,615	108,364
Coin/Currency service	9,626	17,637	103,480
Other	344,092	466,042	397,651
	$4,246,221	$4,026,769	$3,949,745

11. Stock Options

At the Company's annual shareholders meeting on May 15, 2007, the 2007 Equity Plan was approved. Under this plan, 500,000 shares of the Common Stock of the Company were reserved for issuance. Also, in accordance with the 2007 Equity Plan, 300 shares of unrestricted Common Stock were issued to each non-employee director in May 2008 and 2007. No new grants will be made under the 1998 Long Term Incentive Plan. However, incentive stock options issued under this plan will remain outstanding until exercised or until the tenth anniversary of the grant date of such options.

The 1998 Long Term Incentive Plan provided for the granting of common stock options to directors and key employees. In 2004, the shareholders approved increasing the number of shares available for grant under the Plan from 210,000 shares to 300,000 shares. These stock option awards contained a serial feature whereby one third of the options granted vest and can be exercised after each year. Option prices were equal to the estimated fair market value of the common stock at the date of the grant. Options expire ten years after the date of grant or upon employee termination if not exercised.

11. STOCK OPTIONS *(CONTINUED)*

Information with respect to options outstanding is as follows for the years ended December 31:

	2008		2007		2006	
	Shares	*Option Price Range*	*Shares*	*Option Price Range*	*Shares*	*Option Price Range*
Outstanding at beginning of year	184,555		229,030		227,130	
Granted	—		630	$17.25	12,430	$15.35 to $17.16
Exercised	(2,550)	$10.94 to $12.67	(40,685)	$ 9.71 to $18.10	(4,525)	$10.94 to $15.36
Expired/Canceled	(25,620)	$16.70 to $18.10	(4,420)	$14.50 to $17.79	(6,005)	$10.94 to $16.02
Outstanding at end of year	156,385	$9.71 to $18.03	184,555	$ 9.71 to $18.10	229,030	$ 9.71 to $18.10
Exercisable at December 31	151,848		173,732		209,670	
Aggregate intrinsic value at year end	$0.00		$108,640		$ 558,473	

On December 15, 2005, the Board of Directors authorized the grant of 42,000 options to officers and the immediate vesting of such options. All outstanding options to officers where the exercise price of the option exceeded the fair market value of the Company's stock were also approved for accelerated vesting. This resulted in 75,500 options becoming vested in 2005 that would have otherwise vested in future years.

As a result of adopting SFAS 123R on January 1, 2006, incremental stock-based compensation expense recognized was $7,315 and $17,841 during 2008 and 2007. As of December 31, 2008, there was $9,437 of unrecognized compensation expense related to nonvested stock options, which will be recognized over the remaining vesting period. The total intrinsic value of options excised during the year ended December 31, 2008 and 2007 was approximately $5,000 and $86,000, respectively.

A summary of information about stock options outstanding is as follows at December 31, 2008:

Weighted Average Exercise Price	*Shares*	*Weighted Average Remaining Life (Years)*	*Shares Underlying Options Currently Exercisable*
$ 9.71	1,890	2.33	1,890
10.94	17,850	2.42	17,850
12.11	3,150	3.33	3,150
12.14	630	3.16	630
12.67	16,350	3.58	16,350
13.45	13,125	1.58	13,125
13.45	1,890	1.33	1,890
14.45	5,880	6.29	5,880
14.50	3,780	4.33	3,780
14.50	29,000	6.96	29,000
14.85	5,000	6.43	5,000
15.36	1,670	0.33	1,670
15.42	23,730	0.35	23,730
16.02	14,000	5.58	14,000
16.22	5,460	5.33	5,460
16.31	6,720	7.29	4,480
17.16	5,000	8.00	3,333
17.25	630	8.08	210
18.03	630	7.60	420
14.23	156,385	3.77	151,848

11. STOCK OPTIONS *(CONTINUED)*

As of December 31, 2008, the weighted average exercise price of shares underlying options currently exercisable was $14.15 per share.

No options were granted in 2008. The value of each option is estimated on the date of grant using the Black-Scholes option pricing model with the following weighted average assumptions used for grants during the years ended December 31, 2007 and 2006:

	2007	*2006*
Dividend yield	3.30%	2.67%
Expected volatility	36.61%	24.76%
Risk free rate	4.04% to 4.87%	4.91% to 4.99%
Estimated life	6 years	10 years

The dividend yield is based on estimated future dividend yields. The risk-free rate for periods within the contractual term of the share option is based on the U.S. Treasury yield curve in effect at the time of the grant. Expected volatilities are generally based on historical volatilities.

12. NET INCOME PER SHARE

The calculation of net income per common share as restated giving retroactive effect to any stock dividends and splits is as follows for the years ended December 31:

	2008	*2007*	*2006*
Weighted average common shares outstanding	2,620,441	2,829,376	2,812,289
Stock option adjustment	—	10,861	58,953
Weighted average common shares outstanding-diluted	2,620,441	2,840,237	2,871,242
Net income (applicable to common stock)	$ 846,851	$2,126,263	$2,584,779
Basic net income per share	$ 0.32	$ 0.75	$ 0.92
Diluted net income per share	$ 0.32	$ 0.75	$ 0.90

13. COMPREHENSIVE INCOME

Comprehensive income is defined as net income plus transactions and other occurrences which are the result of nonowner changes in equity. For the Company, nonowner equity changes are comprised of unrealized gains or losses on available for sale securities, changes in the fair value of the derivative interest rate floor transaction and changes in the net actuarial gain/loss of the Company’s frozen Defined Benefit Pension Plan. These items, net of taxes, will be accumulated with net income in determining comprehensive income. Presented below is a reconcilement of net income to comprehensive income for the years ended December 31:

	2008	*2007*	*2006*
Net Income	$ 846,851	$ 2,126,263	$ 2,584,779
Other comprehensive income (loss):			
Net unrealized gain (loss) on securities available for sale	(5,385,284)	(197,640)	326,166
Net actuarial (loss)gain on defined benefit retirement plan	(2,013,985)	44,299	(52,862)
Accumulated gain (loss) on effective cash flow hedging derivative	471,257	177,156	(57,171)
Less: Adjustment for security gains realized in net income	(244,036)	—	(2,157,151)
Other comprehensive income (loss) before tax	(7,172,048)	23,815	(1,941,018)
Income taxes (benefit) on comprehensive income	(2,829,015)	9,395	749,685
Other comprehensive income (loss) after tax	(4,343,033)	14,420	(1,191,333)
Comprehensive income (loss)	$(3,496,182)	$ 2,140,683	$ 1,393,446

13. Comprehensive Income (Continued)

The components of accumulated other comprehensive income, net of tax, as of year-end were as follows:

	2008	2007
Net actuarial (loss) gain on defined benefit post-retirement benefit plans	$ (1,192,265)	$ 27,304
Net unrealized (loss) gain on securities available for sale	(2,848,471)	559,371
Accumulated gain on effective cash flow hedging derivatives	358,198	73,820
	$ (3,682,538)	$ 660,485

14. Capital Standards

The Company and the Bank are 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 action taken by regulators that, if undertaken, could have a direct 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 assets, liabilities, and certain off-balance sheet items as calculated under regulatory accounting procedures. The Bank's capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings and other factors.

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios (set forth in the table below) of total and Tier 1 capital (as defined) to risk-weighted assets (as defined), and of Tier 1 capital to average assets (as defined). Management believes, as of December 31, 2008, that the Bank meets all capital adequacy requirements to which it is subject. As of December 31, 2008, the most recent notification from the Federal Reserve Bank and the FDIC categorized the Company and the Bank as "well capitalized" under the regulatory framework for prompt corrective action. There are no conditions or events since that notification that management believes would change the Company's or the Bank's category.

	Actual		Minimum Capital Adequacy		To Be Well Capitalized	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
December 31, 2008						
Total Capital (to risk-weighted assets)						
Consolidated	$34,230,000	10.91%	$25,101,000	8.0%	$31,377,000	10.0%
Carrollton Bank	32,504,000	10.45%	24,893,000	8.0%	31,117,000	10.0%
Tier 1 Capital (to risk-weighted assets)						
Consolidated	30,888,000	9.84%	12,551,000	4.0%	18,826,000	6.0%
Carrollton Bank	29,280,000	9.41%	12,447,000	4.0%	18,670,000	6.0%
Tier 1 Capital (to average assets)						
Consolidated	30,888,000	8.17%	15,114,000	4.0%	18,893,000	5.0%
Carrollton Bank	29,280,000	7.37%	15,045,000	4.0%	18,806,000	5.0%
December 31, 2007						
Total Capital (to risk-weighted assets)						
Consolidated	$38,605,000	13.63%	$22,655,000	8.0%	$28,319,000	10.0%
Carrollton Bank	37,084,000	13.31%	22,284,000	8.0%	27,855,000	10.0%
Tier 1 Capital (to risk-weighted assets)						
Consolidated	34,963,000	12.35%	11,328,000	4.0%	16,992,000	6.0%
Carrollton Bank	33,987,000	12.20%	11,142,000	4.0%	16,713,000	6.0%
Tier 1 Capital (to average assets)						
Consolidated	34,963,000	10.03%	13,946,000	4.0%	17,432,000	5.0%
Carrollton Bank	33,987,000	9.72%	13,980,000	4.0%	17,475,000	5.0%

15. RETIREMENT PLANS

In the year ended December 31, 2006, the Company adopted SFAS No. 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans*, which requires the recognition of the funded status of defined benefit postretirement plans and related disclosures. While it does not impact net income, this resulted in a one-time adjustment to accumulated other comprehensive income in shareholders' equity of $484 (net of tax) for the Pension Plan.

Effective December 31, 2004, the Company froze the Defined Benefit Pension Plan. Participant benefits stopped accruing as of the date of the freeze. No new participants entered the Plan after December 31, 2004.

The following table sets forth the financial status of the Plan as of and for the years ended December 31:

	2008	*2007*	*2006*
CHANGE IN BENEFIT OBLIGATION:			
Benefit obligation at beginning of year	$ 8,504,945	$ 8,290,339	$7,944,785
Service cost	—	—	—
Interest cost	484,362	472,592	469,361
Actuarial (gain) loss	(532,116)	107,258	230,830
Benefits paid	(403,716)	(365,244)	(354,637)
Benefit obligation at end of year	8,053,475	8,504,945	8,290,339
CHANGE IN PLAN ASSETS:			
Fair value of plan assets at beginning of year	8,550,034	8,291,129	7,952,987
Actual return on plan assets	(1,991,902)	687,533	767,957
Employer contribution	—	—	—
Benefits paid and administrative expenses	(473,553)	(428,628)	(429,815)
Fair value of plan assets at end of year	6,084,579	8,550,034	8,291,129
Funded status	$ (1,968,896)	$ 45,089	$ 790
Amounts Recognized in the Consolidated Balance Sheets:			
Prepaid benefit cost	$ —	$ 45,089	$ 790
Other liabilities	(1,968,896)	—	—
Net amount recognized	$ (1,968,896)	$ 45,089	$790
Amounts recognized in accumulated other comprehensive income consist of:			
Net loss (gain)	$ 2,233,588	$ (44,299)	$ 790
Prior service cost (credit)	—	—	—
Net amount recognized (before tax effect)	$ 2,233,588	$ (44,299)	$ 790

15. RETIREMENT PLANS (*CONTINUED*)

	2008	*2007*	*2006*
ASSUMPTIONS USED IN MEASURING THE PROJECTED BENEFIT OBLIGATION WERE AS FOLLOWS FOR THE YEARS ENDED DECEMBER 31:			
Discount rates	6.00%	5.82%	5.82%
Rates of increase in compensation levels	N/A	N/A	N/A
Long-term rate of return on assets	5.85%	5.85%	8.00%
NET PERIODIC PENSION EXPENSE INCLUDES THE FOLLOWING COMPONENTS:			
Service cost	$ —	$ —	$ —
Interest cost	484,362	472,592	469,361
Expected return on plan assets	(489,497)	(475,074)	(622,784)
Net periodic pension (benefit)	$ (5,135)	$ (2,482)	$ (153,423)
ACCUMULATED BENEFIT OBLIGATION AT YEAR END	$8,053,475	$8,504,945	$8,290,339
ALLOCATION OF ASSETS			
Equity securities	49%	59%	52%
Fixed income-guaranteed fund	51%	41%	48%
	100%	100%	100%

There are no net transaction obligation (asset), prior service cost (credit) and estimated net loss (gain) for the Plan that are expected to be amortized from accumulated other comprehensive income into net periodic benefit cost over the next fiscal year.

Benefits expected to be paid from the Plan are as follows:

Year	*Amount*
2009	$ 376,000
2010	383,000
2011	399,000
2012	489,000
2013	487,000
2014-2018	2,509,000

The Plan's investment strategy is predicated on its investment objectives and the risk and return expectations of asset classes appropriate for the Plan. Investment objectives have been established by considering the Plan's liquidity needs and time horizon and the fiduciary standards under ERISA. The asset allocation strategy is developed to meet the Plan's long term needs in a manner designed to control volatility and to reflect the Company's risk tolerance.

In determining the long-term rate of return on pension plan assets assumption, the target asset allocation is first reviewed. An expected long-term rate of return is assumed for each asset class, and an underlying inflation rate assumption is also made. The effects of asset diversification and periodic fund rebalancing are also considered.

The Company has a contributory thrift plan qualifying under Section 401(K) of the Internal Revenue Code. Employees with one year of service are eligible for participation in the Plan. In conjunction with the curtailment of the pension plan, the Company expanded the thrift plan to make it a Safe Harbor Plan. Once an employee has been at the Company for one year, the Company then contributes 3% of the employee's salary to the Plan for the employee's benefit. The Company also matches 50% of the employee 401(K) contribution up to 6% of employee compensation. Contributions to this Plan, included in employee benefit expenses, were $336,882, $319,236 and $319,453, for 2008, 2007, and 2006, respectively.

16. CONTINGENCIES

The Company is involved in various legal actions arising from normal business activities. Management believes that the ultimate liability or risk of loss resulting from these actions will not materially affect the Company's financial position or results of operations.

17. INCOME TAXES

On January 1, 2007, the Company adopted the Financial Accounting Standards Board ("FASB") Final Interpretation Number 48, *Accounting for Uncertainty in Income Taxes*. The Company has no adjustments to report with respect to the effect of adoption of FIN 48.

The components of income tax expense are as follows for the years ended December 31:

	2008	*2007*	*2006*
CURRENT			
Federal	$ (28,953)	$ 999,915	$1,082,628
State	(15,120)	162,767	180,009
	(44,073)	1,162,682	1,262,637
DEFERRED	168,270	(111,908)	60,631
	$ 124,197	$1,050,774	$1,323,268

The components of the deferred tax benefits were as follows for the years ended December 31:

	2008	*2007*	*2006*
Provision for loan losses	$ 39,136	$ (75,795)	$ 79,612
Deferred loan origination costs	(3,433)	(1,626)	(20,427)
Deferred compensation plan	(5,981)	(20,330)	16,466
Depreciation	142,665	(21,286)	522
Discount accretion	(4,114)	7,086	5,178
Retirement benefits	—	—	(20,720)
FHLB stock dividends	(43)	43	—
	$ 168,270	$(111,908)	$ 60,631

The components of the net deferred tax liability were as follows for the years ended December 31:

	2008	*2007*	*2006*
DEFERRED TAX ASSETS			
Allowance for loan losses	$1,010,685	$1,049,861	$ 974,066
Deferred compensation plan	216,737	210,756	190,426
Unrealized losses on available for sale investment securities	1,622,142	—	—
Prepaid retirement benefits	776,631	—	—
Depreciation	—	48,286	27,000
	3,626,195	1,308,903	1,191,492
DEFERRED TAX LIABILITIES			
Deferred loan origination costs	101,586	105,019	106,645
Unrealized gains on available for sale investment securities	—	398,401	317,406
Discount accretion	11,316	15,430	8,344
FHLB Stock dividends	2,019	2,062	2,019
Depreciation	94,379	—	—
	209,300	520,912	434,414
NET DEFERRED TAX ASSET	$3,416,895	$ 787,991	$ 757,078

17. INCOME TAXES (CONTINUED)

The differences between the federal income tax rate of 34 percent and the effective tax rate for the Company are reconciled as follows:

	2008	*2007*	*2006*
Statutory federal income tax rate	34.0%	34.0%	34.0%
Increase (Decrease) resulting from:			
Tax-exempt income	(26.8)	(4.4)	(4.5)
State income taxes, net of federal income tax benefit	3.8	3.8	3.8
Nondeductible expense	1.8	.5	0.6
Change in state rates	—	(.8)	—
	12.8%	33.1%	33.9%

18. LEASE COMMITMENTS

The Company leases various branch and general office facilities to conduct its operations. The leases have remaining terms which range from a period of 1 year to 20 years. Most leases contain renewal options which are generally exercisable at increased rates. Some of the leases provide for increases in the rental rates at specified times during the lease terms, prior to the expiration dates.

The leases generally provide for payment of property taxes, insurance, and maintenance costs by the Company. The total rental expense for all real property leases amounted to $1,249,543, $1,129,007, and $937,160, for 2008, 2007, and 2006, respectively.

Lease obligations will require minimum rental payments as follows:

Period	*Minimum rentals*
2009	$ 1,178,613
2010	1,186,567
2011	967,366
2012	900,531
2013	934,755
Remaining years	8,261,802
	$13,429,634

19. Parent Company Financial Information

The balance sheets as of December 31, 2008 and 2007 and statements of income and cash flows for Carrollton Bancorp (Parent Only) for 2008, 2007 and 2006, are presented below:

Balance Sheets

	December 31, 2008	December 31, 2007
Assets		
Cash	$ 1,000	$ 1,000
Interest-bearing deposits in subsidiary	29,433	46,475
Investment in subsidiary	25,565,823	34,276,436
Investment securities available for sale	1,967,720	1,966,123
Other assets	24,209	11,557
	$27,588,185	$36,301,591
Liabilities and Shareholders' Equity		
Liabilities	$ 197,492	$ 370,291
Shareholders' Equity		
Common Stock	2,564,988	2,834,975
Additional Paid-in Capital	15,255,971	18,781,650
Retained earnings	13,252,272	13,654,180
Accumulated other comprehensive income	(3,682,538)	660,495
	27,390,693	35,931,300
	$27,588,185	$36,301,591

Statements of Income

	Years ended December 31, 2008	2007	2006
Income			
Dividends from subsidiary	$5,623,906	$ 776,520	$ 258,840
Interest and dividends	80,368	59,721	73,720
Security gains (losses)	(103,474)	—	2,157,151
	5,600,800	836,241	2,489,711
Expenses	197,630	314,256	161,751
Income before income taxes and equity in undistributed net income of subsidiary	5,403,170	521,985	2,327,960
Income tax expense (benefit)	(107,597)	(112,265)	785,790
	5,510,767	634,250	1,542,170
Equity in undistributed net income (loss) of subsidiary	(4,663,916)	1,492,013	1,042,609
Net Income	$ 846,851	$2,126,263	$2,584,779

19. PARENT COMPANY FINANCIAL INFORMATION (CONTINUED)

STATEMENTS OF CASH FLOWS

	Years ended December 31,		
	2008	*2007*	*2006*
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net income	$ 846,851	$ 2,126,263	$ 2,584,779
ADJUSTMENTS TO RECONCILE NET INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES:			
Equity in undistributed net (income) loss of subsidiary	4,663,916	(1,492,013)	(1,042,609)
Gains on disposal of securities	(808)	—	(2,157,151)
Write down of equity securities	104,282	—	—
Stock based compensation expense	7,315	17,841	13,447
Stock issued under 2007 Equity Plan	50,400	58,500	—
Decrease (increase) in other assets	(12,652)	16,715	(2,457)
Increase (decrease) in other liabilities	(3,092)	(645,540)	13,126
Net cash provided by (used in) operating activities	5,656,212	81,766	(590,865)
CASH FLOWS FROM INVESTING ACTIVITIES:			
Purchase of securities available for sale	(574,160)	—	(117,269)
Proceeds from sales of securities available for sale	3,046	—	2,766,852
Net cash (used in) provided by investing activities	(571,114)	—	2,649,583
CASH FLOWS FROM FINANCING ACTIVITIES:			
Dividends paid	(1,248,759)	(1,358,330)	(1,266,063)
Common stock repurchase and retirement	(3,883,870)	(264,271)	(128,850)
Stock options exercised	28,656	592,709	52,219
Income tax benefit from exercise of stock options	1,833	32,790	7,014
Net cash used in financing activities	(5,102,140)	(997,102)	(1,335,680)
Net increase (decrease) in cash	(17,042)	(915,336)	723,038
Cash and cash equivalents at beginning of year	47,475	962,811	239,773
Cash and cash equivalents at end of year	$ 30,433	$ 47,475	$ 962,811
Noncash Activities:			
Income taxes paid, net of cash received from subsidiaries	$ 69,344	$ 546,578	$ 769,473

20. Fair Value and Financial Instruments

SFAS 157 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. A fair value measurement assumes that the transaction to sell the asset or transfer the liability occurs in the principal market for the asset or liability or, in the absence of a principal market, the most advantageous market for the asset or liability. The price in the principal (or most advantageous) market used to measure the fair value of the asset or liability shall not be adjusted for transaction costs. An orderly transaction is a transaction that assumes exposure to the market for a period prior to the measurement date to allow for marketing activities that are usual and customary for transactions involving such assets and liabilities; it is not a forced transaction. Market participants are buyers and sellers in the principal market that are (i) independent, (ii) knowledgeable, (iii) able to transact and (iv) willing to transact.

SFAS 157 requires the use of valuation techniques that are consistent with the market approach, the income approach and/or the cost approach. The market approach uses prices and other relevant information generated by market transactions involving identical or comparable assets and liabilities. The income approach uses valuation techniques to convert future amounts, such as cash flows or earnings, to a single present amount on a discounted basis. The cost approach is based on the amount that currently would be required to replace the service capacity of an asset (replacement cost). Valuation techniques should be consistently applied. Inputs to valuation techniques refer to the assumptions that market participants would use in pricing the asset or liability. Inputs may be observable, meaning those that reflect the assumptions market participants would use in pricing the asset or liability developed based on market data obtained from independent sources, or unobservable, meaning those that reflect the reporting entity's own assumptions about the assumptions market participants would use in pricing the asset or liability developed based on the best information available in the circumstances. In that regard, SFAS 157 establishes a fair value hierarchy for valuation inputs that gives the highest priority to quoted prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs. The fair value hierarchy is as follows:

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

Level 2: Significant other observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities, quoted prices in markets that are not active, and other inputs that are observable or can be corroborated by observable market data.

Level 3: Significant unobservable inputs that reflect a company's own assumptions about the assumptions that market participants would use in pricing an asset or liability.

The Company uses the following methods and significant assumptions to estimate fair value for financial assets and financial liabilities:

Securities available for sale: The fair value of securities available for sale are determined by obtaining quoted prices on nationally recognized securities exchanges. If quoted market prices are not available, fair value is determined using quoted market prices for similar securities. Equity securities are reported at fair value using Level 1 inputs.

Derivatives: Derivatives are reported at fair value utilizing Level 2 inputs. The Company obtains dealer quotations to value its interest rate floor. For purposes of potential valuation adjustments to its derivative position, the Company evaluates the credit risk of its counterparty. Accordingly, the Company has considered factors such as the likelihood of default by the counterparty and the remaining contractual life, among other things, in determining if any fair value adjustment related to credit risk is required.

Loans held for sale: The fair value of loans held for sale is determined, when possible, using quoted secondary-market prices. If no such quoted pricing exists, the fair value of a loan is determined using quoted prices for a similar asset or assets, adjusted for the specific attributes of that loan.

Impaired loans and other real estate owned: Nonrecurring fair value adjustments to loans and other real estate owned ("OREO") reflect full or partial write-downs that are based on the loans or OREO's observable market price or current appraised value of the collateral in accordance with SFAS 114, Accounting by Creditors for Impairment of a Loan. Since the market for impaired loans and OREO is not active, loans or OREO subjected to nonrecurring fair value adjustments based on the current appraised value of the collateral may be classified as Level 2 or Level 3 depending on the type of asset and the inputs to the valuation. When appraisals are used to determine impairment and these appraisals are based on a market approach incorporating a dollar-per-square-foot multiple, the related loans or OREO are classified as Level 2. If the appraisals require significant adjustments to market-based valuation inputs or apply an income approach based on unobservable cash flows to measure fair value, the related loans or OREO subjected to nonrecurring fair value adjustments are typically classified as Level 3 due to the fact that Level 3 inputs are significant to the fair value measurement.

20. FAIR VALUE AND FINANCIAL INSTRUMENTS (CONTINUED)

	Fair Value Measurements at December 31, 2008 using:			
	Total	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Available for sale securities	$ 56,393,865	$ 2,065,486	$ 50,194,738	$ 4,133,641
Derivative asset	649,792	—	649,792	—

Approximately $104,000 write down of equity securities was recognized as a reduction of gain on sales.

Certain other assets are measured at fair value on a nonrecurring basis. These adjustments to fair value usually result from application of lower of cost or fair value accounting or write-downs of individual assets due to impairment. For assets measured at fair value on a nonrecurring basis during 2008 that were still held in the balance sheet at year end, the following table provides the level of valuation assumptions used to determine each adjustment and the carrying value of the related individual assets at year end.

	Carrying value at December 31, 2008:			
	Total	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Loans held for sale	$21,701,287	$ —	$21,701,287	$ —
Impaired loans	1,553,548	—	1,553,548	—
Other real estate owned (OREO)	1,736,018	—	1,736,018	—

During 2008, the Company recognized losses related to certain assets that are measured at fair value on a nonrecurring basis (i.e. loans and loans held for sale). Approximately $2.3 million of losses related to loans were recognized as chargeoffs for loan losses and $167,000 write downs of OREO properties were recognized as other operating expenses. During 2008, there were no losses related to loans held for sale accounted for at the lower of cost or fair value.

The following methods and assumptions were used to estimate the fair value of each class of financial instrument.

Cash and cash equivalents

The carrying amount of cash and due from banks is a reasonable estimate of fair value.

Federal funds sold and Federal Home Loan Bank deposit

The carrying amount of federal funds sold and Federal Home Loan Bank deposit is a reasonable estimate of fair value.

Investment Securities

The fair values of securities held to maturity and securities available for sale are based upon quoted market prices or dealer quotes. Level 3 of the fair value hierarchy was used to determine fair value of Trust Preferred securities because the market for these securities at December 31, 2008 was not active.

Loans held for sale

The fair value of residential mortgage loans originated for sale is estimated by discounting future cash flows using current rates for which similar loans would be made to borrowers with similar credit histories.

Loans, net

The fair value of loans receivable is estimated by discounting future cash flows using current rates for which similar loans would be made to borrowers with similar credit histories.

Deposit liabilities

The fair value of demand deposits and savings accounts is the amount payable on demand. The fair value of fixed maturity certificates of deposit is estimated using the rates currently offered for deposits of similar remaining maturities. The estimated fair value of deposits does not take into account the value of the Company's long-term relationships with depositors, commonly known as core deposit intangibles, which are separate intangible assets, and not considered financial instruments. Nonetheless, the Company would likely realize a core deposit premium if its deposit portfolio were sold in the principal market for such deposits.

Federal funds purchased and securities sold under agreements to repurchase

The carrying amount of federal funds purchased and securities sold under agreements to repurchase is a reasonable estimate of fair value.

Advances from the FHLB

The fair value of long-term FHLB advances is estimated by discounting the value of contractual cash flows using rates currently offered for advances with similar terms and remaining maturities.

Commitments to extend credit, standby letters of credit and financial guarantees written

The Company charges fees for commitments to extend credit. Interest rates on loans for which these commitments are extended are normally committed for periods of less than one month. Fees charged on standby letters of credit and other financial guarantees are deemed to be immaterial and these guarantees are expected to be settled at face amount or expire unused. It is impractical to assign any fair value to these commitments.

	December 31, 2008		December 31, 2007	
	Carrying amount	*Fair value*	*Carrying amount*	*Fair value*
FINANCIAL ASSETS				
Cash and cash equivalents	$ 10,162,288	$ 10,162,288	$ 16,926,981	$ 16,926,981
Investment securities (total)	66,768,153	66,525,722	52,792,208	52,786,529
Federal Home Loan Bank stock	3,575,700	3,575,700	1,305,100	1,305,100
Loans held for sale	21,701,287	22,363,923	7,579,765	7,761,521
Loans, net	280,513,415	289,078,738	258,353,408	264,548,464
FINANCIAL LIABILITIES				
Noninterest-bearing deposits	45,324,537	45,324,537	49,619,610	49,619,610
Interest-bearing deposits	247,028,739	250,644,373	236,019,015	237,021,786
Federal funds purchased and securities sold under agreements to repurchase	14,210,755	14,210,755	14,589,152	14,589,152
Advances from the Federal Home Loan Bank	65,230,000	66,088,063	15,000,000	15,009,000

21. CONSOLIDATED QUARTERLY RESULTS OF OPERATIONS (UNAUDITED)

	Year Ended December 31, 2008			
	First Quarter	*Second Quarter*	*Third Quarter*	*Fourth Quarter*
Interest income	$5,559,959	$5,474,229	$5,684,721	$5,687,691
Interest expense	2,157,184	1,930,005	2,167,677	2,202,316
Net interest income	3,402,775	3,544,224	3,517,044	3,485,375
Provision for loan losses	99,000	99,000	799,000	1,099,000
Other noninterest income	1,660,186	1,645,704	1,642,103	1,637,701
Noninterest expenses	4,417,019	4,163,855	4,364,975	4,522,215
Income (loss) before income taxes	546,942	927,073	(4,828)	(498,139)
Income taxes (benefit)	117,993	300,155	(55,557)	(238,394)
Net income (loss)	$ 428,949	$ 626,918	$ 50,729	$ (259,745)
Net income (loss) per share — basic	$ 0.16	$ 0.24	$ 0.02	$ (0.10)
Cash dividends per share	$ 0.12	$ 0.12	$ 0.12	$ 0.12
Market prices: high	$ 15.08	$ 14.99	$ 14.00	$ 9.34
low	$ 12.00	$ 11.75	$ 8.00	$ 5.50

	Year Ended December 31, 2007			
	First Quarter	*Second Quarter*	*Third Quarter*	*Fourth Quarter*
Interest income	$5,837,298	$6,028,065	$6,020,330	$5,790,667
Interest expense	2,408,583	2,465,421	2,472,873	2,415,447
Net interest income	3,428,715	3,562,644	3,547,457	3,375,220
Gains on security sales	66,000	99,000	99,000	272,000
Other noninterest income	1,598,570	1,616,030	1,563,046	1,496,496
Noninterest expenses	4,089,425	4,384,615	3,864,045	4,137,056
Income before income taxes	871,860	695,059	1,147,458	462,660
Income taxes	270,968	242,418	334,436	202,952
Net income	$ 600,892	$ 452,641	$ 813,022	$ 259,708
Net income per share — basic	$ 0.21	$ 0.16	$ 0.29	$ 0.09
Cash dividends per share	$ 0.12	$ 0.12	$ 0.12	$ 0.12
Market prices: high	$ 18.00	$ 18.40	$ 16.73	$ 14.85
low	$ 16.40	$ 15.55	$ 12.00	$ 11.25

Year Ended December 31, 2006				
	First Quarter	*Second Quarter*	*Third Quarter*	*Fourth Quarter*
Interest income	$5,566,706	$5,652,219	$5,855,415	$6,053,164
Interest expense	2,082,985	2,052,221	2,237,219	2,365,025
Net interest income	3,483,721	3,599,998	3,618,196	3,688,139
Gains on security sales	2,157,176	—	—	—
Other noninterest income	1,783,075	1,986,531	1,555,033	1,417,182
Noninterest expenses	6,088,968	5,558,716	3,859,040	3,874,280
Income before income taxes	1,335,004	27,813	1,314,189	1,231,041
Income taxes	467,146	(30,557)	459,078	427,601
Net income	$ 867,858	$ 58,370	$ 855,111	$ 803,440
Net income per share — basic	$ 0.31	$ 0.02	$ 0.30	$ 0.29
Cash dividends per share	$ 0.11	$ 0.11	$ 0.11	$ 0.12
Market prices: high	$ 15.95	$ 18.80	$ 18.00	$ 19.45
low	$ 14.40	$ 15.64	$ 16.11	$ 16.99

22. Subsequent Event

On February 13, 2009, as part of the TARP Capital Purchase Program, the Company entered into a Letter Agreement, and the related Securities Purchase Agreement - Standard Terms (collectively, the “Purchase Agreement”), with the United States Department of the Treasury (“Treasury”), pursuant to which the Company issued (i) 9,201 shares of Fixed Rate Cumulative Perpetual Preferred Stock, Series A, liquidation preference $1,000 per share (“Series A Preferred Stock”), and (ii) a warrant to purchase 205,379 shares of the Company’s common stock, par value $1.00 per share.

The Company raised $9,201,000 through the sale of the Series A Preferred Stock which will qualify as Tier 1 capital. With the full amount of the Treasury’s investment, on a pro-forma basis, at December 31, 2008, the Company’s Tier I capital ratio would increase to approximately 12.78% and total risk-based capital ratio would increase to approximately 13.84%. The Series A Preferred Stock will pay cumulative dividends at a rate of 5% per annum until February 15, 2014. Beginning February 16, 2014, the dividend rate will increase to 9% per annum. Dividends are payable quarterly.

On and after February 15, 2012, the Company may, at its option, redeem shares of Series A Preferred Stock, in whole or in part, at any time and from time to time, for cash at a per share amount equal to the sum of the liquidation preference per share plus any accrued and unpaid dividends to but excluding the redemption date. Prior to February 15, 2012, the Company may redeem shares of Series A Preferred Stock only if it has received aggregate gross proceeds of not less than $ 9,201,000 from one or more qualified equity offerings, and the aggregate redemption price may not exceed the net proceeds received by the Company from such offerings. The redemption of the Series A Preferred Stock requires prior regulatory approval.

The warrant is exercisable in whole or in part at $6.72 per share at any time on or before February 13, 2019. Treasury has agreed not to exercise voting power with respect to any shares of common stock issued upon exercise of the warrant.

The Series A Preferred Stock and the warrant were issued in a transaction exempt from registration pursuant to Section 4(2) of the Securities Act of 1933, as amended. The Company has agreed to register the Series A Preferred Stock, the warrant, and the shares of common stock underlying the warrant (the “warrant shares”) as soon as practicable after the date of the issuance of the Series A Preferred Stock and the warrant. Neither the Series A Preferred Stock nor the warrant will be subject to any contractual restrictions on transfer, except that Treasury may not transfer a portion of the warrant with respect to, or exercise the warrant for, more than one-half of the warrant shares prior to the earlier of (a) the date on which the Company has received aggregate gross proceeds of not less than $9,201,000 from one or more qualified equity offerings and (b) December 31, 2009.

The Purchase Agreement also subjects the Company to certain of the executive compensation limitations included in the Emergency Economic Stabilization Act of 2008 (the “EESA”). As a condition to the closing of the transaction, Robert A. Altieri, James M. Uveges, Gary M. Jewell, William D. Sherman, and Lola B. Stokes (the Company’s Senior Executive Officers, as defined in the Purchase Agreement) each: (i) voluntarily waived any claim against the Treasury or the Company for any changes to such Senior Executive Officer’s compensation or benefits that are required to comply with the regulation issued by the Treasury under the TARP Capital Purchase Program as published in the Federal Register on October 20, 2008 and acknowledging that the regulation may require modification of the compensation, bonus, incentive and other benefit plans, arrangements and policies and agreements (including so-called “golden parachute” agreements) as they relate to the period the Treasury holds any equity or debt securities of the Company acquired through the TARP Capital Purchase Program; and

(ii) entered into an amendment to Messer's Altieri, Uveges, Jewell and Mrs. Stokes employment agreements that provide that any severance payments made to such officers will be reduced, as necessary, so as to comply with the requirements of the TARP Capital Purchase Program.

The Treasury's current consent shall be required for any increase in the common dividends per share until February 13, 2012 unless prior to such date, the Series A preferred stock is redeemed in whole or the Treasury has transferred all of the Series A Preferred Stock to third parties.

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

There have been no changes in or disagreements with accountants, on accounting and financial disclosure during 2008.

ITEM 9A(T): CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures. We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the Securities and Exchange Commission, and that such information is accumulated and communicated to our management, including the Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. Management necessarily applied its judgment in assessing the costs and benefits of such controls and procedures which, by their nature, can provide only reasonable assurance regarding management's control objective.

We carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures pursuant to Exchange Act Rule 13a-15, as of the end of the fiscal period covered by this report on Form 10-K. Based upon that evaluation, each of our Chief Executive Officer and our Chief Financial Officer concluded that our disclosure controls and procedures are effective in timely alerting them to material information relating to us required to be disclosed in our Exchange Act reports.

Management's Report on Internal Control over Financial Reporting. Management is responsible for establishing and maintaining adequate internal control over financial reporting as such term is defined in Exchange Act Rules 13a-15(f). The Company's internal controls over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. Because of its inherent limitations, internal controls over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may be inadequate because of changes in conditions, or the degree of compliance with the policies or procedures may deteriorate.

Under the supervision and with the participation of the Company's Chief Executive Officer and Chief Financial Officer, management conducted an evaluation of the effectiveness of the Company's internal control over financial reporting as of December 31, 2008 based on the framework in Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this evaluation, management concluded that the Company's internal control over financial reporting was effective as of December 31, 2008 under this framework.

This annual report does not include an attestation report of the Company's registered public accounting firm regarding internal control over financial reporting. Management's report was not subject to attestation by the Company's registered public accounting firm pursuant to temporary rules of the Securities and Exchange Commission that permit the Company to provide only management's report in this annual report.

Changes in Internal Control over Financial Reporting. In connection with our evaluation, no change was identified in our internal controls over financial reporting that occurred during the fourth quarter of 2008 that has materially affected, or is reasonably likely to materially affect, our internal controls over financial reporting.

ITEM 9B: OTHER INFORMATION

None.

PART III

ITEM 10: DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

The information required by this Item is incorporated by reference to the information appearing under the captions “Election of Directors,” “Executive Officers” and “Section 16(a) Beneficial Ownership Reporting Compliance” in the Company’s definitive Proxy Statement for the Annual Meeting of Shareholders to be held on May 12, 2009.

ITEM 11: EXECUTIVE COMPENSATION

The information required by this Item is incorporated by reference to the information appearing under the captions “Executive Compensation,” “Outstanding Equity Awards at 2008 Fiscal Year End,” “Grants of Plan-Based Awards,” “Option Exercises and Stocks Vested” and “Pension Benefits and Perquisites” in the Company’s definitive Proxy Statement for the Annual Meeting of Shareholders to be held on May 12, 2009.

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

The information required by this Item is incorporated by reference to the information appearing under the caption “Security Ownership of Directors and Executive Officers” and “Certain Beneficial Owners” in the Company’s definitive Proxy Statement for the Annual Meeting of Shareholders to be held on May 12, 2009.

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

The information required by this Item is hereby incorporated by reference to the information appearing under the caption “Certain Transactions and Relationships” in the Company’s definitive Proxy Statement for the Annual Meeting of Shareholders to be held on May 12, 2009.

ITEM 14: PRINCIPAL ACCOUNTING FEES AND SERVICES

The information required by this Item is hereby incorporated by reference to the information appearing under the caption “Audit Fees and Services” in the Company’s definitive Proxy Statement for the Annual Meeting of Shareholders to be held on May 12, 2009.

PART IV

ITEM 15: EXHIBITS, FINANCIAL STATEMENT SCHEDULES

1. Financial Statements
   - Carrollton Bancorp and Subsidiaries:
     - Report of Independent Registered Public Accounting Firm
     - Consolidated Balance Sheets as of December 31, 2008, and 2007
     - Consolidated Statements of Income for the years ended December 31, 2008, 2007, and 2006
     - Consolidated Statements of Changes in Shareholders’ Equity for the years ended December 31, 2008, 2007, and 2006
     - Consolidated Statements of Cash Flows for the years ended December 31, 2008, 2007, and 2006
     - Notes to Consolidated Financial Statements
2. Financial Statement Schedules
   - None
3. Exhibits

Exhibit Number	*Description*
3.1(i)	Articles of Incorporation of Carrollton Bancorp
3.1(ii)	Articles of Amendment of Carrollton Bancorp
3.1(iii)	Articles Supplementary of Carrollton Bancorp
3.2(i)	By-Laws of Carrollton Bancorp
3.2(ii)	Amendment No. 1 to Bylaws of Carrollton Bancorp
4.1	Form of Stock Certificate for Fixed Rate Cumulative Perpetual Preferred Stock, Series A(1)
4.2	Warrant to Purchase 205,379 Shares of Common Stock of Carrollton Bancorp(1)

10.1	Lease dated January 24, 1989, by and between Hill Management Services, Inc. and The Carrollton Bank of Baltimore.(2)
10.2	Lease dated July 21, 1989, by and between Hill Management Services, Inc. and The Carrollton Bank of Baltimore.(2)
10.7	Lease dated July 19, 1988, by and between Northway Limited Partnership and The Carrollton Bank of Baltimore.(2)
10.8	Lease dated August 11, 1994, by and between KIMCO and Carrollton Bank.(3)
10.9	Lease dated October 11, 1994, by and between Ridgeview Associates Limited Partnership and Carrollton Bank.(3)
10.12	Lease dated January 15, 2004, by and between Turf Village Offices and Carrollton Bank (2300 York Road, Suite 114, 115, 116)
10.14	Lease dated February 15, 2005, by and between Turf Village Offices and Carrollton Bank (2300 York Road, Suites 213, 214, 215, 216)
10.15	Lease dated February 18, 2005, by and between Broadway 205 Associates, LLP and Carrollton Mortgage Services, Inc.
10.16	Lease dated October 26, 2005, by and between Arthur Lea Stabler and Helen H. Stabler and Carrollton Bank
10.17	Lease dated June 11, 2004, by and between Mario J. Orlando and Matthew J. Salafia and Carrollton Mortgage Services, Inc.
10.18	Lease dated November 4, 2003, by and between Hickory Crossing, LLC and Carrollton Bank
10.20	Lease dated January 13, 2006, by and between Scotts Corner LLLP and Carrollton Bank
10.21	Lease dated April 27, 2006, by and between Arbutus Shopping Center Limited Partnership and Carrollton Bank
10.22	Employment agreement with Gary M. Jewell(4)
10.23	Lease dated August 13, 2007, by and between Tarragon, Inc. and Carrollton Bank
10.24	Employment agreement with Robert A. Altieri(5)
10.25	Employment agreement with Lola B. Stokes(6)
10.26	Employment agreement with James M. Uveges(7)
10.27	Lease dated September 8, 2008 by and between Gateway 38 LLC and Carrollton Bancorp (8)
10.28	Letter Agreement and related Securities Purchase Agreement - Standard Terms, dated February 13, 2009 between Carrollton Bancorp and United States Department of the Treasury(1)
10.29	Form Waiver executed by each of Robert A. Altieri, James M. Uveges, Gary M. Jewell, William D. Sherman and Lola B. Stokes(1)
21.1	Subsidiaries of Carrollton Bancorp
23.1	Consent of Independent Registered Public Accounting Firm by Exchange Act Rule 13-a-14(a)
31.1	Certification by the Principal Executive Officer required by Exchange Act Rule 13-a-14(a)
31.2	Certification by Principal Financial Officer required by Exchange Act Rule 13-a-14(a)
32.1	Certification by the Principal Executive Officer
32.2	Certification by the Principal Financial Officer

(1) Incorporated by reference to the Registrant’s Form 8-K filed 2/17/2009 (File No.: 000-23090).
(2) Incorporated by reference from Registration Statement dated January 12, 1990, on SEC Form S-4 (1933 Act File No.: 33-33027).
(3) Incorporated by reference from Annual Report on Form 10-KSB for the fiscal year ended December 31, 1994, (1934 Act File No.: 0-23090).
(4) Incorporated by reference to the Registrant’s Form 8-K filed 6/19/2007 (File No.: 000-23090).
(5) Incorporated by reference to the Registrant’s Form 8-K filed 9/25/2007 (File No.: 000-23090).
(6) Incorporated by reference to the Registrant’s Form 8-K filed 10/24/2007 (File No.: 000-23090).
(7) Incorporated by reference to the Registrant’s Form 8-K filed 11/8/2007 (File No.: 000-23090).
(8) Incorporated by reference to the Registrant’s Form 8-K filed 9/30/2008 (File No.: 000-23090)

SIGNATURES

Pursuant to the requirement of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

CARROLLTON BANCORP
(Registrant)

March 3, 2009

By: /s/ Robert A. Altieri
Robert A. Altieri
President and Chief Executive Officer

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

March 3, 2009

By: /s/ Robert A. Altieri
Robert A. Altieri
President and Chief Executive Officer

PRINCIPAL FINANCIAL AND ACCOUNTING OFFICER

March 3, 2009

By: /s/ James M. Uveges
James M. Uveges
(Principal financial and accounting officer)
Senior Vice President and Chief Financial Officer

Board of Directors

March 3, 2009

By: /s/ Robert J. Aumiller
Robert J. Aumiller
Director

March 3, 2009

By: /s/ Steven K. Breeden
Steven K. Breeden
Director

March 3, 2009

By: /s/ Albert R. Counselman
Albert R. Counselman
Chairman of the Board

March 3, 2009

By: /s/ Harold I. Hackerman
Harold I. Hackerman
Director

March 3, 2009

By: /s/ William L. Hermann
William L. Hermann
Director

March 3, 2009	By: /s/ David P. Hessler David P. Hessler Director
March 3, 2009	By: /s/ Howard S. Klein Howard S. Klein Director
March 3, 2009	By: /s/ Charles E. Moore, Jr. Charles E. Moore, Jr. Director
March 3, 2009	By: /s/ Bonnie L. Phipps Bonnie Phipps Director
March 3, 2009	By: /s/ John Paul Rogers John Paul Rogers Director
March 3, 2009	By: /s/ William C. Rogers, III William C. Rogers, III Director
March 3, 2009	By: /s/ Francis X. Ryan Francis X. Ryan Director

Exhibit Index

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31.2	Certification by the Principal Financial Officer required by Exchange Act Rule 13a-14(a)	

32.1	Certification by the Principal Executive Officer
32.2	Certification by Principal Financial Officer

(1) Incorporated by reference to the Registrant's Form 8-K filed February 17, 2009 (File No.: 000-23090).

(2) Incorporated by reference from Registration Statement dated January 12, 1990 on SEC Form S-4 (1933 Act File No.: 33-33027).

(3) Incorporated by reference from Annual Report on Form 10-KSB for the fiscal year ended December 31, 1994 (1934 Act File No.: 0-23090).

(4) Incorporated by reference to the Registrant's Form 8-K filed June19, 2007 (File No.: 000-23090)

(5) Incorporated by reference to the Registrant's Form 8-K filed September 25, 2007 (File No. : 000-23090)

(6) Incorporated by reference to the Registrant's Form 8-K filed October 24, 2007 (File No. : 000-23090)

(7) Incorporated by reference to the Registrant's Form 8-K filed November 8, 2007 (File No. : 000-23090)

(8) Incorporated by reference to the Registrant's Form 8-K filed September 30, 2008 (File No.: 000-23090)

EXHIBIT 21.1

Subsidiaries of Carrollton Bancorp	*State of Incorporation*	*Owned by*	*Percentage Ownership*
Carrollton Bank	Maryland	Carrollton Bancorp	100%
Carrollton Financial Services Inc.	Maryland	Carrollton Bank	100%
Carrollton Community Development Corp.	Maryland	Carrollton Bank	96.4%
Carrollton Mortgage Services, Inc.	Maryland	Carrollton Bank	100%
Mulberry Street, LLC	Maryland	Carrollton Bank	100%

EXHIBIT 23.1

CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors
Carrollton Bancorp

As Independent Registered Public Accounting Firm, we hereby consent to the incorporation of our report dated March 3, 2009 on the consolidated financial statements of Carrollton Bancorp and Subsidiary included in this Form 10-K into Carrollton Bancorp's previously filed registration statements on Form S-8, File Nos. 333-82915 and 333-120929.

/s/ Rowles & Company, LLP

Baltimore, Maryland
March 3, 2009

EXHIBIT 31.1

CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER (EXCHANGE ACT RULE 13-A-14(A)

I, Robert A. Altieri, President and Chief Executive Officer, certify that:

(1) I have reviewed this annual report on Form 10-K of Carrollton Bancorp;

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

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

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

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

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

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

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

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

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

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

/s/ ROBERT A. ALTIERI
Robert A. Altieri
President and Chief Executive Officer

Date: March 3, 2009

EXHIBIT 31.2

CERTIFICATION OF PRINCIPAL FINANCIAL OFFICER

I, James M. Uveges, Chief Financial Officer, certify that:

(1) I have reviewed this annual report on Form 10-K of Carrollton Bancorp;

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

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

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

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

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

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

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

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

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

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

/s/ JAMES M. UVEGES
James M. Uveges
Senior Vice President and Chief Financial Officer

Date: March 3, 2009

EXHIBIT 32.1

CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER

I, Robert A. Altieri, President and Chief Executive Officer (principal executive officer) of Carrollton Bancorp (the "Registrant"), hereby certify pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes/Oxley Act of 2002, to the best of my knowledge and belief, that:

(1) such Form 10-K for the year ended December 31, 2008, fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) The information contained in such Form 10-K for the year ended December 31, 2008, fairly presents, in all material respects, the financial conditions and results of operations of Carrollton Bancorp.

/s/ ROBERT A. ALTIERI

Robert A. Altieri
President and Chief Executive Officer
March 3, 2009

EXHIBIT 32.2

CERTIFICATION OF PRINCIPAL FINANCIAL OFFICER

I, James M. Uveges, Senior Vice President and Chief Financial Officer (principal financial officer) of Carrollton Bancorp, hereby certify pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes/Oxley Act of 2002, to the best of my knowledge and belief, that:

(1) such Form 10-K for the year ended December 31, 2008, fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) the information contained in such Form 10-K for the year ended December 31, 2008, fairly presents, in all material respects, the financial conditions and results of operations of Carrollton Bancorp.

/s/ JAMES M. UVEGES
James M. Uveges
Senior Vice President and Chief Financial Officer
March 3, 2009

CARROLLTON BANCORP

7151 Columbia Gateway Drive, Suite A
Columbia, Maryland 21046

NOTICE OF ANNUAL MEETING OF SHAREHOLDERS
TO BE HELD ON MAY 12, 2009

To the Shareholders of Carrollton Bancorp:

The Annual Meeting (the "Annual Meeting") of Shareholders of Carrollton Bancorp, a Maryland corporation (the "Company"), will be held at 7151 Columbia Gateway Drive, Suite A, Columbia, Maryland 21046, on May 12, 2009 at 10:00 a.m., prevailing local time, for the purpose of considering and acting upon:

1. The election of four directors for three-year terms ending in 2012 and one director for a one year term ending in 2010 and in each case until their respective successors are duly elected and qualified.

2. The ratification of the appointment of Rowles & Company, LLP as the independent registered public accounting firm to serve for the fiscal year ending December 31, 2009.

3. The approval of the following advisory (non-binding) proposal:

   RESOLVED: that the shareholders of the Company approve the compensation of the Company's executives as described in the Summary Compensation Table as well as in the Compensation Discussion and Analysis and the other executive compensation tables and related discussions contained in the Proxy Statement for the 2009 Annual Meeting of Shareholders.

4. Any other matters that may properly come before the Annual Meeting or any adjournment thereof.

The close of business on March 25, 2009 has been fixed by the Board of Directors of the Company as the record date for determining shareholders entitled to receive notice of and to vote at the Annual Meeting or any adjournment thereof.

Your attention is directed to the enclosed Proxy Statement and annual report of the Company for the fiscal year ended December 31, 2008.

Whether or not you plan to attend the meeting in person all shareholders are urged to promptly vote your shares either via the Internet, or by telephone, or if you have received a copy of the proxy card by mail, by signing, dating and mailing the enclosed proxy. The enclosed envelope requires no postage if mailed in the

U.S.A. or Canada. Shareholders attending the meeting may revoke their proxies and personally vote on all matters that are considered. It is important that your shares be voted.

By Order of the Board of Directors

Allyson Cwiek
Secretary

Columbia, Maryland
March 27, 2009

Carrollton Bancorp
Proxy Statement

Table of Contents

CARROLLTON BANCORP
7151 Columbia Gateway Drive, Suite A
Columbia, Maryland 21046

PROXY STATEMENT
ANNUAL MEETING OF SHAREHOLDERS

TO BE HELD ON MAY 12, 2009

SOLICITATION, VOTING AND REVOCATION OF PROXIES

This Proxy Statement (the "Proxy Statement") and the enclosed proxy will be furnished on or about March 27, 2009 to the shareholders of Carrollton Bancorp (the "Company") as of the close of business on March 25, 2009, in connection with the solicitation of proxies by the Board of Directors of the Company (the "Board" or "Board of Directors") to be voted at the Annual Meeting of Shareholders to be held on May 12, 2009 at 10:00 a.m., prevailing local time (the "Annual Meeting"), and any adjournments thereof. The Annual Meeting of Shareholders will be held at our principal executive offices which are located at 7151 Columbia Gateway Drive, Suite A, Columbia, Maryland 21046.

The Board of Directors has selected Steven K. Breeden, Harold I. Hackerman and Howard S. Klein and each of them, to act as proxies with full power of substitution. A proxy may be revoked at any time prior to its exercise by (i) giving written notice of revocation to the Company, (ii) executing and delivering a substitute proxy to the Company, or (iii) attending the Annual Meeting and voting in person. Executed but unmarked proxies will be voted on all business matters as recommended by the Board of Directors.

Information About Proxy Materials and Voting

Pursuant to new rules recently adopted by the Securities and Exchange Commission (the "SEC") the Company has elected to provide shareholders access to proxy materials over the Internet. Accordingly, the Company has sent a Notice of Internet Availability of Proxy Materials (the "Notice") to shareholders of record and beneficial owners. All shareholders will have the ability to access the proxy materials on a website referred to in the Notice or request to receive a printed set of the proxy materials. Instructions on how to access the proxy material over the Internet or to request a printed copy may be found on the Notice. In addition, shareholders may request to receive proxy materials in printed form by mail on an ongoing basis.

Shareholders of record may vote in one of four ways: (i) by internet at https://secure.amstock.com/voteproxy/login2.asp, (ii) by toll-free telephone by following instructions on the proxy card, (iii) by completing and mailing your proxy card, or (iv) by written ballot at the Annual Meeting. A Company representative will give shareholders of record a ballot when they arrive. Beneficial owners may vote by following the voting instructions sent by their broker, trustee or nominee.

The cost of soliciting proxies will be borne by the Company. In addition to the solicitation of proxies by mail, the Company also may solicit proxies personally or by telephone or telegraph through its directors, officers, and regular employees. The Company also will request persons, firms, and corporations holding shares in their names or in the name of nominees that are beneficially owned by others to send proxy materials to and obtain proxies from those beneficial owners and will reimburse the holders for their reasonable expenses in doing so.

We plan to take advantage of the householding rules of the SEC that permit us to deliver one set of the proxy materials, one annual report and one Notice to shareholders who have the same address, unless they request otherwise. Doing so will allow us to reduce the expenses of delivering duplicate materials. We will continue to send a separate proxy card for each shareholder residing in a shared address.

Quorum Requirement

Consistent with state law and the Company's Bylaws, a majority of the shares entitled to vote on a particular matter, present in person or represented by proxy, constitutes a quorum as to such matter. Persons appointed by the Company to act as election inspectors for the meeting will count votes cast by proxy or in person at the Annual Meeting. Generally, abstentions and broker non-votes will not be counted as votes cast for proposals submitted to the Company's shareholders and will have no effect on the result of the vote, although they will count toward the presence of a quorum.

If a quorum is present, the affirmative vote of the holders of a plurality of the votes properly cast for the election of directors at the Annual Meeting is required to elect the four nominees for election for three-year terms expiring in 2012 and one nominee for election to complete the remainder of the term of a director who retired, which expires in 2010. Abstentions will not be treated as votes cast and will therefore have no effect on the outcome of the vote.

Approval of each of the other proposals requires the affirmative vote of a majority of the votes cast at the annual meeting. Abstentions from voting, as well as broker non-votes, if any, are not treated as votes cast and, therefore, will have no effect on the outcome of the vote on any proposal.

Voting Procedures

A copy of the Annual Report on Form 10-K for the year ended December 31, 2008, as filed with the SEC, but excluding exhibits, is provided with this Proxy Statement. Shareholders may obtain a copy of the exhibits to the Annual Report on Form 10-K, free of charge, upon writing Allyson Cwiek, Secretary, at Carrollton Bancorp, 7151 Columbia Gateway Drive, Suite A, Columbia, Maryland 21046. Shareholders also may access a copy of the Form 10-K including exhibits on the SEC Website at www.sec.gov or through the Company's Website at www.carrolltonbank.com. Click on "About Us" – "SEC Filings".

Shareholders who share the same address may receive only one Annual Report on Form 10-K and Proxy Statement, unless the shareholder has provided the Company with contrary instructions. Shareholders who wish to receive separate copies of the Annual Report on Form 10-K and Proxy Statement, and shareholders sharing an address who received multiple copies of these documents but wish to request delivery of single copies of them should follow the instructions provided by the shareholder's brokerage firms or banks or contact Allyson Cwiek at the above address or by phone at 410.536.7332 or 800.222.6656.

Submission of Matters to a Vote of Shareholders

There have been no matters submitted to a vote of the Company's shareholders since the Company's 2008 Annual Shareholders' Meeting held on May 13, 2008.

Voting Securities

The close of business on March 25, 2009 has been fixed by the Board of Directors as the record date for determining the shareholders entitled to receive notice of and to vote at the Annual Meeting.

There were 2,564,988 shares of Common Stock, $1.00 par value per share, outstanding as of March 9, 2009, each entitled to one vote.

PROPOSAL 1: ELECTION OF DIRECTORS

The Board of Directors has set the total number of directors at 12, in accordance with the Company's Charter and Bylaws. The Company's Board of Directors is divided into three classes, as nearly equal as possible. Each year the directors in one class are elected to serve for a term of three years, or until their respective successors are duly elected and qualified. The shareholders will vote at this Annual Meeting for the election of four directors for the three year term expiring at the Annual Meeting of Shareholders in 2012 and one director to serve for a remaining one year term expiring at the Annual Meeting of Shareholders in 2010.

The directors nominated to be elected to serve for three-year terms expiring at the Annual Meeting of Shareholders in 2012 and until their successors are duly elected and qualified are Messrs. Counselman, Hessler and Ryan and Ms. Phipps, and the director nominated to be elected to serve for a one-year term expiring at the Annual Meeting of Shareholders in 2010 and until his successor is duly elected and qualified is Mr. Rogers, III.

The proxies solicited hereby, unless directed to the contrary, will be voted "FOR" the election as directors of all five nominees listed in the following tables. A plurality of the shares voted at the Annual Meeting at which a quorum is present is sufficient to elect a nominee as a director.

The Board of Directors unanimously recommends a vote "FOR" the election of each of the nominees named below as directors of the Company.

In the event that any of the nominees should be unable to serve on the Board of Directors, the persons named in the proxy will vote for such substitute nominee or nominees as they, in their sole discretion, shall determine. The Board of Directors has no reason to believe that any nominee named herein will be unable to serve. Alternatively, the Board of Directors may elect to reduce the size of the Board of Directors.

The following material shows, as of December 31, 2008, the names and ages of all nominees, the principal occupation and business experience of each nominee during the last five years and the year in which each nominee was first elected to the Board of Directors. The material also contains information on those directors whose terms continue beyond the date of the Annual Meeting.

Nominees for Director Whose Terms Expire in 2009

Albert R. Counselman – Mr. Counselman, age 60, has served as a director of Carrollton Bank ("the Bank"), the principal subsidiary of the Company, since April 1985 and of the Company since its inception in 1990. Mr. Counselman was elected Chairman of the Board of the Company in January 2002. He has been President and Chief Executive Officer of Riggs, Counselman, Michaels & Downes, Inc., an insurance brokerage firm, since September 1987, and served in various executive positions with that firm from 1972 to September 1987.

David P. Hessler – Mr. Hessler, age 52, has served as a director of the Bank since March 1999, and the Company since May 1999. He has been President and CEO of Eastern Sales & Engineering, an electrical contracting and service maintenance firm, since 1987 and was Vice President from 1986 to 1987. Mr. Hessler has been Vice President of Advanced Petroleum Equipment, a distributorship, since its inception in 1998. (1)(3)(4)

Bonnie L. Phipps – Ms. Phipps, age 60, has served as a director of the Bank and of the Company since January 2, 2009. She has been President and CEO of St. Agnes Healthcare since December 2005. Prior to that, Ms. Phipps was President and CEO of St. Joseph's Health System in Atlanta, Georgia. She has held various positions in the healthcare field since 1974. (1)(2)(4) Effective January 2, 2009

Francis X. Ryan – Mr. Ryan, age 57, has served as a director of the Bank and of the Company since January 25, 2007. Since 1991, Mr. Ryan has served as President of F.X. Ryan & Associates, Ltd., a management consulting firm. (4)

William C. Rogers, III. – Mr. Rogers, age 53, has served as a director of the Bank and of the Company since September 2008. He has been a partner in the law firm of Rogers, Moore and Rogers and counsel to the Bank, since 1992. He has been a director of The Security Title Guarantee Corporation of Baltimore since 1983, and was President from 1993 until 2003. Mr. Rogers has been a director of Maryland Mortgage Company since 1983. Also, he has been Corporate Secretary and a director of Moreland Memorial Park Cemetery, Inc. since 1986.

Directors Continuing In Office

Directors Whose Terms Expire in 2010

Robert J. Aumiller – Mr. Aumiller, age 60, currently is serving as a director of the Bank and the Company beginning with his appointment in 2001. He has been the Executive Vice President and General Counsel of MacKenzie Commercial Real Estate Services, LLC involved in brokerage and real estate development of various commercial real estate projects, since 1983.

Charles E. Moore, Jr. – Mr. Moore, age 59, currently is serving as a director of the Bank and the Company beginning with his appointment in 2001. He is retired from being the Co-Founder, Director, President and CFO of TelAtlantic, a consolidation of rural telephone companies across the United States, from 1999 through 2007. (1)(2)(3)(4)

John Paul Rogers – Mr. Rogers, age 73, has served as director of the Bank since 1970 and of the Company since its inception in 1990. Mr. Rogers has been Chairman of the Board of the Bank since February 1994. He was a partner of the law firm of Rogers, Moore and Rogers, counsel of the Bank, from 1970 until 1992. Mr. Rogers was senior title officer of The Security Title Guarantee Corporation of Baltimore from May 1991 until December 1992, having served as President from March 1989 until May 1991, and as Executive Vice President from March 1970 until March 1989.

Directors Whose Terms Expire in 2011

Steven K. Breeden – Mr. Breeden, age 50, has served as a director of the Bank since June 1994 and of the Company since October 1995. Mr. Breeden is currently a managing member of Security Development LLC and related real estate and development companies, a position he has held since 1980. (2)(3)(4)

Harold I. Hackerman – Mr. Hackerman, age 57, has served as a director of the Bank and the Company since February 2002. Since 1984, Mr. Hackerman has been Vice President of Ellin & Tucker, a certified public accounting firm, and has provided audit, accounting and consulting services since 1973. (1)(2)(4)(5)

William L. Hermann – Mr. Hermann, age 67, has served as a director of the Bank and the Company since April, 2006. Mr. Herman is a retired certified public accountant; and, since 1981, the founder and Chief Executive Officer of William L. Hermann, Inc., a financial management and consulting company. (1)(2)(4)

Howard S. Klein – Mr. Klein, age 50, has served as a director of the Bank since March 1999 and of the Company since April 1999. Mr. Klein has been Vice President and General Counsel for Klein's Super Markets, a family-operated chain of seven full service supermarkets and related development and operating companies since 1987. (1)(4)

(1) Member of the Audit Committee
(2) Member of the Compensation Committee
(3) Member of the Nominating/Corporate Governance Committee
(4) Independent Director
(5) Financial expert for Audit Committee

Family Relationships

Mr. John Paul Rogers is Mr. William C. Rogers, III uncle. Mr. Howard S. Klein is married to Mr. John Paul Rogers' niece.

CORPORATE GOVERNANCE

Committees of the Board of Directors

The Board of Directors has an Audit Committee, Nominating/Corporate Governance Committee, Compensation Committee, Executive Committee, Loan Committee, Strategic Plan Committee, Strategic Finance Committee, Facilities Committee, and an Asset/Liability Committee. The Audit Committee, the Compensation Committee, and the Nominating/Corporate Governance Committee are discussed below.

The **Audit Committee** is composed of Messrs. Moore, Chairman Hackerman, Hermann, Klein and Ms. Phipps. Effective December 31, 2008, Mr. Hessler was replaced by Ms. Phipps. The Audit Committee is appointed by the Board to assist the Board in monitoring the integrity of the financial statements and of financial reporting, including the proper operation of internal and disclosure controls and procedures in accordance with the Sarbanes-Oxley Act of 2002, compliance with legal and regulatory requirements and the independence and performance of internal and external auditors. The Audit Committee reviews the Forms 10-K and 10-Q prior to filing. All members of the Audit Committee are "independent" as defined in applicable law, regulations of the SEC, the Federal Deposit Insurance Act and related regulations (the "FDIA"), and the Listing Standards of the NASDAQ Stock Market, Inc., (the "Listing Standards"). Members of the committee also meet all other applicable requirements of the SEC, FDIA, and Listing Standards for financial, accounting or related expertise. The Board of Directors has determined that Mr. Harold I. Hackerman qualifies as an audit committee financial expert under the Listing Standards and applicable securities regulations. During 2008, nine meetings of the Audit Committee were held. The Audit Committee also approves all insider loans. The Audit Committee may also examine and consider other matters relating to the financial affairs of the Company as it determines appropriate.

The **Compensation Committee** is composed of Messrs. Hackerman, Chairman Hermann, Hessler and Ms. Phipps. Effective December 31, 2008, Messrs Breeden and Moore were replaced by Mr. Hessler and Ms. Phipps. Mr. Hermann was Chairman during 2008. All members of the committee are independent directors within the meaning of the Listing Standards. The purpose of the Compensation Committee is to review and approve major compensation and benefit policies of the Company and the Bank. In addition, the Compensation Committee recommends to the Board the compensation to be paid to all officers, Senior Vice President and above, of the Company and Bank. The Compensation Committee also administered the Carrollton Bancorp 2007 Equity Plan (the "2007 Equity Plan") and the Carrollton Bancorp 1998 Long Term Incentive Plan, as amended (the "1998 Plan"). No new grants will be made under the 1998 Plan. During 2008, four meetings of the Compensation Committee were held.

The **Nominating/Corporate Governance Committee** is composed of Messrs. Hessler, Chairman Breeden, and Moore. Members of the committee are independent directors within the meaning of the Listing Standards. The purposes of the Nominating/Corporate Governance Committee are (a) to assist the Board by identifying individuals qualified to become Board members and to recommend to the Board nominees for the next annual meeting of shareholders, (b) to recommend to the Board the corporate governance principles applicable to us, (c) to lead the Board in its annual review of its performance, and (d) to recommend to the Board members the chairpersons of each committee. During 2008, there was one meeting of the Nominating/Corporate Governance Committee.

Code Of Ethics

The Company has a Code of Ethics that applies to all of its employees and directors with a specific code applicable to the Chief Executive Officer, Chief Financial Officer, and the Controller. The code of ethics is posted on the Company's website at www.carrolltonbank.com.

DIRECTOR COMPENSATION

Directors who are not employees of the Company or Bank received a monthly retainer fee of $1,000 for Board meetings and an additional $300 for attending each Board meeting and between $200 and $600 for each committee meeting attended. The Chairman of the Board of the Company and Bank received a monthly fee of $1,450. Directors do not receive additional fees for their service as directors of the Company. In addition, each non-employee director serving on the Board of Directors on the date of the Annual Meeting receives, pursuant to the 2007 Equity Plan, a grant of 300 shares of unrestricted stock. The Directors Deferred Compensation Plan (the "Plan") was frozen as of 1990. No new participants have entered the Plan since 1990. No new grants will be made under the 1998 Plan. However, incentive stock options issued under the 1998 Plan will remain outstanding until exercised or until the tenth anniversary of the grant date of such options. Options have a maximum term of ten years and an exercise price that may not be less than 100% of the closing price of the common stock on the date of the grant. Director's options are included in the computation of share dilution.

The following table sets forth the compensation paid to the Company's directors during the year ended December 31, 2008.

2008 Directors' Compensation

Name	Fees Earned or Paid in Cash (1)	Stock Awards (2)	Option Awards (3)	Non-Equity Incentive Plan Compensation	Change in Pension Value and Nonqualified Deferred Compensation Earnings (4)	All Other Compensation	Total
Robert J. Aumiller	$18,700	$4,200	$158	—	—	—	$23,058
Steven K. Breeden	22,950	4,200	158	—	—	—	27,308
Albert R. Counselman	17,700	4,200	158	—	—	—	22,058
Harold I. Hackerman	20,200	4,200	158	—	—	—	24,558
William L. Hermann	22,350	4,200	158	—	—	—	27,128
David P. Hessler	22,950	4,200	158	—	—	—	27,308
Howard S. Klein	21,800	4,200	158	—	—	—	26,158
Charles E. Moore, Jr.	24,400	4,200	158	—	—	—	28,758
John P. Rogers	26,600	4,200	158	—	—	—	30,958
William C. Rogers, Jr. (5)	21,250	4,200	158	—	—	—	25,608

William C. Rogers, III	4,500	—	—	—	—	—	4,500
Francis X. Ryan (6)	30,050	4,200	413	—	—	—	34,663

(1) Please see the description of the directors' fees above.

(2) Stock was awarded pursuant to the 2007 Equity Plan approved at the May 13, 2008 Annual Meeting.

(3) There were no new stock options granted in 2008. The amounts shown represent the amount of stock-based compensation expense related to stock options recognized during 2008 in accordance with SFAS 123R. At December 31, 2008, directors held the unexercised (vested and unvested) options for the following number of shares: Aumiller – 2,100, Breeden – 5,040, Counselman – 1,260, Hackerman – 3,780, Hermann – 630, Hessler – 5,040, Klein – 1,260, Moore – 630, P. Rogers – 4,410, W. Rogers, Jr. – 2,510, Ryan – 630.

(4) We report earnings on nonqualified deferred compensation in this table only to the extent such earnings are preferential or "above market."

(5) Mr. William C. Rogers, Jr. retired from the board of the Bank and the Company effective December 26, 2008 after 53 years of service.

(6) Mr. Ryan received a fee of $12,250 for consulting services to the Company in 2008.

Attendance at Board Meetings and Annual Meetings

The Board of Directors of the Company met six times and the Board of Directors of the Bank met twelve times during the year ended December 31, 2008. The Board of Directors of the Bank meets regularly twelve times each year. No director attended fewer than 75% of the total number of meetings of both Boards and each committee to which they were assigned during the year ended December 31, 2008. The Company expects, but does not require, directors to attend the annual meeting of shareholders. All of our directors attended last year's annual meeting of shareholders.

Shareholder Communications with the Board

Shareholders may send communications to the Board by mailing the same addressed to: Board of Directors, Carrollton Bancorp, 7151 Columbia Gateway Drive, Suite A, Columbia, Maryland 21046.

Director Nomination Process

The Nominating/Corporate Governance Committee operates pursuant to a charter adopted by the Board, a copy of which can be found on the Company's website at www.carrolltonbank.com.

In recommending director nominees, the Nominating/Corporate Governance Committee will consider candidates recommended by the Company's shareholders. Notice of Nominees to the Board recommended by shareholders must be timely, delivered in writing to the Secretary of the Company prior to the meeting. To be timely, the notice must be delivered within the time permitted for nomination of directors in Article I, Section VII of the Bylaws of the Company. The notice must include:

- information regarding the shareholder making the nomination, including name, address, and the number of shares of our stock beneficially owned by the shareholder; and

- the name, age, principal occupation or employment and residence and business address of the person(s) being nominated and such other information regarding each nominee that would be required in a proxy statement filed pursuant to the proxy rules adopted by the Securities and Exchange Commission if the person had been nominated for election by or at the direction of the Board of Directors.

The Nominating/Corporate Governance Committee will evaluate nominees recommended by shareholders against the same criteria that it uses to evaluate other nominees. Whether recommended by a shareholder or chosen independently by the Nominating/Corporate Governance Committee, a candidate will be recommended for nomination based on his or her talents in relation to the talents of the existing Board members and the needs of the Board. It is the goal of the Nominating/Corporate Governance Committee in recommending director nominees to foster relationships among directors that are complimentary and that will make the Board most effective.

A candidate, whether recommended by a Company shareholder or otherwise, will not be considered for nomination unless he or she (i) is of good character, (ii) is a citizen of the United States, (iii) owns shares of the Company's common stock, the aggregate value of which is not less than $500, as determined in accordance with the Financial Institutions Article of the Annotated Code of Maryland, and (iv) satisfies all other requirements imposed under applicable law. Additionally, the Nominating/Corporate Governance Committee believes that it is important for candidates recommended for nomination to have the ability to attract business to the Company, live or work within the communities in which the Company operates, and possess the skills and expertise necessary to provide leadership to the Company. Certain Board positions, such as Audit Committee membership, may require other special skills or expertise. To identify potential nominees for the Board, the Nominating/Corporate Governance Committee first evaluates the current members of the Board willing to continue in service. Current members of the Board are considered for re-nomination, balancing the value of their continued service with that of obtaining new perspectives and in view of our developing needs. If necessary, the Nominating/Corporate Governance Committee then solicits ideas for possible candidates from a number of sources, which can include other Board members, senior management, individuals personally known to members of the Board and research. The Nominating/Corporate Governance Committee may also retain a third party to assist it in identifying potential nominees; however, the committee has not done so in the past.

The Nominating/Corporate Governance Committee is responsible for assembling and maintaining a list of qualified candidates to fill vacancies on the Board. The Nominating/Corporate Governance Committee periodically reviews this list and researches the talent, skills, expertise, and general background of these candidates.

SECURITY OWNERSHIP OF DIRECTORS AND EXECUTIVE OFFICERS

The following table sets forth, as of December 31, 2008 certain information concerning shares of the Common Stock of the Company beneficially owned by (i) the executive officers of the Company and Bank; (ii) all current directors and nominees for directors of the Company and the Bank; (iii) all directors and executive officers of the Company and the Bank as a group; and (iv) other significant shareholders.

Beneficial Owner	Amount and Nature of Beneficial Ownership	Percent of Class
Executive Officers:		
Chief Executive Officer – Bank and Company: Robert A. Altieri	39,698(2)	1.55%
Senior Vice President – Bank and Company: Michael J. Camiel	2,000(3)	*
Senior Vice President – Bank and Company: Gary M. Jewell	28,483(4)	1.11%
Senior Vice President – Bank and Company: William D. Sherman	6,000(5)	*
Senior Vice President – Bank and Company: Lola B. Stokes	105	*
Senior Vice President – Bank and Company: James M. Uveges	7,500(6)	*
Directors:		
Robert J. Aumiller – Bank and Company	8,055(7)	*
Steven K. Breeden – Bank and Company	23,718(8)	*
Albert R. Counselman – Bank and Company	40,773(9)	1.59%
Harold I. Hackerman – Bank and Company	9,303(10)	*
William L. Hermann – Bank and Company	2,120(11)	*
David P. Hessler – Bank and Company	11,856(12)	*
Howard S. Klein – Bank and Company	16,837(13)	*
Charles E. Moore, Jr. – Bank and Company	14,420(14)	*
John Paul Rogers – Bank and Company	141,376(15)	5.51%
William C. Rogers, III – Bank and Company	96,135(16)	3.75%
Francis X. Ryan - Bank and Company	11,243(17)	*
All Directors and Executive Officers of the Company as a Group (17 persons)	449,578(18)	17.53%

* Less than 1%

(1) Unless otherwise indicated, the named person has sole voting and investment power with respect to all shares.

(2) Includes 1,157 shares owned jointly by Mr. Altieri and his wife, 191 shares Mr. Altieri holds as trustee for minor children under the Maryland Uniform Gifts to Minors Act, and 38,350 fully vested options to purchase shares at an exercise price of between $10.94 and $15.41 per share.

(3) Includes 2,000 fully vested options to purchase shares at an exercise price of $14.50 per share.

(4) Includes 4,050 shares owned by Mr. Jewell and his wife and 24,433 fully vested options to purchase shares at an exercise price of between $12.67 and $17.16 per share.

(5) Includes 6,000 fully vested options to purchase shares at an exercise price of between $14.50 and $16.02 per share.

(6) Includes 2,500 shares owned by Mr. Uveges and 5,000 fully vested options to purchase shares at an exercise price of $14.85 per share.

(7) Includes 6,065 shares owned jointly by Mr. Aumiller and his wife and 1,890 fully vested options to purchase shares at an exercise price of between $14.45 and $16.31 per share.

(8) Includes 13,295 shares owned jointly by Mr. Breeden and his wife and 4,830 fully vested options to purchase shares at an exercise price of between $9.71 and $16.69 per share.

(9) Includes 1,050 fully vested options to purchase shares at an exercise price of between $14.45 and $16.31 per share, but excludes 23,944 shares owned by Mr. Counselman's wife.

(10) Includes 5,299 shares owned jointly by Mr. Hackerman and his wife, and 3,570 fully vested options to purchase shares at an exercise price of between $12.11 and $16.31 per share.

(11) Includes 420 fully vested options to purchase shares at an exercise price of $18.03 per share.

(12) Includes 1,470 shares owned jointly by Mr. Hessler and his wife and 4,830 fully vested options to purchase shares at an exercise price of between $9.71 and $16.31 per share.

(13) Includes 1,680 shares owned by Colgate Investments, LLP, of which Mr. Klein is partner and 2,079 shares Mr. Klein holds as trustee for minor children under the Maryland Uniform Gifts to Minors Act. Also includes 1,050 fully vested options to purchase shares at an exercise price of between $14.45 and $16.31 per share.

(14) Includes 420 fully vested options to purchase at an exercise price of between $14.45 and $16.31. Excludes 18,000 shares owned by Mr. Moore's wife and 4,689 shares of which Mrs. Moore has voting control as a personal representative of an estate.

(15) Includes 4,200 fully vested options to purchase shares at an exercise price of between $12.11 and $16.31 per share. Also includes 63 shares owned by The Security Title Guarantee Corporation of Baltimore and 9,981 shares owned by Maryland Mortgage Company of which Mr. Rogers is a principal shareholder.

(16) Includes 63 shares owned by The Security Title Guarantee Corporation of Baltimore of which William C. Rogers, III is a shareholder and Director. Also includes 1,110 shares Mr. Rogers holds as custodian for his children. Includes 13,015 shares owned by the Moreland Memorial Park Bronze Perpetual Care Trust Fund, 47,470 owned by the Moreland Memorial Park Perpetual Care Fund, 9,981 shares owned by Maryland Mortgage Company of which William C. Rogers, III is Vice President and Director and 5,506 shares owned by HEWI Partnership of which Mr. Rogers is an owner/partner. Also includes 7,429 shares of which Mr. Rogers has voting control as a trustee of three trusts.

(17) Includes 4,140 shares owned by Semper Finance, Inc. of Maryland and 4,703 shares owned by Semper Finance, Inc. of Pennsylvania of which Mr. Ryan is President and principal owner. Also includes 210 fully vested options to purchase shares at an exercise price of $17.25 per share.

(18) All directors, executive officers and other significant shareholders may be contacted at the Company's corporate offices by addressing correspondence to the appropriate person, care of Carrollton Bancorp, 7151 Columbia Gateway Drive, Suite A, Columbia, Maryland, 21046.

Certain Beneficial Owners

The table below includes all of the shareholders of the Company known by the Company to beneficially own more than five percent of its Common Stock as of December 31, 2008 unless otherwise indicated.

Name and address of Beneficial Owner	Common Stock Beneficially Owned	Investment Power			Voting Power			Common Stock Beneficially Owned as a Percentage of Outstanding Common Stock
		Sole	Shared	None	Sole	Shared	None	
John Paul Rogers* 46 C Queen Anne Way Chester, MD 21619	141,376	131,332	10,044		131,332	10,044		5.51%
William C. Rogers, Jr.* 6 South Calvert Street Baltimore, MD 21202	210,372	4,580	205,792		4,580	205,792		8.20%
Patricia A. Rogers* P.O. Box 246 Gibson Island, MD 21056	108,426	98,382	10,044		98,382	10,044		4.23%

*The information furnished is based upon information contained in a respective Schedule 13G filed with the SEC, a copy of which was provided to the Company.

Executive Officers

Certain information regarding significant employees of the Company and Bank other than those previously mentioned is set forth below:

Robert A. Altieri – Mr. Altieri, age 47, has been President and Chief Executive Officer of both the Bank and Company since his appointment in February 2001. Mr. Altieri previously was the Senior Vice President – Lending of the Bank since June 1994, and Vice President – Commercial Lending since September 1991.

Michael J. Camiel – Mr. Camiel, age 55, has been Senior Vice President - Chief Credit Officer since March 2007. He was previously Vice President – Chief Credit Officer from March 2003 to March 2007. Prior to joining the Bank, Mr. Camiel was a Relationship Manager with Maryland Department of Business and Economic Development from June 1999 to March 2003.

Gary M. Jewell – Mr. Jewell, age 62, has been Senior Vice President – Electronic Banking since July 1998. He was previously Senior Vice President and Retail Delivery Group Manager from March 1996 to July 1998. Prior to joining the Bank, Mr. Jewell was Director of Product Management and Point of Sale Services for the MOST EFT network in Reston, Virginia from March 1995 to March 1996.

Deanna L. Lintz – Ms. Lintz, age 40, has been Senior Vice President – Branch Administration since March 2007. She was previously Relationship Manager/Business Banking for M&T Bank from February 2006 to March 2007. Ms. Lintz held a similar position at Provident Bank from September 2004 to February 2006. Prior to September 2004, Ms. Lintz spent 14 years with Bank of America where she held a variety of positions.

William D. Sherman – Mr. Sherman, age 57, has been Senior Vice President – Chief Lending Officer since March 23, 2007. He was previously the Team Leader for Commercial Real Estate Lending from April 2003 through March 2007. Prior to working at Carrollton Bank, Mr. Sherman was in Commercial Real Estate Lending with Susquehanna Bank from April 1998 through April 2003.

Lola B. Stokes – Mrs. Stokes, age 51, has been Senior Vice President and Compliance/CRA Director of the Bank since June 2006. She was previously Senior Vice President in charge of Bank Secrecy Act at Provident Bank since January 2005. Prior to that, Mrs. Stokes held the position of Vice President of Compliance at Carrollton Bank from July 2000 to January 2005.

James M. Uveges – Mr. Uveges, age 58, has been Senior Vice President and Chief Financial Officer of the Company and Bank since June 6, 2005. He was previously an Interim Executive Consultant from May 2004 to June 2005. Prior to that, Mr. Uveges held the position of Senior Vice President and Chief Financial Officer at Spectera, Inc. from March 1999 to April 2004, Susquehanna Bank from January 1998 to February 1999 and American National Bancorp from 1990 to 1997.

Compensation Discussion and Analysis

Overview of Compensation Philosophy and Program

The Company’s executive compensation program is designed to:

- Align the financial interests of the executive officers with the long-term interests of the Company’s shareholders;
- Attract and retain high performing executive officers to lead the Company to greater levels of profitability; and
- Motivate and incent executive officers to attain the Company’s earnings and performance goals.

The compensation program for the Company’s executive officers has four primary components:

- base salary;
- annual incentive awards;
- long-term equity-based awards; and
- employee benefits as well as perquisites.

The Compensation Committee has the authority to obtain the advice and assistance of legal or independent compensation consulting firms as it deems desirable or appropriate. In developing the compensation program for 2008, the Compensation Committee conducted a review of the executive compensation program.

The Compensation Committee operates pursuant to a charter adopted by the Board, a copy of which, can be found on the Company’s website at www.carrolltonbank.com.

The philosophy is to pay conservatively competitive base salaries based on company and individual experience, performance, and contributions. Short-term incentives, generally payable in cash, and long-term incentives, generally provided through equity based awards, are targeted to be competitive but depend more heavily upon Company performance than does base pay. Total compensation and accountability are intended to increase with position and responsibility.

The Company recognizes that executives have significant influence on the overall financial results of the Company and aligns the financial interests of the executive officers with the long-term interests of the shareholders by using equity-based awards that increase in value as shareholder value increases and by choosing financial measures and goals for cash incentive compensation that are based on the key measures that drive the financial performance of the Company.

Effect of the Emergency Economic Stabilization Act of 2008

On October 14, 2008, the United States Department of Treasury (the "Treasury Department") announced the Troubled Asset Relief Program Capital Purchase Program (the "Capital Purchase Program" or "CPP") under the Emergency Economic Stabilization Act of 2008 ("EESA"). Pursuant to the Capital Purchase Program, the Treasury Department would make preferred stock investments in participating financial institutions.

We participated in the Capital Purchase Program in 2009 by selling preferred stock and a common stock purchase warrant to the Treasury Department. As a result, we became subject to certain executive compensation requirements under EESA, Treasury Department regulations, and the contract pursuant to which we sold such preferred stock. Those requirements apply to what the Treasury Department refers to as our Senior Executive Officers ("SEOs"). Presently, these are the same officers who are our Named Executive Officers (as defined herein). Those requirements are:

• Prohibition on Compensation that Provides an Incentive to Take Unnecessary and Excessive Risks. EESA prohibits us from providing incentive compensation arrangements that encourage our SEOs to take unnecessary and excessive risks that threaten the value of the financial institution.

- • Risk Review. Treasury Department regulations require the Compensation Committee to review SEO incentive compensation arrangements with our senior risk officers to ensure that SEOs are not encouraged to take such risks. The regulations also require the Compensation Committee to meet at least annually with our senior risk officers to discuss and review the relationship between our risk management policies and practices and the SEO incentive compensation arrangements.

• Clawback. EESA requires us to recover any bonus or incentive compensation paid to an SEO where the payment is later found to have been based on statements of earnings, gains, or other criteria which prove to be materially inaccurate. We have made certain amendments to the employment agreements of certain SEOs (the "SEO Employment Agreements") to conform to the details of EESA. One cash bonus has been paid to an SEO in 2007 and 2008 based on the Company's Point of Sale revenue which has been paid to the Company.

• Golden Parachutes. We contractually agreed to abide by a provision of EESA which limits the amounts that can be paid under change in control and similar agreements which provide payments upon separation of service. EESA also amended Section 280G of the Internal Revenue Code by expanding the definition of a parachute payment to include certain severance payments paid by reason of an involuntary termination or in connection with bankruptcy, liquidation or receivership of the employer. Each SEO has contractually agreed to abide by the limits imposed by EESA for so long as the limit applies to us and to him or her. The changes to the SEO Employment Agreements as a result of EESA and Section 280G are discussed below under the heading "Employment Agreements", below.

• Limit on Tax Deduction. A provision of EESA and Treasury Department regulations limits our tax deduction for compensation paid to any SEO to $500,000 annually. Each of our SEO's annual compensation is less than $500,000. The provision of EESA amended the Internal Revenue Code by adding 162(m)(5). Section 162(m)(5) imposes the $500,000 deduction limit. In addition, prior to the amendment, certain performance based compensation paid under shareholder approved plans did not count toward such deduction limit. EESA and Section 162(m)(5) eliminate that exclusion for us. We discuss the effect of this provision in greater detail under the heading, "Tax and Accounting Implications", below.

• Binding SEO Agreements. Prior to selling our preferred stock to the Treasury Department, each of our SEOs executed a waiver which voluntarily waived any claim against the United States or the Company for any change in his or her compensation and other benefits to the extent necessary to comply with these EESA requirements. These waivers will remain effective for so long as the Treasury Department owns any of our CPP debt or equity securities. We publicly filed a form of these waivers with the SEC as Exhibit 10.2 to our Current Report on Form 8−K on February 17, 2009.

Effect of Treasury Department Guidelines Announced February 4, 2009

On February 4, 2009, the Treasury Department announced executive compensation guidelines (the "Treasury Guidelines"). The Treasury Guidelines contain expansive new restrictions on executive compensation for financial institutions and other companies participating in the CPP. The Treasury Guidelines generally continue the existing restrictions under

EESA and add substantially to them in several areas. Among other things, the Treasury Guidelines contemplate an absolute $500,000 annual compensation limit for senior executives under certain circumstances. The Treasury Guidelines do not define which executives would be subject to this limit, but do clarify that such limit would not apply to CPP participants unless they further participated in an exceptional assistance program or further participated in a generally available capital access program.

However, the Treasury Guidelines are general in nature and appear to contemplate new rulemaking by Treasury before they become effective. Further, many, but not all of the elements of the Treasury Guidelines were incorporated into ARRA, discussed below.

Effect of the America Reinvestment and Recovery Act of 2009

On February 17, 2009, President Obama signed into law the America Reinvestment and Recovery Act of 2009 (“ARRA”). ARRA contains expansive new restrictions on executive compensation for financial institutions and other companies participating in the CPP. These restrictions apply to us. ARRA amends the executive compensation and corporate governance provisions of EESA. In doing so it continues all the same compensation and governance restrictions and adds substantially to the restrictions in several areas. ARRA implements many, but not all, of the restrictions in the Treasury Guidelines and in several instances goes beyond the Treasury Guidelines. We already comply with many of the new requirements of ARRA, and will comply with all other new requirements of ARRA promptly after the Treasury Department publishes the regulations contemplated by ARRA.

Some key features of the new executive compensation restrictions in ARRA are described below.

• ARRA prohibits bonus and similar payments to top employees. ARRA prohibits the payment of any “bonus, retention award, or incentive compensation” to our five Named Executive Officers and the next 20 most highly−compensated employees for as long as any CPP−related obligations are outstanding. The prohibition does not apply to bonuses payable pursuant to “employment agreements” in effect prior to February 11, 2009. ARRA does not explain how to identify the most highly−compensated employees and does not define “incentive compensation.” The Treasury Guidelines do not contain a similar limit on bonuses. Instead, the Treasury Guidelines impose a $500,000 annual compensation cap for a company’s senior executive officers, but allow the cap to be waived for all companies other than those receiving “exceptional” assistance. We have not received “exceptional assistance.” Waiver under the Treasury Guidelines is conditioned on our full disclosure of compensation and allowing shareholders a non−binding “say on pay” vote.

• Limited amount of restricted stock excluded from bonus prohibition. “Long−term” restricted stock is excluded from ARRA’s bonus prohibition, but only to the extent the value of the stock does not exceed one−third of the total amount of annual compensation of the employee receiving the stock, the stock does not “fully vest” until after all CPP−related obligations have been satisfied, and any other conditions which the Treasury Department may specify have been met. The Treasury Guidelines also exempt an unlimited amount of restricted stock from the $500,000 annual compensation cap described above. Neither ARRA nor the Treasury Guidelines explain how to value various items, such as equity compensation, indirect compensation such as benefits and taxes, when assessing this limit.

• Shareholder “say on pay” vote required. ARRA requires every company receiving CPP assistance to permit a non−binding shareholder vote to approve the compensation of executives as disclosed in the company’s proxy statement. The Treasury Guidelines contain a similar requirement but only for companies receiving “exceptional” assistance. ARRA directs the SEC to adopt regulations within one year to implement “say on pay.” We have included a “say on pay” proposal as Proposal 3 in this Proxy Statement.

• Stricter restrictions on “golden parachute” payments. EESA generally limited “golden parachute” payments to senior executives to 2.99 times the executives’ base compensation. ARRA prohibits any payment to a senior executive officer or any of the next five most highly−compensated employees upon termination of employment for any reason for as long as any CPP−related obligations remain outstanding. For all companies other than companies receiving “exceptional” assistance, the Treasury Guidelines limit golden parachute payments to one time base compensation and only apply the limit to the senior executive officers.

• Broader bonus clawback requirements. EESA required companies participating in the CPP to recover any bonus or other incentive payment paid to a senior executive officer on the basis of materially inaccurate financial or other performance criteria. ARRA extends this recovery requirement to the next 20 most highly compensated employees in addition to the senior executive officers. This extension is consistent with the Treasury Guidelines.

• Prohibition on compensation plans that "encourage" earnings manipulation. ARRA prohibits CPP participants from implementing any compensation plan that would encourage manipulation of the reported earnings of the Company in order to enhance the compensation of any of its employees. The Treasury Guidelines do not contain a similar requirement.

• Board compensation committee required. ARRA requires CPP participants to establish a board compensation committee and requires the committee to meet at least semiannually to discuss and evaluate employee compensation plans in light of an assessment of any risk to the company posed by such plans. The Treasury guidelines do not contain a similar requirement.

• New reporting and certification requirements. ARRA requires the CEO and CFO of any publicly−traded company participating in the CPP to provide a written certification of compliance with the executive compensation restrictions in ARRA in the Company's annual filings with the SEC (presumably its annual report on Form 10−K or proxy statement). The Treasury Guidelines require reporting and certification as well but do not detail how the reporting and certification are to be accomplished. Recent guidance from the SEC indicates that the SEC is not currently requiring these certifications.

• Policy on luxury expenditures. ARRA requires each company participating in the CPP to implement a company−wide policy regarding excessive or luxury expenditures, including excessive expenditures on entertainment or events, office and facility renovations, aviation or other transportation services. This is consistent with the Treasury Guidelines which contain a similar requirement.

• Treasury review of prior payments. ARRA directs the Treasury Department to review bonuses, retention awards, and other compensation paid to the senior executive officers and the next 20 most highly−compensated employees of each company receiving CPP assistance before ARRA was enacted, and to "seek to negotiate" with the CPP recipient and affected employees for reimbursement if it finds any such payments were inconsistent with CPP or otherwise in conflict with the public interest.

In addition to the above requirements, ARRA adopts and continues two requirements from EESA essentially unchanged:

• $500,000 annual deduction limit. Like EESA, ARRA prohibits CPP participants from deducting annual compensation paid to senior executive officers in excess of $500,000. The Treasury Guidelines, in contrast, contain the $500,000 annual compensation cap for senior executives described above (which may be waived by all companies other than those receiving "exceptional" assistance) but do not specifically address the deduction limit.

• No excessive risks. Like EESA, ARRA requires the Treasury Department to implement limits on compensation that exclude incentives for senior executive officers of a Company participating in the CPP to take unnecessary and excessive risks that threaten the value of the company for as long as any CPP−related obligation remains outstanding. The Treasury Department implemented this directive under EESA by requiring periodic compensation committee review and certification of the risk characteristics of a company's incentive compensation arrangements, and presumably these same review and certification requirements would apply going forward under ARRA. ARRA requires that the compensation committee perform such a review at least semi−annually.

ARRA requires both the Treasury Department and the SEC to issue rules to implement these new executive compensation restrictions.

Many aspects of the foregoing restrictions will not be clear until Treasury and the SEC publish new rules.

The foregoing restrictions imposed by ARRA implement many, but not all, of the restrictions of the Treasury Guidelines. At the present time, the Treasury Department has not announced whether it intends to publish rules to implement the aspects of the Treasury Guidelines that were not addressed by ARRA.

The Company has already implemented, or is in the process of implementing, the prior requirements of EESA. The Compensation Committee will consider the new limits on executive compensation of ARRA, the Treasury Guidelines, and any forthcoming regulations. When such regulations are published, the Compensation Committee promptly will make appropriate changes to the Company's executive compensation program, if needed.

Base Salary

The Company believes that competitive base salaries are necessary to attract and retain high performing executive officers. In determining base salaries, the Compensation Committee considers the executive's qualifications and experience, scope of responsibilities and future potential, the goals and objectives established for the executive, the executive's past performance, as well as competitive salary practices at other financial institutions.

With respect to the compensation of the Company's Chief Executive Officer, all of the members of the board of directors provide input and recommendations through a formal annual performance review process. The performance review of the Chief Executive Officer is generally based on objective criteria including performance of the Company, accomplishment of strategic objectives, development of management, and other measures of performance.

The Compensation Committee compared the proposed compensation of Mr. Altieri, the Company's Chief Executive Officer, with independent studies published reflecting compensation information of the peer group commercial banking institutions participating in the study and with the compensation of executive officers of banking institutions, based on proxy information covering institutions comparable to the Company in terms of criteria including the nature and quality of operations, or geographic proximity. This group included financial institutions having high returns on assets, capital significantly in excess of that required by current federal regulations, and located within a 100 mile radius of Baltimore, Maryland so as to include companies operating in a comparable economic climate. No target was established in the comparison with this group of institutions.

The average salary increase for the six Senior Vice Presidents in 2008 was 4.00%. The Chief Executive Officer received an increase of 4.00%. The base salary earned in 2008 by each of the Named Executive Officers is set forth in the "Summary Compensation Table."

Annual Incentive Plan

All of the Company's Named Executive Officers participate in the Bonus Plan ("BP"). The BP encourages executive officers of the Company to work together as a team to achieve specific annual financial goals. The BP is designed to motivate executive officers of the Company to achieve strategic goals, strengthen links between pay and the performance of the Company and align management's interests more closely with the interests of the shareholders.

The plan is designed to pay out a cash reward based on pre-established key performance indicators, which also has a minimum net income trigger that must be met before payouts may be made. The key performance indicators are:

- Growth as measured by gross loans, noninterest bearing accounts, and interest-bearing accounts and repurchase agreements;
- Pricing/profitability as measured through net interest margin, fee and service charge income;
- Quality as measured through non-performing assets and net charge offs and
- Productivity as measured through efficiency ratio.

Incentives are calculated based on budget and business plan goals as measured by the key performance indicators. For 2008, the budgeted amounts were approved at the December 2007 meeting of the Board of Directors. No payouts were made in 2008 based on the final Company performance for the year ended December 31, 2008. In 2008, Mr. Jewell received $33,438 in accordance with the terms of his employment agreement.

2007 Equity Plan

The 2007 Equity Plan was approved at the Company's Annual Meeting of Shareholders held on May 15, 2007. All of the Company's Named Executive Officers participate in receiving equity awards under the Company's 2007 Equity Plan. The purpose of long-term compensation arrangements is to more closely align the financial interests of the executive officers with the long-term interests of the Company's shareholders. Vesting schedules for equity based awards also encourage officer retention. The 2007 Equity Plan provides for a variety of different types of compensation arrangements, such as stock options, restricted stock, stock appreciation rights, restricted performance stock, unrestricted company stock and performance unit awards, all of which increase in value as the value of the Common Stock increases. The Compensation Committee recommends, in its discretion, the form and number of equity based awards and the full Board of Directors approves the awards. The 2007 Equity Plan prescribes that all outstanding awards automatically become fully vested on such change in control, all restrictions, if any, with respect to such awards, shall lapse, and all performance criteria, if any, with respect to such awards, shall be deemed to have been met in full. The 2007 Equity Plan provides for automatic annual grants of 300 shares of unrestricted stock of the Company to each non-employee director serving on the Board of Directors on the date of the Annual Meeting of the Shareholders.

1998 Plan

No new grants will be made under the 1998 Plan. However, incentive stock options issued under the plan will remain outstanding until exercised or until the tenth anniversary of the grant date of such options.

Potential Post-Employment Payments

The Company has entered into certain SEO Employment Agreements and maintains certain plans that will require it to provide compensation to Named Executive Officers in the event of a termination of employment. Post-employment payments are provided for under the SEO Employment Agreements described in the "Executive Compensation – Employment Agreements" section of this Proxy Statement, the 2007 Equity Plan and the 1998 Plan.

Employment Agreements

Upon termination without cause or upon a change in control, Mr. Altieri, Mr. Jewell, Mrs. Stokes and Mr. Uveges will be eligible for specific benefits under their respective SEO Employment Agreements. These benefits are outlined in the "Executive Compensation – Employment Agreements" section of this Proxy Statement.

Potential Payments Upon Termination

The table below represents the lump sum maximum amount each Named Executive Officer would have been eligible to receive under their respective employment agreement upon a change in control or if their employment was terminated under one of the various scenarios described below as of December 31, 2008. Benefits payable under the Company's defined benefit/pension plan or 401(K) Plan are not included.

Name	Quit/Termination for Cause ($)	Involuntary Termination Not For Cause ($)	Change in Control ($)
Robert A. Altieri	—	$515,736	$692,660
Gary M. Jewell	—	346,609	384,086
Lola B. Stokes	—	139,288	131,152
James M. Uveges	—	183,432	289,758

Tax and Accounting Implications

Section 162(m) of the Internal Revenue Code generally disallows a tax deduction to publicly held companies for compensation paid to the Chief Executive Officer and the four most highly compensated executive officers other than the Chief Executive Officer, to the extent that total compensation exceeds $1 million per covered officer in any taxable year. As discussed above, a provision of EESA and Treasury Department regulations now limit the Company's tax deduction for compensation paid to any SEO to $500,000 annually. The $1 million limitation previously applied only to compensation which was not considered to be performance-based. Compensation deemed paid by the Company in connection with disqualifying dispositions of incentive stock option shares or exercises of non-qualified stock options and stock appreciation rights granted under the 2007 Equity Plan qualifies as performance-based compensation for purposes of Section 162(m) if the grants were made by a committee of "outside directors" as defined under Section 162(m). As discussed above, however, a provision of EESA eliminated the exclusion for performance-based compensation for purposes of Section 162(m) for the Company.

While we anticipate that any compensation deemed paid by us in connection with disqualifying dispositions of incentive stock option shares or exercises of non-qualified stock options and stock appreciation rights will qualify as performance-based compensation for purposes of Section 162(m), based on the provisions of EESA, such compensation will nevertheless be taken into account for purposes of the $500,000 limitation. Accordingly, all compensation deemed paid with respect to those stock options should no longer be deductible by us without limitation under Section 162(m) of the Internal Revenue Code. Compensation paid by us in connection with restricted stock, restricted performance stock, unrestricted stock and performance unit awards may be taken into account for purposes of the $500,000 limitation unless the non-employee director or key employee is not subject to Section 162(m) at the time the compensation is taken into account for purposes of Section 162(m).

During 2008, none of the Company's SEOs received total compensation in excess of $500,000 and accordingly, all compensation paid to the Company's SEOs should be deductible by the Company without limitation under Section 162(m) of the Internal Revenue Code.

Compensation Committee Report

We have reviewed and discussed the foregoing Compensation Discussion and Analysis with management. Based on our review and discussion with management, we have recommended to the Board of Directors that the Compensation Discussion and Analysis be included in this proxy statement and in the Company's Annual Report on Form 10-K for the year ended December 31, 2008.

The Compensation Committee

William L. Hermann, Chairman
Steven K. Breeden
Harold I. Hackerman
Charles E. Moore, Jr.

EXECUTIVE COMPENSATION

The following table sets forth the compensation earned by or awarded to the Company's Chief Executive Officer, Chief Financial Officer, and the three most highly compensated other executive officers for 2008 (the "Named Executive Officers").

Summary Compensation Table

Named Executive Officer and principal position	Year	Salary	Bonus	Stock Awards (1)	Option Awards (2)	Changes in Pension Value & Nonqualified Deferred Compensation Earnings(3)	All Other Compensation (4)	Total
Robert A. Altieri	2008	$234,000	$ —	—	—	$ 7,774	$20,252	$262,026
President &	2007	225,000	—	—	—	7,278	18,037	250,315
Chief Executive Officer	2006	215,000	—	—	—	6,822	18,383	240,205
James M. Uveges	2008	163,800	—	—	—	—	20,191	183,991
Senior Vice President &	2007	157,500	—	—	—	—	19,445	176,945
Chief Financial Officer	2006	150,000	—	—	—	—	9,602	159,602
William D. Sherman	2008	142,800	—	—	—	968	7,252	151,020
Senior Vice President	2007	131,865	—	—	—	896	7,150	139,911
	2006	109,387	—	—	—	830	4,816	115,033
Gary M. Jewell	2008	133,750	33,438	—	—	10,068	9,982	187,237
Senior Vice President	2007	125,000	31,250	—	—	9,250	10,797	176,297
	2006	120,000	30,000	—	5,000	8,526	11,332	169,858
Lola B. Stokes	2008	122,200	—	—	—	1,232	6,947	130,380
Senior Vice President(5)	2007	117,500	—	—	—	1,149	6,787	124,364
	2006	57,961	—	—	—	1,072	3,420	61,453

(1) No stock awards were made in 2008, 2007, or 2006.

(2) All unexercised options to Named Executive Officers were fully vested at December 31, 2005.

(3) The pension plan was frozen effective December 31, 2004. No new participants entered the plan after December 2004.

(4) Amount includes 3% of Named Executive Officer's salary as a safe harbor contribution and 50% of the 401(K) contribution up to 6% of compensation as a matching contribution to the Bank's 401(K) plan, compensation attributed to the portion of the premium paid by the Bank for a group term life insurance policy for coverage in excess of $50,000 and personal use of a Company vehicle. None of the values of individual benefits and perquisites exceeded $25,000.

(5) Mrs. Stokes was rehired in June 2006. She was originally hired in July 2000 and resigned January 2005.

Outstanding Equity Awards At 2008 Fiscal Year End

The following table shows all outstanding equity awards held by Named Executive Officers as of December 31, 2008:

	Option Awards			
Name	Number of Securities Underlying Unexercised Options (#) Exercisable	Number of Securities Underlying Unexercised Options (#) Unexercisable	Option Exercise Price ($)	Option Expiration Date
Robert A. Altieri	6,300	—	$15.419	5/13/2009
	3,150	—	13.452	7/27/2010
	10,500	—	10.943	5/24/2011
	8,400	—	12.667	7/25/2012
	10,000	—	14.500	12/15/2015
James M. Uveges	5,000	—	14.850	6/6/2015
William D. Sherman	3,000	—	16.020	7/22/2014
	3,000	—	14.500	12/15/2015
Gary M. Jewell	6,300	—	15.419	5/13/2009
	3,150	—	13.452	7/27/2010
	1,650	—	12.667	7/25/2012
	5,000	—	16.020	7/22/2014
	5,000	—	14.500	12/15/2015
	5,000	1,667	17.160	12/31/2016
Lola B. Stokes	—	—	—	

Grants of Plan-Based Awards

The following table contains information concerning the grant of stock options under the 2007 Equity Plan and the 1998 Plan during the year ended December 31, 2008.

Name	Grant Date	Number of Securities Underlying Options	Exercise or Base Price of Option Awards ($1/sh)
Robert A. Altieri	—	—	$ —
James M Uveges	—	—	—
William D. Sherman	—	—	—
Gary M. Jewell	—	—	—
Lola B. Stokes	—	—	—

A total of 3,600 unrestricted shares without terms and conditions thereon were granted in 2008 and 2007 under the 2007 Equity Plan to directors. Stock options for 630 shares were granted to Mr. Francis Ryan in January 2007 under the 1998 Plan.

Option Exercises and Stock Vested

The following table shows exercises of stock by the Company's Named Executive Officers during the year ended December 31, 2008 and the value realized by them:

	Option Awards	
Name	Number of Shares Acquired on Exercise	Value Realized on Exercise
Robert A. Altieri	—	$ —
James M. Uveges	—	—
William D. Sherman	—	—
Gary M. Jewell	2,550	4,776
Lola B. Stokes	—	—

Employment Agreements

On February 13, 2009, as part of the CPP, the Company entered into a Letter Agreement, and the related Securities Purchase Agreement - Standard Terms (collectively, the "Purchase Agreement"), with the Treasury Department, pursuant to which the Company issued (i) 9,201 shares of Fixed Rate Cumulative Perpetual Preferred Stock, Series A, liquidation preference $1,000 per share ("Series A Preferred Stock"), and (ii) a warrant to purchase 205,379 shares of the Company's common stock, par value $1.00 per share.

Under the terms of the EESA, in order for the Company to participate in the CPP each SEO of the Company and the Bank signed a waiver which voluntarily waived any claim against the United States or the Company for any changes to his or her compensation or benefits that are required to comply with the regulation issued by the Treasury Department as published in the Federal Register on October 20, 2008. Each SEO Employment Agreement was amended to: (a) incorporate all provisions required for compliance with the executive compensation provisions and regulations of the EESA (the "EESA Executive Compensation Provisions"); and (b) modify such provisions of such SEO Employment Agreements which are inconsistent with or in violation of the EESA Executive Compensation Provisions and the regulations promulgated thereunder, to the extent necessary to comply with the EESA Executive Compensation Provisions and the regulations promulgated thereunder.

Without limiting the generality of the foregoing, the provisions of Section 6 of each SEO Employment Agreement were modified to provide that anything contained therein to the contrary notwithstanding, the Company or the Bank, as applicable, or any “acquiring institution” (as such term is used in each of the SEO Employment Agreements) would not be required to make any payment or provide any benefit to the SEO which would constitute a “golden parachute payment” in violation of Section 111(b)(2)(C) of EESA and the regulations promulgated thereunder. The amendments to the SEO Employment Agreements will cease to be of any force or effect if and when the Treasury Department ceases to hold an equity or debt position in the Company acquired under the CPP and the Company and the Bank are no longer required to comply with the relevant provisions of the EESA and the regulations promulgated thereunder.

On August 1, 2007, the Company and the Bank (which for purposes of such employment agreement are referred to as the “Bank”) entered into an employment agreement with Robert A. Altieri, President and Chief Executive Officer. The term of the agreement began on August 1, 2007 and is effective for three years. As part of the agreement, the Bank will pay Mr. Altieri a minimum annual base salary of $234,000. At the end of each calendar year, Mr. Altieri may receive a cash bonus not to exceed 40% of his base salary. The amount of the bonus will be determined by the Compensation Committee based on defined goals and objectives established by the foresaid committee and the Board of Directors. In addition, Mr. Altieri is entitled to participate in all employee benefit plans and arrangements as offered by the Bank to all employees and officers and is entitled to a Bank-owned car. In the event that the Bank terminates Mr. Altieri without cause, he will be entitled to receive his then current monthly salary for up to twenty-four months. In the case of termination as a result of any sale of the Bank, Mr. Altieri will receive a severance package to include: (i) three years of his current base salary; (ii) continuation for a period of eighteen months of all medical and long-term disability insurance in amounts and subject to the provisions in effect as of the date of sale and for a period of six months thereafter, said insurance, if available at the same cost, will be provided to Mr. Altieri and, if not available at the same cost, the Bank shall pay monthly an amount of money equal to the monthly premium paid by the Bank for the insurance in the eighteen month after Mr. Altieri’s termination; and (iii) at Mr. Altieri’s option, he can purchase the Bank-owned car assigned to him at no cost to him except for transfer costs. Additional provisions include a non-compete clause which for two years following the termination of Mr. Altieri’s employment without cause, prohibits Mr. Altieri from soliciting customers of the Bank and within an area of thirty-five miles from the Bank’s then main office, Mr. Altieri will not accept employment with a bank, thrift or credit union as a President, senior officer or in a managerial capacity. Mr. Altieri is also required to develop a plan of succession.

On June 13, 2007, the Bank entered into an employment agreement with Gary M. Jewell, Senior Vice President, Electronic Banking. The term of the agreement began on June 8, 2007 and is effective for three years. As part of the agreement, the Bank will pay Mr. Jewell a minimum annual base salary of $133,750. At the end of each calendar year, Mr. Jewell shall receive a cash bonus of 25% of his base salary provided the annual Point of Sale revenue received by the Bank during the calendar year exceeds One Million Dollars ($1,000,000). In addition, Mr. Jewell is entitled to participate in all employee benefit plans and arrangements as offered by the Bank to all employees and officers and is entitled to a Bank-owned car. In the event that the Bank terminates Mr. Jewell without cause, he will be entitled to receive his then current monthly salary for up to twenty-four months and at the expiration of said twenty-four months, he shall receive for the next six consecutive months, 65% of the monthly salary being received at the time of his termination. In the case of termination as a result of any sale of the Bank, Mr. Jewell will receive a severance package to include: (i) three years of his current base salary (ii) continuation of all medical and long-term disability insurance in amounts and subject to the provisions in effect as of the date of sale. After the three year term, Mr. Jewell is entitled for an additional three years to receive 65% of his base salary received at the time of sale and medical and long-term disability insurance in amounts and subject to the provisions in effect as of the date of sale. Additional provisions include a non-compete clause which for one year following the termination of employment, prohibits Mr. Jewell from soliciting, servicing, or assisting in Point of Sale transactions originated by any company whose Point of Sale transactions were being handled by the Bank at the time his employment terminated. Mr. Jewell is also required to train other persons designated by the Bank in all aspects of electronic banking.

On October 16, 2007, the Bank entered into an employment agreement with Lola B. Stokes, Senior Vice President and Compliance Officer. The term of the agreement began on June 1, 2007 and is effective for two years. As part of the agreement, the Bank will pay Ms. Stokes a minimum annual base salary of $122,200. At the end of each calendar year, Ms. Stokes may receive a cash bonus not to exceed 10% of her base salary. The amount of the bonus will be determined by the Compensation Committee based on defined goals and objectives established by the foresaid committee and the Board of Directors. In addition, Ms. Stokes is entitled to participate in all employee benefit plans and arrangements as offered by the Bank to all employees and officers. In the event that the Bank terminates Ms. Stokes without cause, she will be entitled to receive her then current monthly salary for up to twelve months. In the case of termination as a result of any sale of the Bank, Ms. Stokes will receive a severance package to include: (i) one year of her current base salary (ii) continuation for a period of one year of all medical and long-term disability insurance in amounts and subject to the provisions in effect as of the date of sale. Additional provisions include a non-compete clause which for one year following the termination of employment without cause, prohibits Ms. Stokes from soliciting customers of the Bank. Ms. Stokes is also required to develop a plan of succession.

On November 8, 2007, the Company and the Bank (which for purposes of such employment agreement are referred to as the "Bank") entered into an employment agreement with James M. Uveges, Senior Vice President and Chief Financial Officer. The term of the agreement began on November 8, 2007 and is effective for two years. As part of the agreement, the Bank will pay Mr. Uveges a minimum annual base salary of $163,800. At the end of each calendar year, Mr. Uveges may receive a cash bonus not to exceed 25% of his base salary. The amount of the bonus will be determined by the Compensation Committee based on defined goals and objectives established by the Compensation Committee and the Board of Directors. In addition, Mr. Uveges is entitled to participate in all employee benefit plans and arrangements as offered by the Bank to all employees and officers and is entitled to a Bank-owned car. In the event that the Bank terminates Mr. Uveges without cause, he will be entitled to receive his then current monthly salary for up to twelve months. In the case of termination as a result of any sale of the Bank, Mr. Uveges will receive a severance package to include: (i) eighteen months of his current base salary (ii) continuation for a period of eighteen months of all medical and long-term disability insurance in amounts and subject to the provisions in effect as of the date of sale (iii) at Mr. Uveges' option, he can purchase the Bank-owned car assigned to him at no cost to him except for transfer costs. Additional provisions include a non-compete clause which for eighteen months following the termination of employment without cause, prohibits Mr. Uveges from soliciting customers of the Bank. Mr. Uveges is also required to develop a plan of succession.

The employment agreements with Messrs. Altieri, Jewell, and Uveges and Ms. Stokes are the SEO Employment Agreements referred to above under the caption Effect of Emergency Stabilization Act of 2008 and each such SEO Employment Agreement has been amended as described above.

Pension Benefits and Perquisites

Effective December 31, 2004, the Company froze its defined benefit plan. Participant benefits stopped accruing as of the date of the freeze. No new participants entered the defined benefit plan after December 31, 2004. Assets of the plan are held in a trust fund managed by an insurance company.

As of December 31, 2008, the following table shows the present value of accumulated benefits under the Company's defined benefit plan for each Named Executive Officer:

Name	Plan Name	Number of Years of Credited Service	Present Value of Accumulated Benefits
Robert A. Altieri	Pension Plan	13	$131,685
James M. Uveges(2)	Pension Plan	N/A	—
William D. Sherman	Pension Plan	2	14,971
Gary M. Jewell	Pension Plan	9	148,378
Lola B. Stokes	Pension Plan	4	20,187

(2) Mr. Uveges was hired subsequent to the Plan freeze.

The Company has a contributory thrift plan ("Thrift Plan") qualifying under Section 401(K) of the Internal Revenue Code. Employees with three months of service are eligible for participation in the Thrift Plan. After the participant has been employed at the Company for one year, the Company contributes 3% of the employee's salary to the Thrift Plan for the employee's benefit. Also, the Company matches 50% of the employee's 401(K) contribution up to 6% of the employee's compensation. All Named Executive Officers participated in the Thrift Plan in 2008 and received matching funds. Such amounts attributable to each Named Executive Officer are included in all other compensation.

COMPENSATION COMMITTEE INTERLOCKS AND INSIDER PARTICIPATION

During 2008, Messrs. Herman, Breeden, Hackerman and Moore served as members of the Compensation Committee. In 2008, the Company and the Bank had banking and other relationships, in the ordinary course of business, with a number of its directors and companies associated with its directors. The Company purchased insurance through its broker, Riggs, Counselman, Michaels & Downes, Inc., of which Mr. Counselman is President and Chief Executive Officer. The insurance coverage purchased was made on substantially the same terms, as those prevailing at the time, for comparable transactions with others. Management believes the terms of the insurance coverage obtained through Riggs, Counselman, Michaels & Downes, Inc. were at least as favorable to the Company as could have been obtained elsewhere.

Outstanding loans exist to Robert J. Aumiller, David P. Hessler, Charles E. Moore, Jr., John Paul Rogers and William C. Rogers, III and their related companies which were made on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with others not considered outsiders, and did not involve more than the normal risk of collectibility or present other unfavorable features.

CERTAIN TRANSACTIONS AND RELATIONSHIPS

During the past year the Company, through the Bank, has had banking transactions in the ordinary course of its business with: (i) its directors and nominees for directors; (ii) its executive officers; (iii) its 5% or greater shareholders; (iv) members of the immediate family of its directors, nominees for directors or executive officers and 5% shareholders; and (v) the associates of such persons on substantially the same terms, including interest rates, collateral, and repayment terms on loans, as those prevailing at the same time for comparable transactions with others. The extensions of credit by the Company, through the Bank, to these persons have not had and do not currently involve more than the normal risk of collectibility or present other unfavorable features. At December 31, 2008, the balance of loans outstanding to directors, executive officers, owners of 5% or more of the outstanding Common Stock, and their associates, including loans guaranteed by such persons, aggregated $2,788,468 which represented approximately 10.2% of the Company's equity capital accounts.

William C. Rogers, III, a director of both the Company and the Bank, is a partner of the law firm of Rogers, Moore and Rogers, which performs legal services for the Company, the Bank, and Bank subsidiaries (Carrollton Financial Services, Inc., Carrollton Mortgage Services, Inc., and Carrollton Community Development Corporation). Management believes that the terms of these transactions, which totaled approximately $381,000 in 2008, were at least as favorable to the Company as could have been obtained elsewhere.

Albert R. Counselman, a director of both the Company and the Bank, is President and Chief Executive Officer of Riggs, Counselman, Michaels & Downes, Inc., an insurance brokerage firm through which the Company, the Bank, and Bank subsidiaries place various insurance policies. The Company and the Bank paid total premiums for insurance policies placed by Riggs, Counselman, Michaels & Downes, Inc. in 2008 of approximately $214,000. Management believes that the terms of these transactions were at least as favorable to the Company as could have been obtained elsewhere.

Robert J. Aumiller, a director of both the Company and the Bank, is Executive Vice President of MacKenzie Real Estate Services, a brokerage and real estate development firm, through which the Company and the Bank paid approximately $2,000 in 2008 for appraisal, construction, brokerage and property management services provided by MacKenzie Commercial Real Estate Services. Management believes these terms were as favorable as could have been obtained elsewhere.

We use the following guidelines to determine the impact of a credit relationship on a director's independence. We consider extensions of credit which comply with Federal Reserve Regulation O to be consistent with director independence. In other words, we do not consider normal, arm's−length credit relationships entered into in the ordinary course of business to negate a director's independence.

Regulation O requires such loans to be made on substantially the same terms, including interest rates and collateral, and following credit−underwriting procedures that are no less stringent than those prevailing at the time for comparable transactions by the Company with other persons not related to the lender. Such loans also may not involve more than the normal risk of repayment or present other unfavorable features. Additionally, no event of default may have occurred (that is, such loans are not disclosed as non−accrual, past due, restructured, or potential problems). The Audit Committee must review and approve any credit to a director or his or her related interests and submit such transaction to the full Board of Directors for approval.

In addition, we do not consider as independent any director who is also an executive officer of a company to which we have extended credit unless such credit meets the substantive requirements of Regulation O. We also do not consider independent any director who is an executive officer of a company that makes payments to, or receives payments from, the Company for property or services in an amount which, in any fiscal year, is greater than 2% of such director's company's consolidated gross revenues.

AUDIT COMMITTEE REPORT

The Audit Committee has adopted a written charter which was included as part of the definitive proxy statement delivered to shareholders with respect to the 2004 Annual Meeting and a copy of which, can be found on the Company's website at www.carrolltonbank.com. The members of the Audit Committee are "independent" as such term is defined in Rule 4200(a)(15) of the NASDAQ Stock Market, Inc. listing standards and applicable SEC rules. The Audit Committee has (1) reviewed and discussed the Company's audited financial statements with management and representatives of Rowles & Company, LLP, the Company's independent registered public accounting firm; (2) discussed with Rowles & Company, LLP all matters required to be discussed by Statement on Auditing Standards No. 61, as amended by Statement on Auditing Standards No. 90 (Communication with Audit Committees); and (3) reviewed the written disclosures required by Independence Standards Board Standard No. 1, which were received from the Company's independent registered public accounting firm, and has discussed the Company's independent registered public accounting firm's independence with them. The Audit Committee has reviewed the fees of the Independent Registered Accounting Firm for non-audit services and believes that such fees are compatible with the independence of the Company's independent registered accounting firm.

Based on these reviews and discussions, the Audit Committee recommended to the Board of Directors that the audited financial statements be included in the Company's Annual Report on Form 10-K for the year ended December 31, 2008.

Audit Committee:

Charles E. Moore, Jr., Chairman
Harold I. Hackerman
William L. Hermann
David P. Hessler
Howard S. Klein

SECTION 16(a) BENEFICIAL OWNERSHIP REPORTING COMPLIANCE

Under the securities laws of the United States, the Company's directors, executive officers and any persons holding more than 10% of the Common Stock of the Company are required to report their ownership of the Common Stock and any changes in that ownership to the SEC. Specific due dates for these reports have been established and pursuant to applicable rules, the Company is required to report in its proxy statement any failure to file by these dates. Based on the Company's review of copies of such reports that such persons have filed with the SEC, the Company believes that all required reports of its directors and executive officers have been timely filed with the SEC during 2008.

PROPOSAL 2: RATIFICATION OF THE APPOINTMENT OF THE INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors has ratified and affirmed the Audit Committee's appointment of the accounting firm of Rowles & Company, LLP, to serve as independent registered public accounting firm for the Company for 2009 subject to ratification by the shareholders of the Company. Rowles & Company, LLP has served as independent auditors for the Company since 1955. No qualified opinions have been issued during such engagement. A representative of Rowles & Company, LLP will be present at the 2009 Annual Meeting of Shareholders and will be given the opportunity to make a statement, if he or she so desires, and to respond to appropriate questions.

Audit Fees and Services

	2008	2007
Audit Fees	$ 79,215	$ 94,061
Audit – Related Fees	10,375	10,500
Tax Fees	10,904	11,917
All Other Fees	—	7,780
Total	$100,494	$124,258

Audit services of Rowles & Company, LLP for 2008 and 2007 consisted of professional services rendered for the audit of the Company's annual consolidated financial statements included in the Company's Form 10-K and the review of the consolidated financial statements included in the Company's Quarterly Reports on Forms 10-Q. "Audit- Related Fees" incurred in 2008 and 2007 include charges related to the Company's defined benefit plan audit and the Company's 401(K) plan audit. "Tax Fees" in 2008 and 2007 represent income tax return preparation and advice. All other fees in 2007 represented review of documentation of key controls for compliance with Sarbanes-Oxley Act of 2002.

The Audit Committee's policy is to pre-approve all audit and permitted non-audit services other than de minimis non-audit services as defined in Section 10A(i)(1) of the Exchange Act, which will be approved prior to the completion of the independent auditor's report. The Audit Committee has reviewed summaries of the services provided and the related fees and has determined that the provision of non-audit services is compatible with maintaining the independence of Rowles & Company, LLP.

Financial Information Systems Design and Implementation Fee

During the year ended December 31, 2008, Rowles & Company, LLP did not render to the Company any professional services with regard to financial information systems design and implementation described in paragraph (c)(4)(ii) of Rule 2-01 of Regulation S-X.

A majority of the votes cast at the annual meeting is required for approval of the ratification of the appointment of Rowles & Company, LLP as the Company's independent registered public accounting firm for 2009 as set forth in this Proposal 2. Abstentions and broker non-votes, if any, will have no effect on the vote for this Proposal 2.

The Board of Directors unanimously recommends a vote "FOR" ratification of Rowles & Company, LLP, as the Company's independent registered public accounting firm for 2009.

PROPOSAL 3: ADVISORY VOTE ON EXECUTIVE COMPENSATION

RESOLVED, that the shareholders of the Company approve the compensation of the Company's executives as described in the Summary Compensation Table as well as in the Compensation Discussion and Analysis and the other executive compensation tables and related discussions contained in the Proxy Statement for the 2009 Annual Meeting of Shareholders.

We believe that our compensation policies and procedures are competitive, are focused on pay for performance principles and are strongly aligned with the long−term interests of our shareholders. We also believe that both the Company and shareholders benefit from responsive corporate governance policies and constructive and consistent dialogue. The resolution described above, commonly known as a "say on pay" proposal, gives you as a shareholder the opportunity to endorse or not endorse the compensation we pay to our named executive officers by voting to approve or not approve such compensation as described in this Proxy Statement.

We encourage you to closely review our Compensation Discussion and Analysis and the tabular disclosure which follows it. We organized the Compensation Discussion and Analysis to discuss each element of compensation, beginning with direct, short−term compensation (base salary) and ending with indirect, long−term compensation (retirement benefits) and termination benefits. In that section, we also discuss our policies and other factors, such as financial and regulatory constraints, which affect our decisions or those of our Compensation Committee.

Generally, in this Proxy Statement we are required to disclose information for our 5 most highly−compensated officers for the past 3 years. Therefore, most of our tabular disclosure is backwards−looking. When possible, we have discussed our plans for changes to compensation practices for the current year and beyond. Importantly, recent legislation and new regulations will greatly affect our compensation practices going forward. We discuss these in the Compensation Discussion and Analysis Section under the captions, "Effect of the Emergency Economic Stabilization Act of 2008," "Effect of Treasury Department Guidelines Announced February 4, 2009," and "Effect of the America Reinvestment and Recovery Act of 2009" which appear at pages 13 to 18 of this Proxy Statement. These laws apply to us because we sold preferred stock to the United States Treasury in the first quarter of 2009 under its Capital Purchase Program. Unfortunately, key details of these new laws will be determined only after the Treasury Department and the SEC issue new regulations. As a result, we cannot reliably predict what changes we will be required to make to our compensation programs. In the Compensation Discussion and Analysis section, we have attempted to discuss these as best we could. We will fully comply with all applicable requirements as soon as the details of such requirements are known by us.

Also, in many cases, we are required to disclose in the executive compensation tables accounting or other non−cash estimates of future compensation. Because of this, we encourage you to read the footnotes and narratives which accompany each table in order to understand any non−cash items.

No cash bonus was paid to our CEO or any of our other SEOs for 2007 or 2008, except for the payment of a cash bonus in 2007 and 2008 to one SEO based on the Company's Point of Sale revenue which has actually been paid to and received by the Company.

Currently, each of the Company's SEOs annual compensation is less than $500,000. The Company has also instituted a six month deferral of salary increases for all SEOs in 2009.

We use stock options and restricted stock instead as long−term incentives because we wanted to enhance the alignment between shareholder interest and executive compensation. There were no grants of stock or options to our CEO or any of our other SEOs in 2007 or 2008.

As evidence of the greater alignment with shareholders' interest mentioned above, the value of the incentive stock options previously granted to our SEOs has declined as our stock price declined.

Under the ARRA, your vote is advisory and will not be binding upon our Board of Directors. However, the Compensation Committee will take into account the outcome of the vote when considering future executive compensation arrangements.

A majority of the votes cast at the annual meeting is required for approval of this proposal. Abstentions and broker non-votes, if any, will have no effect on the vote for this Proposal 3.

The Board of Directors unanimously recommends a vote "FOR" the approval of the compensation of the Company's executives as described in the Summary Compensation Table as well as in the Compensation Discussion and Analysis and the other executive compensation tables and related discussions contained in the Proxy Statement for the 2009 Annual Meeting of Shareholders.

SHAREHOLDER PROPOSALS FOR THE 2010 ANNUAL MEETING OF SHAREHOLDERS

Proposals of shareholders to be presented at the 2010 Annual Meeting of the Company's shareholders must be received at the Company's principal executive offices prior to December 11, 2009 in order to be included in the proxy statement for such meeting. In order to curtail controversy as to compliance with this requirement, shareholders are urged to submit proposals to the Secretary of the Company by Certified Mail – Return Receipt Requested.

Delivery of Documents to Shareholders Sharing an Address

The SEC has adopted rules that allow us to deliver a single annual report, proxy statement, proxy statement combined with a prospectus, or any information statement to any household at which two or more shareholders reside who share the same last name or whom we believe to be members of the same family. This is known as "householding."

If you share the same last name and address with one or more shareholders, from now on, unless we receive contrary instructions from you (or from one of these other shareholders), you and all other shareholders who have your last name and live at the same home address will receive only one copy of any of our annual report, proxy statement for our Annual Meeting of Shareholders, proxy statement we file and deliver in connection with any other meeting of shareholders, proxy statement combined with a prospectus or information statement. We will include with the household materials for our annual meetings, or any other shareholders' meeting, a separate proxy card for each registered shareholder who shares your last name and lives at your home address.

If you do not wish to participate in the householding program, please contact our transfer agent, American Stock Transfer & Trust Company, at 1-800-937-5449 to "opt-out" or revoke your consent. If you "opt-out" or revoke your consent to householding, each primary account holder residing at your address will receive individual copies of the Company's proxy statement, annual report and other future shareholder mailings.

Most banks and brokers are delivering only one copy of the annual report and proxy statement to consenting street-name stockholders (you own shares in the name of a bank, broker or other holder of record on the books of our transfer agent) who share the same address. Those street-name shareholders who wish to receive separate copies may do so by contacting their bank or broker or other holder of record.

Electronic Access to Future Documents

If you would like to receive future shareholder communications over the Internet exclusively, and no longer receive any material by mail please visit http://amstock.com. Click on Shareholder Account Access to enroll. Please enter your account number and tax identification number to log in, then select Receive Company Mailings via E-Mail and provide your email address.

To View the Annual Report and Proxy Materials Online go to: www.carrolltonbank.com

OTHER MATTERS

The management of the Company knows of no matters to be presented for action at the meeting other than those mentioned above; however, if any other matters properly come before the 2009 Annual Meeting of Shareholders, it is intended that the persons named in the accompanying proxy will vote on such other matters in accordance with their judgment of the best interest of the Company.