

LETTER TO OUR SHAREHOLDERS

Dear Shareholders:

This year marks the second consecutive year of record core earnings for our Company. On behalf of the Directors, Officers and all of our associates, we are proud to present our 2006 annual results and to share highlights with our valued shareholders.

In 2006, our Company surpassed 2005 results by achieving both record revenues and core earnings. The year was challenging and marked by an after tax charge of \$1.2 million relating to a well publicized check kiting scheme perpetrated by a commercial depository customer; nevertheless, the Company was able to overcome the one time charge and post net income of \$2,585,000 or \$0.90 per diluted share compared to \$2,458,000 or \$0.87 per diluted share in 2005.

For most of the second half of 2006, the interest rate environment was characterized by an inverted yield curve (long term rates are lower than short term rates). During the first quarter of 2006, the Company restructured \$35.0 million of fixed rate (6.84%) long term Federal Home Loan Bank advances into short term borrowings. This decision reduced our exposure to future changes in interest rates by providing greater flexibility in our interest rate planning process. We incurred a prepayment penalty of \$2.3 million, which was substantially offset by the gain of approximately \$2.2 million from the sale of equity securities.

This restructuring and the growth in loans and investment securities enabled the Company to increase its net interest margin from 3.89% in 2005 to 4.57% in 2006. The Company expects to see the net interest margin decline due to continued pressure in 2007. To offset lower margins, the Company will focus on growth in commercial and residential lending while continuing to maintain credit quality. Net chargeoffs to average loans for 2006 was 0.08% compared to 0.06% in 2005.

2007 will bring a renewed focus on improving the deposit mix by focusing on generating lower cost accounts. As a percentage of total deposits, the Company is in the upper percentile of our peer groups as it relates to non-interest bearing deposits. The Company ended 2006 with non-interest bearing deposits as a percentage of total deposits of 18.0% compared to 24.7% in 2005. This is a challenging part of our business. However, it is one that will require a steadfast effort to grow, aiding the Company to maintain and improve its net interest margin. In the first half of 2007, the Bank will introduce remote deposit capture which will help reduce the age long obstacle that community banks face of not having a branch within close proximity of a commercial client. By implementing remote deposit capture, a commercial customer can make a deposit from their office without entering a branch. We expect this product to improve efficiencies and to enhance the Company's product generation abilities.

In 2007, the Bank will open its eleventh full service branch facility in Cockeysville, Maryland located at the corner of Scott Adam and York Roads. This branch will be a full service branch housing the Company's Financial Services subsidiary, Carrollton Financial Services, Inc. as well as a commercial lender to service the Cockeysville/Hunt Valley area of Baltimore County.

The Company continues to methodically and meticulously grow its loan portfolio, with commercial real estate and business loans comprising almost 78% of the Company's total loan portfolio. Our ability to continue to grow our loan portfolio in an extremely competitive marketplace is directly attributable to the Company's unwavering commitment to become a strong commercial bank supporting the Baltimore business community.

In 2006, the Company saw a decrease in total assets, due primarily to the utilization of cash and cash equivalents toward the pay down of borrowings. The Company decreased its cash and cash equivalent position by \$25.5 million to pay down Federal Home Loan Bank advances of \$18.0 million and to fund loan growth. The Company experienced yet another year of solid loan growth predominantly in commercial real estate and business lending. Overall, gross loans, excluding loans held for sale, grew \$12.0 million or 4.9% over 2005. In particular, commercial real estate and business loans increased \$9.5 million to \$202.9 million compared to 2005. The Company's continued efforts to focus on commercial lending will have a positive impact on net interest margins; however, the spreads once seen in commercial loans are reducing.

Carrollton Bancorp continues to be a well capitalized financial institution. The Company's year end capital and Tier-1 risk based capital ratios were 13.20% and 11.92%, respectively. Each measure continues to substantially exceed the federal regulatory standards for well capitalized financial services institutions. As part of our overall capital management, we have increased dividends 12.5% in 2006 and 6.6% for 2007.

Thank you for your investment in Carrollton Bancorp and your continued support. Finally, I want to thank our associates for the hard work and dedication to providing extraordinary service to our customers. This commitment is the foundation of this institution and will remain our strength for many years to come.

Most Sincerely,



Albert R. Counselman
Chairman of the Board



Robert A. Altieri
President and Chief Executive Officer

ITEM 6: SELECTED FINANCIAL DATA

	2006	2005	2004	2003	2002
CONSOLIDATED INCOME STATEMENT DATA:					
Interest income	\$ 23,127,504	\$ 19,071,379	\$ 15,500,323	\$ 15,935,691	\$ 18,985,364
Interest expense	8,737,450	7,375,083	5,321,622	6,639,734	8,692,320
Net interest income	14,390,054	11,696,296	10,178,701	9,295,957	10,293,044
Provision for loan losses	—	—	—	243,000	526,000
Net interest income after provision for loan losses	14,390,054	11,696,296	10,178,701	9,052,957	9,767,044
Noninterest income	8,898,996	10,718,636	8,781,151	8,268,612	7,534,802
Noninterest expenses	19,381,003	18,634,124	17,751,000	16,058,355	14,536,958
Income before income taxes	3,908,047	3,780,808	1,208,852	1,263,214	2,764,888
Income taxes	1,323,268	1,322,371	320,488	338,500	847,630
Net income	\$ 2,584,779	\$ 2,458,437	\$ 888,364	\$ 924,714	\$ 1,917,258
CONSOLIDATED BALANCE SHEET DATA, AT YEAR END					
Assets	\$349,824,752	\$360,467,146	\$319,123,132	\$302,409,975	\$324,221,615
Gross loans	260,001,314	247,943,073	219,726,294	199,296,561	205,220,126
Deposits	277,903,801	271,626,503	225,846,145	207,056,100	230,264,108
Shareholders' equity	34,711,378	34,640,165	34,215,280	34,124,882	33,691,079
PER SHARE DATA:					
Number of shares of Common Stock outstanding, at year-end	2,806,705	2,809,698	2,834,823	2,828,078	2,821,757
Net income:					
Basic	\$ 0.92	\$ 0.87	\$ 0.31	\$ 0.33	\$ 0.68
Diluted	0.90	0.87	0.31	0.32	0.68
Cash dividends declared	0.45	0.40	0.38	0.36	0.34
Book value, at year end	12.37	12.33	12.07	12.07	11.94
Performance and capital ratios:					
Return on average assets	0.75%	0.72%	0.29%	0.29%	0.57%
Return on average shareholders' equity	7.55%	7.12%	2.61%	2.71%	5.70%
Net interest margin (a)	4.57%	3.89%	3.81%	3.36%	3.47%
Average shareholders' equity to average total assets	9.91%	10.13%	11.11%	10.83%	9.99%
Year-end capital to year-end risk-weighted assets:					
Tier 1	11.92%	11.63%	11.52%	13.75%	13.57%
Total	13.20%	13.51%	12.74%	15.51%	15.07%
Year-end Tier 1 leverage ratio	9.74%	8.96%	9.41%	10.35%	9.54%
Cash dividends declared to net income	48.98%	45.97%	121.17%	109.96%	50.80%
ASSET QUALITY RATIOS:					
Allowance for loan losses, at year-end to:					
Gross loans	1.20%	1.35%	1.59%	1.83%	1.74%
Nonperforming, restructured and past-due loans	54.93%	209.50%	132.05%	151.37%	111.68%
Net charge-offs to average gross loans	0.08%	0.06%	0.08%	0.09%	0.13%
Nonperforming assets as a percent of period-end gross loans and foreclosed real estate	2.19%	0.64%	1.20%	1.26%	1.67%

(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.

CARROLLTON BANCORP
344 North Charles Street, Suite 300
Baltimore, Maryland 21201

NOTICE OF ANNUAL MEETING OF SHAREHOLDERS
TO BE HELD ON MAY 15, 2007

TO THE SHAREHOLDERS OF CARROLLTON BANCORP:

The Annual Meeting of Shareholders of Carrollton Bancorp, a Maryland corporation (the "Company"), will be held at 344 North Charles Street, Baltimore, Maryland on May 15, 2007 at 10:00 a.m., prevailing local time, for the purpose of considering and acting upon:

1. The election of four directors for a three-year term ending in 2010, one director for a two-year term ending in 2009 and one director for a one-year term ending in 2008, or, in each case, until their respective successors are duly elected and qualified.
2. The approval of the 2007 Equity Plan.
3. 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, 2007.
4. Any other matters that may properly come before the Annual Meeting or any adjournment thereof.

The close of business on April 2, 2007, has been fixed by the Board of Directors 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, 2006.

PLEASE SIGN, DATE AND MAIL THE ACCOMPANYING PROXY CARD IN THE ENCLOSED, SELF-ADDRESSED, STAMPED ENVELOPE, AS DIRECTED ON THE PROXY CARD IN ORDER THAT YOUR STOCK MAY BE VOTED. YOU MAY WITHDRAW YOUR PROXY AT THE MEETING SHOULD YOU BE PRESENT AND DESIRE TO VOTE YOUR SHARES IN PERSON. YOUR COOPERATION IS RESPECTFULLY REQUESTED.

By Order of the Board of Directors



Allyson Cwiek
Secretary

Baltimore, Maryland
April 13, 2007

CARRROLLTON BANCORP, INC.
PROXY STATEMENT

Table of Contents

SOLICITATION, VOTING, AND REVOCATION OF PROXIES	5
PROPOSAL I: ELECTION OF DIRECTORS	6
CORPORATE GOVERNANCE	8
DIRECTOR COMPENSATION	9
SECURITY OWNERSHIP OF DIRECTORS AND EXECUTIVE OFFICERS	11
CERTAIN BENEFICIAL OWNERS	12
COMPENSATION DISCUSSION AND ANALYSIS	13
COMPENSATION COMMITTEE REPORT	15
EXECUTIVE COMPENSATION	16
COMPENSATION COMMITTEE INTERLOCKS AND INSIDER PARTICIPATION	19
CERTAIN TRANSACTIONS AND RELATIONSHIPS	19
AUDIT COMMITTEE REPORT	19
SECTION 16(a) BENEFICIAL OWNERSHIP REPORTING COMPLIANCE	20
PROPOSAL II: APPROVAL OF THE 2007 EQUITY PLAN	20
PROPOSAL III: RATIFICATION OF APPOINTMENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM	24
SHAREHOLDER PROPOSALS FOR THE 2008 ANNUAL MEETING	25
OTHER MATTERS	25
APPENDIX A: 2007 EQUITY PLAN	

CARROLLTON BANCORP
344 North Charles Street, Suite 300
Baltimore, Maryland 21201

PROXY STATEMENT
ANNUAL MEETING OF SHAREHOLDERS

MAY 15, 2007

SOLICITATION VOTING AND REVOCATION OF PROXIES

This Proxy Statement (the "Proxy Statement") is furnished on or about April 13, 2007 to the shareholders of Carrollton Bancorp (the "Company") in connection with the solicitation of proxies by the Board of Directors of the Company to be voted at the Annual Meeting of Shareholders to be held on May 15, 2007 (the "Annual Meeting"), and any adjournments thereof. Our principal executive offices are located at 344 North Charles Street, Baltimore, Maryland 21201.

The Board of Directors has selected Harold I. Hackerman, William L. Hermann 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 giving written notice of revocation to the Company, by executing and delivering a substitute proxy to the Company, or by attending the Annual Meeting and voting in person. If no instructions are specified in the proxy, it is the intention of the persons named therein to vote **FOR** the election of the nominees named herein as directors of the Company, **FOR** the adoption of the 2007 Equity Plan and **FOR** the ratification of Rowles and Company, LLP as the independent registered public accounting firm to audit the financial statements of the Company for 2007.

Shareholders of the Company are requested to complete, date and sign the accompanying proxy card and return it promptly to the Company in the enclosed envelope. If a proxy card is properly executed and returned in time for voting, the shares represented thereby will be voted as indicated thereon.

The Company does not know of any matter to be presented at the Annual Meeting except as described herein. If any other matters are properly brought before the Annual Meeting, the persons named in the enclosed proxy card intend to vote the proxies granted to them according to their best judgment.

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 Securities and Exchange Commission ("SEC") that permit us to deliver one set of the proxy materials and annual report 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.

A separate notice of our intentions to use the householding rules is included with this mailing. Please note that if you own shares of the Company's common stock through a nominee (such as bank or broker), information regarding householding should be forwarded to you by the nominee.

VOTING PROCEDURES

Generally, each proposal submitted to the Company shareholders for a vote is deemed approved if a majority of the votes cast by the shareholders present, in person or by proxy, at a meeting at which a quorum is present, are in favor of the proposal. The presence of a majority, in person or by proxy, of shareholders entitled to cast votes at the meeting constitutes a quorum. A shareholder is entitled to one vote for each share owned. 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.

Shareholder votes are tabulated by the Company's Registrar and Transfer Agent. Proxies received by the Company, if the proxy card granting such proxy is properly executed and delivered, will be voted in accordance with the voting specifications made on such proxy. Proxies received by the Company on which no voting specification has been made by the shareholder will be voted "for" all items discussed in the Proxy Statement, in the manner stated on the proxy card. Shareholders who execute and deliver proxy cards retain the right to revoke them by notice delivered to the Company Secretary at any time before such proxies are voted.

The vote of a plurality of all of the votes cast at a meeting at which a quorum is present is necessary for the election of a director. For purposes of the election of directors, abstentions and broker non-votes will not be counted as votes cast and will have no effect on the result of the vote, although they will count toward the presence of a quorum.

A copy of the Annual Report on Form 10-K for the year ended December 31, 2006, 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 upon writing Allyson Cwiek, Secretary, at Carrollton Bancorp, 344 North Charles, Suite 300, Baltimore, Maryland 21201. 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 "Insider Transactions SEC Filings" – "SEC Filings".

Shareholders whose shares are held in a brokerage firm or bank and who share the same address may receive only one Annual Report on Form 10-K and Proxy Statement, unless the shareholder has provided 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 shareholders's brokerage firms or banks or contact Ms. Cwiek at the above address or by phone at 410.536.7326 or 800.222.6566.

SUBMISSION OF MATTERS TO A VOTE OF SHAREHOLDERS

There have been no matters submitted to a vote of the Company's shareholders since its 2006 Annual Shareholders' Meeting held on April 18, 2006.

VOTING SECURITIES

The close of business on April 2, 2007 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.

On March 28, 2007, the Company had outstanding 2,821,195 shares of Common Stock, \$1.00 par value per share. Each share of Common Stock entitles the holder thereof to one vote on each matter to be voted upon at the Annual Meeting. Neither the Company's Charter nor its Bylaws provides for cumulative voting rights.

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 By-Laws. 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 2010, one director who will complete the remainder of the term of a new directorship created by an increase in the number of directors which will expire at the Annual Meeting of Shareholders in 2008, and one director who will complete the remainder of the term of a director who resigned in January 2007 which will expire at the Annual Meeting of Shareholders in 2009.

The proxies solicited hereby, unless directed to the contrary, will be voted **FOR** the election as directors of all six 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. For purposes of the election of directors, abstentions and broker non-votes will not be counted as votes cast and will have no effect on the result of the vote, although they will count toward the presence of a quorum. Each nominee has consented to serve as a director, if elected.

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 here 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, 2006, 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 2007 OR ARE OTHERWISE TO BE ELECTED BY THE SHAREHOLDERS

Robert J. Aumiller – Mr. Aumiller, age 58, currently is serving as a director of Carrollton Bank (“the Bank”), the principal subsidiary of the Company, 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. (2)(4)

Ben F. Mason – Mr. Mason, age 69, currently is serving as a director of the Bank and the Company beginning with his appointment in 2001. He is the Director of Institutional Education at Sojourner-Douglass College since January 2006 and formerly Executive Vice President of the Plexus Corporation, a network engineering corporation, as of August 2004. Prior to August 2004, Mr. Mason served as the Executive Director of the Baltimore City Chamber of Commerce, a member business association that promotes business development within Baltimore City. (2)(4)

Charles E. Moore, Jr. – Mr. Moore, age 57, currently is serving as a director of the Bank and the Company beginning with his appointment in 2001. He has been the Co-Founder, Director, President and CFO of TelAtlantic, a consolidation of rural telephone companies across the United States, since 1999. (1)(2)(3)(4)

John Paul Rogers – Mr. Rogers, age 71, 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. He is the brother of William C. Rogers, Jr., a director of the Bank and the Company.

William L. Hermann – Age 66, has served as a director of the Bank and the Company since April, 2006 when he was appointed by the Board of Directors to fill the vacancy in the class of directors whose term expires in 2008 created by the increase in the number of directors from 11 to 12. 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. Under applicable law, since Mr. Hermann was appointed as a director by the Board of Directors after the 2006 annual meeting of shareholders to fill a vacancy on the Board of Directors, Mr. Hermann can serve only until the annual meeting of shareholders following his appointment unless he is elected by the shareholders to fill the remainder of the term of the class of directors in which the vacancy occurs. If Mr. Hermann is elected as a director by the shareholders, he will serve for a term expiring at the Annual Meeting of Shareholders in 2008. (1)(4)

Francis X. Ryan – Age 55, has served as a director of the Bank and of the Company since January 25, 2007 when he was appointed by the Board of Directors to fill the vacancy on the Board created by the resignation of John P. Hauswald who resigned as a director in January, 2007. Since 1991, Mr. Ryan has served as President of F.X. Ryan & Associates, Ltd., a management consulting firm. Under applicable law, since Mr. Ryan was appointed as a director by the Board of Directors to fill a vacancy on the Board of Directors, he can serve only until the annual meeting of shareholders following his appointment unless he is elected by the shareholders to fill the remainder of the term of Mr. Hauswald. If Mr. Ryan is elected as a director, he will serve for a term expiring at the Annual Meeting of Shareholders in 2009.

DIRECTORS CONTINUING IN OFFICE

DIRECTORS WHOSE TERMS EXPIRE IN 2008

Steven K. Breeden – Mr. Breeden, age 48, 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 55, 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)

Howard S. Klein – Mr. Klein, age 48, 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

DIRECTORS WHOSE TERMS EXPIRE IN 2009

Albert R. Counselman – Mr. Counselman, age 58, has served as a director of the Bank 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.

John P. Hauswald – Mr. Hauswald, age 84, has served as a director of the Bank since 1964 and of the Company since its inception in 1990. He was, until his retirement in October 1989, President of The Hauswald Bakery. (4) Mr. Hauswald resigned as a director of the Bank effective March 2006 and as director of the Company effective January 2007, and Francis X. Ryan was appointed by the Board of Directors to fill the vacancy created by Mr. Hauswald's resignation.

David P. Hessler – Mr. Hessler, age 50, 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)

William C. Rogers, Jr. – Mr. Rogers, age 80, has served as a director of the Bank since 1955 and of the Company since its inception in 1990. He has been a partner in the law firm of Rogers, Moore and Rogers, counsel to the Bank, since 1950. He has been Chairman of the Board of The Security Title Guarantee Corporation of Baltimore since 1989 and a director since 1952, and was President from 1970 until March 1989. Mr. Rogers is President of Maryland Mortgage Company where he has been a director since 1953. He is also President of Moreland Memorial Park Cemetery, Inc. where he has been a director since 1959. He is the brother of John Paul Rogers, a director of the Bank and the Company.

FAMILY RELATIONSHIPS

Mr. John Paul Rogers and Mr. William C. Rogers, Jr. are brothers. Mr. Howard S. Klein is married to Messrs. 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, 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, Hessler and Klein. 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 committee are "independent" as defined in applicable law, regulations of the Securities and Exchange Commission ("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 2006, twelve meetings of the Audit Committee were held. The Committee also approves all insider loans. The 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. Mason, Chairman, Aumiller, Breeden, Hackerman, and Moore. 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 committee recommends to the Board the compensation to be paid to all officers, Senior Vice President and above, of the Bank. The committee also administered the 1998 Long Term Incentive Plan as amended, (the "1998 Plan"). During 2006, eight meetings of the Compensation Committee were held.

- (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

The Nominating/Corporate Governance Committee is composed of Messrs. Hessler, Chairman, Breeden, and Moore. 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 and chairpersons of each committee. During 2006, one meeting of the Nominating/Corporate Governance Committee was held.

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 Bank received a monthly retainer fee of \$1,000 for Board meetings and an additional \$300 for attending the Board meeting, and between \$200 and \$600 for each committee meeting attended. The Chairman of the Board of the 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 of the Shareholders received, pursuant to the 1998 Plan, a grant of 630 stock options which vest in three equal installments commencing on the first anniversary of the grant date, assuming that the director is still serving as director of the Company on such dates. The Directors Deferred Compensation Plan was frozen as of 1990. No new participants have entered the Plan since 1990. These 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. Directors options are included in the computation of share dilution. Options for 6,930 shares were granted in 2006 to directors who were not employees of the Company with an exercise price of \$16.31.

The following table sets forth the compensation paid to the Company's directors during the year ended December 31, 2006.

2006 DIRECTORS' COMPENSATION

<i>Name</i>	<i>Fees Earned or</i>		<i>Option Awards</i>	<i>Non-Equity</i>	<i>Change in</i>	<i>Total</i>
	<i>Paid in Cash</i>	<i>Stock Awards</i>				
	<i>(1)</i>	<i>(2)</i>	<i>(3)</i>	<i>Compensation</i>	<i>Deferred</i>	
					<i>Earnings</i>	
					<i>(4)</i>	
Robert J. Aumiller	\$20,100	—	—	—	—	\$20,100
Steven K. Breeden	19,750	—	—	—	—	19,750
Albert R. Counselman	16,600	—	—	—	—	16,600
Harold I. Hackerman	18,900	—	—	—	—	18,900
John P. Hauswald	6,400	—	—	—	—	6,400
William L. Hermann	14,350	—	—	—	—	14,350
David P. Hessler	19,950	—	—	—	—	19,950
Howard S. Klein	18,550	—	—	—	—	18,550
Ben F. Mason	20,300	—	—	—	—	20,300
Charles E. Moore, Jr.	22,000	—	—	—	—	22,000
John P. Rogers	24,100	—	—	—	—	24,100
William C. Rogers, Jr.	17,630	—	—	—	—	17,630

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

(2) No stock awards were issued in 2006.

(3) Stock options for 630 shares of the Company's common stock were issued to each director in April 2006 under the 1998 Plan. Such options vest over a 3 year period. At year-end 2006, the above directors held the unexercised (vested and unvested) options for the following number of shares: Aumiller – 2,100, Breeden – 6,300, Counselman – 3,780, Hackerman – 3,780, Hauswald – 6,090, Hermann – 0, Hessler – 5,040, Klein – 5,040, Mason – 4,410, Moore – 2,100, P. Rogers – 5,670, W. Rogers – 3,980.

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

ATTENDANCE AT BOARD MEETINGS

The Board of Directors of the Company met six times and the Board of Directors of the Bank met fifteen times during the year ended December 31, 2006. 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 committees to which they were assigned during the year ended December 31, 2006.

SHAREHOLDER COMMUNICATIONS WITH THE BOARD

Shareholders may send communications to the Board by mailing the same addressed to: Board of Directors, Carrollton Bancorp, Suite 300, 344 North Charles Street, Baltimore, Maryland 21201.

DIRECTOR NOMINATION PROCESS

The Nominating/Corporate Governance Committee operates pursuant to a charter adopted by the Board, a copy of which is attached to this proxy statement and can also 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 stockholders. 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 stockholder 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 stockholder 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, 2006, 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 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.

<i>Beneficial Owner(1)(21)</i>	<i>Amount and Nature of Beneficial Ownership</i>	<i>Percent of Class</i>
Executive Officers:		
Chief Executive Officer – Bank and Company: Robert A. Altieri	45,877(2)	1.64%
Senior Vice President – Bank and Company: Edward R. Bootey	32,475(3)	1.16%
Senior Vice President – Bank and Company: John A. Giovanazi	17,665(4)	*
Senior Vice President – Bank and Company: Robert F. Hickey	16,390(5)	*
Senior Vice President – Bank and Company: Gary M. Jewell	32,850(6)	1.17%
Senior Vice President – Bank and Company: Lola B. Stokes	105	*
Senior Vice President – Bank and Company: James M. Uveges	5,000(7)	*
DIRECTORS:		
Robert J. Aumiller – Bank and Company	4,410(8)	*
Steven K. Breeden – Bank and Company	22,328(9)	*
Albert R. Counselman – Bank and Company	39,731(10)	1.42%
Harold I. Hackerman – Bank and Company	5,295(11)	*
John P. Hauswald – Bank and Company	17,332(12)	*
William L. Hermann – Bank and Company	100	*
David P. Hessler – Bank and Company	7,510(13)	*
Howard S. Klein – Bank and Company	11,827(14)	*
Ben F. Mason – Bank and Company	70,979(15)	2.53%
Charles E. Moore, Jr. – Bank and Company	5,928(16)	*
John Paul Rogers – Bank and Company	207,622(17)	7.40%
William C. Rogers, Jr. – Bank and Company	273,828(18)(19)(20)	9.76%
All Directors and Executive Officers of the Company as a Group (19 persons)	673,073(21)	23.98%

* Less than 1%

- (1) Unless otherwise indicated, the named person has sole voting and investment power with respect to all shares.
- (2) Includes 1,054 shares owned jointly by Mr. Altieri and his wife, 173 shares Mr. Altieri holds as trustee for minor children under the Maryland Uniform Gifts to Minors Act, and 44,650 fully vested options to purchase shares at an exercise price of between \$10.94 and \$17.79 per share.
- (3) Includes 2,425 shares owned jointly by Mr. Bootey and his wife and 30,050 fully vested options to purchase shares at an exercise price of between \$10.94 and \$17.79 per share.
- (4) Includes 14,515 fully vested options to purchase shares at an exercise price of between \$12.667 and \$16.02 per share.
- (5) Includes 13,000 fully vested options to purchase shares at an exercise price of between \$14.50 and \$17.75 per share.
- (6) Includes 32,850 fully vested options to purchase shares at an exercise price of between \$10.94 and \$17.79 per share.
- (7) Includes 5,000 fully vested options to purchase shares at an exercise price of \$14.85 per share.
- (8) Includes 3,465 shares owned jointly by Mr. Aumiller and his wife and 840 fully vested options to purchase shares at an exercise price of between \$14.45 and \$16.31 per share.
- (9) Includes 11,995 shares owned jointly by Mr. Breeden and his wife and 5,040 fully vested options to purchase shares at an exercise price of between \$9.71 and \$18.10 per share.
- (10) Includes 2,520 fully vested options to purchase shares at an exercise price of between \$12.11 and \$18.10 per share, but excludes 16,454 shares owned by Mr. Counselman's wife.
- (11) Includes 2,670 shares owned jointly by Mr. Hackerman and his wife, and 2,520 fully vested options to purchase shares at an exercise price of between \$12.11 and \$16.31 per share.
- (12) Includes 210 shares owned jointly by Mr. Hauswald and his wife and 4,830 fully vested options to purchase shares at an exercise price of between \$9.71 and \$18.10 per share.

- (13) Includes 1,470 shares owned jointly by Mr. Hessler and his wife and 3,780 fully vested options to purchase shares at an exercise price of between \$9.71 and \$16.31 per share.
- (14) 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 3,780 fully vested options to purchase shares at an exercise price of between \$9.71 and \$16.31 per share.
- (15) Includes 3,150 fully vested options to purchase shares at an exercise price of between \$9.71 and \$16.31 per share. Also includes 67,099 shares owned by The Security Title Guarantee Corporation of Baltimore of which Mr. Mason is a Director.
- (16) Includes 840 fully vested options to purchase shares at an exercise price of between \$12.11 and \$16.31 per share. Excludes 17,320 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.
- (17) Includes 4,410 fully vested options to purchase shares at an exercise price of between \$12.11 and \$18.10 per share. Also includes 67,099 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.
- (18) Includes 67,099 shares owned by The Security Title Guarantee Corporation of Baltimore of which William C. Rogers, Jr. is Chairman, as well as a Director. Also includes 2,720 fully vested options to purchase shares at an exercise price of between \$14.45 and \$18.10 per share.
- (19) Includes 6,818 shares owned by the Moreland Memorial Park Cemetery Bronze Perpetual Care Trust Agreement, Inc., 6,168 shares owned by Moreland Memorial Park Perpetual Care, 34,034 shares owned by Moreland Memorial Park Perpetual Care Trust, 3,597 shares owned by Moreland Memorial Park, Inc. Bronze Marker Perpetual Care Trust Fund, 6,168 shares owned by Moreland Memorial Park Cemetery, Inc. Perpetual Care Trust Agreement, and 9,981 shares owned by Maryland Mortgage Company of which William C. Rogers, Jr., is President as well as a Director.
- (20) Includes 135,263 shares owned jointly by Mr. Rogers and his wife. Excludes 12,380 shares owned by Mr. Roger's wife.
- (21) 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, 344 North Charles Street, Suite 300, Baltimore, Maryland 21201.

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, 2006 unless otherwise indicated.

<i>Name and address of Beneficial Owner</i>	<i>Common Stock Beneficially Owned</i>	<i>Investment Power</i>			<i>Voting Power</i>			<i>Common Stock Beneficially Owned as a Percentage of Outstanding Common Stock</i>
		<i>Sole</i>	<i>Shared</i>	<i>None</i>	<i>Sole</i>	<i>Shared</i>	<i>None</i>	
John Paul Rogers 46 C Queen Anne Way Chester, MD 21619	207,622	130,452	77,080		130,452	77,080		7.40%
William C. Rogers, Jr. 6 South Calvert Street Baltimore, MD 21202	273,828	4,700	269,128		4,700	269,128		9.76%
Patricia A. Rogers P.O. Box 246 Gibson Island, MD 21056	178,462	101,382	77,080		101,382	77,080		6.36%
Hot Creek, LLC 6900 South McCarran Blvd. Suite 3040 Reno, NV 89509	174,255	174,225			174,225			6.21%

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

EXECUTIVE OFFICERS

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

Robert A. Altieri – Mr. Altieri, age 45, 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.

Edward R. Bootey – Mr. Bootey, age 60, has been Senior Vice President – Automation & Technology since October, 1995, and was Senior Vice President – Operations of the Bank from June 1994 to October 1995. Mr. Bootey previously served as Vice President – Operations from January 1991. He served as Assistant Vice President – Operations from December 1987 until January 1991.

John A. Giovanazi – Mr. Giovanazi, age 49, has been Senior Vice President and Chief Lending Officer since his appointment in February 2001. Mr. Giovanazi previously was Vice President of Commercial Lending since August 1996. Prior to joining Carrollton Bank, he was a Vice President, Commercial Lending, with Citizens Bank of Maryland, from 1992 to 1996. Mr. Giovanazi resigned effective March 23, 2007.

Robert F. Hickey – Mr. Hickey, age 45, has been Senior Vice President – Branch Administration since December 2003. Prior to joining Carrollton Bank, Mr. Hickey was an Account Executive for Chase Manhattan Mortgage from 2000 to 2003. He served as President of Carrollton Mortgage Services, Inc. from 1997 to 2000. Mr. Hickey resigned effective January 26, 2007.

Gary M. Jewell – Mr. Jewell, age 60, 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.

James M. Uveges – Mr. Uveges, age 56, has been Senior Vice President and Chief Financial Officer of the 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.

Lola B. Stokes – Mrs. Stokes, age 49, 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.

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 services of independent compensation consulting firms to provide advice on executive compensation matters. In developing the compensation program for 2006, the Compensation Committee retained Clark Consulting to develop and review competitive market data.

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.

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 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 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 Named Executive Officers, as defined below, other than the chief executive officer, in 2006 was 6.4%. The chief executive officer received an increase of 7.5%. The base salary earned in 2006 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.
- Productivity as measured through efficiency ratio.

Incentives are calculated based on budget and business plan goals as measured by the key performance indicators. For 2006, the budgeted amounts were approved at the December 2005 meeting of the Board of Directors. No payouts were made in 2007 based on the final Company performance for the year ended December 31, 2006 due to the \$1.8 million charge from the check kiting scheme by one of the Bank's commercial customers. In 2006, Mr. Jewell received \$30,000 in accordance with the terms of his employment agreement and \$5,615 awarded by the Compensation Committee.

1998 PLAN

All of the Company's Named Executive Officers participate in receiving equity awards under the Company's 1998 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 1998 Plan provides for a variety of different types of compensation arrangements, such as stock options, restricted stock, stock appreciation rights, phantom shares, bonus shares or cash 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. In December 2006, the Compensation Committee recommended and

the Board of Directors approved the grant of 5,000 incentive stock options to Mr. Jewell in accordance with the terms of his employment agreement. Options vest one-third each on the first, second and third anniversaries of the grant. The 1998 Plan prescribes that all outstanding awards granted more than six months prior to the date of any change in control 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.

POTENTIAL POST-EMPLOYMENT PAYMENTS

The Company has entered into certain 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 employment agreements described in the “Executive Compensation – Employment Agreements” section of this proxy statement, and the 1998 Plan.

EMPLOYMENT AGREEMENTS

Upon termination without cause or upon a change in control, Mr. Altieri and Mr. Jewell will be eligible for specific benefits under their 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, 2006. Benefits payable under the Company’s pension plan or 401(K) Plan are not included.

<i>Named Executive Officer</i>	<i>Quit/Termination for</i>	<i>Involuntary</i>	<i>Change in Control</i>
	<i>Cause</i>	<i>Termination Not For</i>	
	<i>(\$)</i>	<i>Cause</i>	<i>(\$)</i>
Robert A. Altieri	—	\$456,957	\$725,436
Gary M. Jewell	—	249,218	616,814

TAX AND ACCOUNTING IMPLICATIONS

Section 162(m) of the Internal Revenue Code provides for non-deductibility, in certain cases, of compensation paid to certain executives in excess of \$1 million per year. The Company does not have a policy limiting compensation to amounts deductible under Section 162(m). The 1998 Plan has been approved by the shareholders and is designed to be a qualified performance-based plan so that Section 162(m) limits would not apply to plan benefits. Section 162(m) limits would apply to salary, bonuses in excess of bonuses under the annual incentive compensation plan and certain amounts included under “Other Annual Compensation” and “All Other Compensation” in the Summary Compensation Table.

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, 2006.

The Compensation Committee
 Ben F. Mason, Chairman
 Robert J. Aumiller
 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 Principal Executive Officer, Principal Financial Officer, and the three most highly compensated other executive officers for 2006 (the "Named Executive Officers").

SUMMARY COMPENSATION TABLE

<i>Name and principal position</i>	<i>Year</i>	<i>Salary</i>	<i>Bonus</i>	<i>Stock Awards (1)</i>	<i>Option Awards (2)</i>	<i>Changes in Pension Value & Nonqualified Deferred Compensation Earnings(3)</i>	<i>All Other Compensation (4)</i>	<i>Total</i>
Robert A. Altieri	2006	\$215,000	\$ —	—	—	\$ 6,822	\$18,383	\$240,205
President & Chief Executive Officer	2005	200,648	50,000	—	10,000	6,401	12,218	262,866
	2004	191,879	—	—	—	66,731	4,873	196,752
James M. Uveges	2006	150,000	—	—	—	—	9,602	159,602
Senior Vice President & Chief Financial Officer(5)	2005	76,464	13,500	—	5,000	—	774	90,738
	2004	—	—	—	—	—	—	—
John A. Giovanazi	2006	137,700	—	—	—	3,359	13,462	154,521
Senior Vice President	2005	121,221	18,509	—	5,000	3,135	7,542	147,272
	2004	115,285	5,500	—	5,000	38,076	2,975	123,760
Gary M. Jewell	2006	120,000	30,000	—	5,000	8,526	11,332	169,858
Senior Vice President	2005	109,782	35,615	—	5,000	7,876	7,747	153,144
	2004	104,931	28,072	—	5,000	98,733	3,295	136,298
Robert F. Hickey	2006	121,275	—	—	—	1,527	6,535	129,337
Senior Vice President	2005	121,275	5,775	—	5,000	1,433	3,666	130,716
	2004	116,217	—	—	5,000	15,208	180	116,397

(1) No stock awards were made in 2006, 2005, or 2004.

(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.

(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) Mr. Uveges was hired in June 2005.

OUTSTANDING EQUITY AWARDS AT 2006 FISCAL YEAR END

The following table shows all outstanding equity awards held by Named Executive Officers as of December 31, 2006:

<i>Name</i>	<i>Option Awards</i>		<i>Option Exercise Price (\$)</i>	<i>Option Expiration Date</i>
	<i>Number of Securities Underlying Unexercised Options (#) Exercisable</i>	<i>Number of Securities Underlying Unexercised Options (#) Unexercisable</i>		
Robert A. Altieri	6,300	—	\$17.790	5/13/1998
	6,300	—	15.419	5/14/1999
	3,150	—	13.452	7/27/2000
	10,500	—	10.943	5/24/2001
	8,400	—	12.667	7/25/2002
	10,000	—	14.500	12/15/2005
James M. Uveges	5,000	—	14.850	6/6/2005
John A. Giovanazi	840	—	15.419	5/13/1999
	525	—	13.452	7/27/2000
	3,150	—	12.667	7/25/2002
	5,000	—	16.020	7/22/2004
	5,000	—	14.500	12/15/2005
Gary M. Jewell	4,200	—	17.790	5/14/1998
	6,300	—	15.419	5/13/1999
	3,150	—	13.452	7/27/2000
	1,050	—	10.943	5/24/2001
	3,150	—	12.667	7/25/2002
	5,000	—	16.020	1/22/2004
	5,000	—	14.500	12/15/2005
	5,000	5,000	17.160	12/31/2006
Robert F. Hickey	3,000	—	17.750	12/31/2003
	5,000	—	16.020	7/22/2004
	5,000	—	14.500	12/15/2005

GRANTS OF PLAN-BASED AWARDS

The following table contains information concerning the grant of stock options under the 1998 Plan during the year ended December 31, 2006.

<i>Name</i>	<i>Grant Date</i>	<i>Number of Securities Underlying Options</i>	<i>Exercise or Base Price of Option Awards (\$/sh)</i>
Robert A. Altieri	—	—	\$ —
James M Uveges	—	—	—
John A. Giovanazi	—	—	—
Gary M. Jewell	12/31/2006	5,000	17.16
Robert F. Hickey	—	—	—

A total of 12,430 incentive stock options were granted in 2006 under the 1998 Plan to directors and employees. Of that total, 6,930 stock options were granted to directors at an exercise price of \$16.31. The options granted to directors vest over a three-year period and expire, if not exercised, in 2016.

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, 2006 and the value realized by them:

<i>Name</i>	<i>Option Awards</i>	
	<i>Number of Shares Acquired on Exercise</i>	<i>Value Realized on Exercise</i>
Robert A. Altieri	—	\$ —
James M. Uveges	—	—
John A. Giovanazi	3,150	12,780
Gary M. Jewell	—	—
Robert F. Hickey	—	—

EMPLOYMENT AGREEMENTS

During 2004, the Company entered into an employment agreement with Mr. Robert A. Altieri, President and Chief Executive Officer. The term of the agreement begins on June 1, 2004 and is effective for three years. As part of the agreement, the Bank will pay Mr. Altieri a minimum annual base salary of \$200,000. 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. 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 (24) months and two years of medical/disability insurance. In the case of termination as a result of Sale of Bank and Mr. Altieri is not offered similar employment with the acquiring institution, Mr. Altieri would be entitled to: (i) three years of his current salary payable in 36 monthly installments (ii) three years of medical/disability insurance (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.

In addition, during 2004, the Company entered into an employment contract with Gary M. Jewell, Senior Vice President, Electronic Banking Department. The term of the agreement begins on June 8, 2004 and is effective for three years. As part of the agreement, the Bank will pay Mr. Jewell a minimum annual base salary of \$102,831. At the end of each calendar year, Mr. Jewell shall receive a cash bonus of 25% of his base salary and option grants to purchase five thousand (5,000) shares of Bank common stock, 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 (24) months. In the case of termination as a result of Sale of Bank and Mr. Jewell will receive a severance package to include: (i) three years of his current salary payable in 36 monthly installments and (ii) three years of medical/disability insurance. After the three year term, Mr. Jewell is entitled to an additional three (3) years to receive 65% of his salary and medical/disability insurance. Additional provisions include a Non-Compete cause which for one year following the termination of employment, prohibits Mr. Jewell from soliciting, servicing, or assisting in Point of Sale transactions for any other company. Mr. Jewell is also required to train other persons designated by the Bank in all aspects of Electronic Banking.

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, 2006, the following table shows the present value of accumulated benefits under the Company's defined benefit plan for each Named Executive Officer:

<i>Name</i>	<i>Plan Name</i>	<i>Number of Years of Credited Service</i>	<i>Present Value of Accumulated Benefits</i>
Robert A. Altieri	Pension Plan	13	\$ 116,633
James M. Uveges(2)	Pension Plan	N/A	—
John A. Giovanazi	Pension Plan	8	55,851
Gary M. Jewell	Pension Plan	9	129,060
Robert F. Hickey	Pension Plan	7	26,114

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

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 defined benefit 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's 401(K) contribution up to 6% of the employee's compensation. All Named Executive Officers participated in the 401(K) plan in 2006 and received matching funds. Such amounts attributable to each Named Executive Officer are included in all other compensation.

COMPENSATION COMMITTEE INTERLOCKS AND INSIDER PARTICIPATION

In 2006, 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, Steven K. Breeden, David P. Hessler and William C. Rogers, Jr. 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 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 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, 2006, 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 \$7,976,614 which represented approximately 22.9% of the Company's equity capital accounts.

William C. Rogers, Jr., 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 \$195,000 in 2006, 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 2006 of approximately \$282,000. 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 for appraisal, construction, brokerage and management services of approximately \$356,000 in 2006 for appraisal and property management services provided by MacKenzie Commercial Real Estate Services. Management believes these terms were as favorable as could have been obtained elsewhere.

Under the Company's policies and procedures for review and approval of transactions with related persons, such transactions are to be approved by a majority of the directors who have no financial interest in the transaction.

AUDIT COMMITTEE REPORT

The Audit Committee has adopted a written charter which was included as part of the definitive proxy statement delivered to stockholders with respect to the 2004 Annual Meeting. The members of the Audit Committee are "independent" as such term is defined in Rule 4200(a)(15) of the National Association of Securities Dealers' 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 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 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, 2006.

Audit Committee:

Charles E. Moore, Jr., Chairman

Harold I. Hackeman

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 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 since the beginning of 2006.

PROPOSAL 2: APPROVAL OF THE 2007 EQUITY PLAN

On March 29, 2007, the Board of Directors approved, subject to shareholder approval, the Carrollton Bancorp 2007 Equity Plan (the "2007 Equity Plan"), under which 500,000 shares of the Common Stock of the Company will be reserved for issuance. The 2007 Equity Plan will not become effective until it is approved by the Company's shareholders. The Board of Directors is requesting that the shareholders of the Company approve the 2007 Equity Plan so that the Company may issue to directors and key employees, awards that are linked to the value of the Company's Common Stock. The 2007 Equity Plan will replace the 1998 Plan. If the 2007 Equity Plan is not approved, then the 1998 Plan will remain in effect.

DESCRIPTION OF THE 2007 EQUITY PLAN

The following is a description of the purpose and a summary of the provisions of the 2007 Equity Plan. The summary is qualified in its entirety by reference to the complete text of the 2007 Equity Plan, which is attached hereto as Appendix A.

General. The 2007 Equity Plan permits us to issue stock options, stock appreciation rights ("SARs"), restricted stock, restricted performance stock, unrestricted company stock and performance unit awards, to non-employee directors and employees (including officers who are directors) of Carrollton Bancorp and its subsidiaries. The 2007 Equity Plan does not permit the repricing of stock options or stock appreciation rights or the granting of discounted stock options or stock appreciation rights. The Plan provides for automatic annual grants of 300 shares of unrestricted stock of the Company to each non-employee director.

Purpose. The purposes of the Plan are as follows:

- To attract and retain employees and non-employee directors of outstanding ability;
- To strengthen the Company's capability to develop, maintain, and direct a competent management team;
- To provide an effective means for selected employees and non-employee directors to acquire and maintain ownership of Company stock;
- To motivate employees to achieve long-range performance goals and objectives; and
- To provide incentive compensation opportunities competitive with peer financial institution holding companies.

Administration of the Plan. The Board has the authority and the discretion under the Plan to grant awards to non-employee directors of the Company. The Compensation Committee of the Board of Directors has the authority and the discretion to administer the Plan in general and to issue awards to employees of the Company and its subsidiaries and to directors of subsidiaries of the Company. The term "Grantor" as used in this summary refers to the Board, with respect to awards to non-employee directors, and to the Compensation Committee, with respect to awards to employees of the Company and its subsidiaries and to directors of subsidiaries of the Company. Except as expressly limited by the Plan, the authority of the Grantor includes the authority to determine the timing of awards, to select the recipients of awards, and to determine the terms of each award, including, among other things, any modifications of awards, applicable restrictions, termination and vesting conditions.

The Compensation Committee is comprised solely of non-employee directors of the Board.

Number of Shares Available for Issuance. The aggregate number of such shares which may be issued upon exercise of options or in connection with other awards under the 2007 Equity Plan shall not exceed Five Hundred Thousand (500,000). If an award or portion of an award is cancelled, terminated, expires or is forfeited before it is exercised or becomes fully vested, the shares of common stock underlying that award or portion of the award will be available for future grants under the 2007 Equity Plan. The maximum aggregate dollar value of, and the maximum number of shares of Company stock subject to, restricted stock, restricted performance stock and performance units awarded to any employee with respect to a performance period or restriction period may not exceed 500,000 shares of Company stock (for stock awards) and \$500,000 (for non-stock awards), respectively, for each fiscal year included in such restriction period or performance period. The maximum number of shares of common stock for which Options or SARs may be granted to any employee in any one fiscal year shall not exceed 500,000. The Compensation Committee or the Board may adjust the 500,000 share limit if it determines that a dividend, recapitalization, stock split, merger, consolidation or other similar corporate transaction or event equitably requires an adjustment.

Types of Awards. The 2007 Equity Plan provides for the issuance of incentive stock options to our employees and nonqualified stock options, stock appreciation rights, restricted stock, restricted performance stock, unrestricted company stock and performance unit awards to our employees and non-employee directors. Rights to awards may be contingent on the satisfaction of performance criteria determined by the Grantor, including but not limited to earnings per share (actual or targeted growth); net income after capital costs; net income (before or after taxes); return measures (including, but not limited to, return on average assets, risk-adjusted return on capital, or return on average equity); efficiency ratio; full-time equivalency control; stock price (including, but not limited to, growth measures and total shareholder return); noninterest income compared to net interest income ratio; expense targets; operating efficiency; EVA[®]; credit quality measures; customer satisfaction measures; loan growth; deposit growth, net interest margin; fee income; and operating expense ("Performance Criteria").

Stock Options. The plan provides for two types of stock options: incentive stock options and non-qualified stock options. The differences between incentive stock options and non-qualified stock options relate mainly to their tax treatment under the U.S. Internal Revenue Code (see *U.S. Tax Consequences*, below). A stock option gives the holder the right to receive a designated number of shares of our common stock during the period that the option is vested upon payment of the exercise price for the stock options, subject to the terms and conditions that the Grantor, in its sole discretion, shall determine at the time the award is made. The exercise price of an option may not be less than the fair market value of our stock on the date of grant of the option, except for incentive stock options granted to 10% shareholders, in which case the exercise price must be at least 110% of the fair market value of our stock on the date of grant. Incentive stock options must expire no later than the tenth anniversary of the date of grant, except for incentive stock options granted to 10% shareholders, in which case expiration may be no later than the fifth anniversary of the date of grant.

Stock Appreciation Rights. A stock appreciation right entitles the holder to a payment in cash or shares of our common stock equal to the excess of the fair market value of the number of shares of our common stock underlying the stock appreciation right as of the date the stock appreciation right is exercised over such fair market value as of the date the stock appreciation right is granted. A stock appreciation right is subject to the terms and conditions that the Grantor, in its sole discretion, shall determine at the time the award is made.

Restricted Stock and Restricted Performance Stock. A restricted stock award is an award of shares of our common stock subject to the terms and conditions that the Grantor, in its sole discretion, shall determine at the time the award is made. Generally, restricted stock is forfeited to the Company if the individual to whom it was awarded terminates service prior to the end of the vesting period determined by the Grantor. A restricted performance stock award is an award of shares of our common stock that is forfeited to the Company if specific performance criteria, including one or more of the Performance Criteria, are not met during a defined period, called a performance period. The Grantor has the sole discretion to determine the performance criteria and the performance period and such other terms and conditions of the award.

Unrestricted Stock. An unrestricted stock award is an award of shares of our common stock subject to the terms and conditions that the Grantor, in its sole discretion, shall determine at the time the award is made. However, unrestricted stock awards are fully vested, and therefore are not subject to forfeiture. In order to ensure that non-employee directors have a significant ownership stake in the Company, each non-employee director will be granted 300 shares of unrestricted Company stock on the date of each annual shareholders meeting, and each new non-employee director will be granted 300 shares of unrestricted stock when he or she commences service as a director.

Performance Units. A performance unit represents the right to receive a payment in cash or shares of our common stock subject to specific performance criteria, including one or more of the Performance Criteria.

Effect of Termination on Outstanding Awards. A Grantor's termination of service with the Company and all subsidiaries will have the following effect on outstanding Awards, unless the award agreement provides otherwise:

- *Death, disability or retirement.* If the grantee dies, becomes disabled or retires, all of his outstanding options, stock appreciation rights, restricted stock awards and restricted performance stock awards shall become fully vested. Options and stock appreciation rights may be exercised by the grantee or his or her personal

representative at any time before the earlier of (i) one year after the grantee's termination of service or (ii) the expiration date of the Award.

- *Discharge for cause.* If the grantee is discharged for cause, his or her outstanding options and stock appreciation rights shall terminate immediately and his or her non-vested restricted stock awards and restricted performance stock awards shall immediately be forfeited.
- *Termination for other reasons.* If the grantee terminates for any other reason, his or her outstanding vested options and stock appreciation rights may be exercised at any time within three months after such termination. Any outstanding options and stock appreciation rights and restricted stock and restricted performance stock rights that are not vested will be forfeited..
- *Performance Units.* If the grantee terminates service with the Company and all of its subsidiaries at any time during the applicable performance period, all outstanding performance units will terminate.

Adjustments for Changes in Capitalization. If the Company undergoes a reorganization, recapitalization, reclassification, stock split, stock dividend, distribution, combination of shares, merger, consolidation, rights offering, or any other changes in its corporate structure or shares, appropriate adjustments shall be made by the Committee or the Board, in the aggregate number and kind of shares subject to the Plan, and the number and kind of shares and the option price per share subject to outstanding options or which may be issued under outstanding awards and the other terms of awards.

Change in Control. All outstanding awards vest upon a "change in control." "Change in control" means the occurrence of one or more of the following:

- The acquisition by any one person, or more than one person acting as a group, of ownership of stock of the Company that, together with stock held by such person or group, constitutes more than 50 percent of the total fair market value or total voting power of the stock of the Company. However, if any one person, or more than one person acting as a group, is considered to own more than 50 percent of the total fair market value or total voting power of the stock of the Company, the acquisition of additional stock by the same person or persons is not considered to cause a change in control. An increase in the percentage of stock owned by any one person, or persons acting as a group, as a result of a transaction in which the Company acquires its stock in exchange for property is treated as an acquisition of stock for this purpose.
- The acquisition by any one person, or more than one person acting as a group during any 12-month period of ownership of stock of the Company possessing 35 percent or more of the total voting power of the stock of the Company.
- The replacement of a majority of members of the Board during any 12-month period by directors whose appointment or election is not endorsed by a majority of the members of the Board prior to the date of the appointment or election.
- The acquisition by any one person, or more than one person acting as a group, during any 12-month period of assets from the Company that have a total gross fair market value equal to or more than 40 percent of the total gross fair market value of all of the assets of the Company immediately prior to such acquisition or acquisitions.

Amendment and Termination. The 2007 Equity Plan may be terminated by the Board at any time. The Board may amend the 2007 Equity Plan (and the awards issued thereunder), but may not, without prior approval of the stockholders:

- increase the maximum number of shares of common stock that may be issued under the Plan;
- expand the types of awards available to Participants under the Plan;
- materially change the method of determining the option price of options;
- permit the repricing of Options;
- extend the termination date of the Plan; or
- take any other action that requires shareholder approval to comply with any legal or stock exchange requirements.

U.S. Tax Consequences. The following brief description, which is based on existing law, sets forth certain of the federal income tax consequences of the grant of awards under the 2007 Equity Participation Plan. This description may differ from the actual tax consequences incurred by any individual recipient of an award. Moreover, existing law is subject to change by new legislation, by new regulations, by administrative pronouncements and by court decisions or by new or clarified interpretations or applications of existing laws, regulations, administrative pronouncements and court decisions. Any such change may affect the federal income tax consequences described below.

Non-Qualified Stock Options. A non-employee director or employee who is granted a non-qualified stock option will not recognize taxable income at the time the stock option is granted. In general, an optionee will be subject to

tax for the year of exercise on an amount of ordinary income equal to the excess of the fair market value of the shares on the date of exercise over the option exercise price, and the Company will receive a corresponding Federal income tax deduction. Income tax withholding requirements apply upon exercise. The optionee's basis in the shares so acquired will be equal to the option exercise price plus the amount of ordinary income upon which he or she is taxed. Upon subsequent disposition of the shares, the optionee will recognize capital gain or loss, long-term or short-term, depending upon the length of time the shares are held after the stock option is exercised.

Incentive Stock Options. An optionee is not taxed at the time an incentive stock option is granted. The tax consequences upon exercise and later disposition generally depend upon whether the optionee was an employee of the Company or a subsidiary at all times from the date of grant until three months preceding exercise (one year in the case of disability) and on whether the optionee holds the shares for more than one year after exercise and two years after the date of grant of the stock option.

If the optionee satisfies both the employment rule and the holding rule, for regular tax purposes the optionee will not recognize income upon exercise of the stock option and the Company will not be allowed an income tax deduction at any time. The difference between the option exercise price and the amount realized upon disposition of the shares by the optionee will constitute a long-term capital gain or a long-term capital loss, as the case may be.

If the optionee meets the employment rule but fails to observe the holding rule (a "disqualifying disposition"), the optionee generally recognizes as ordinary income, in the year of the disqualifying disposition, the excess of the fair market value of the shares at the date of exercise over the option exercise price. Any excess of the sales price over the fair market value at the date of exercise will be recognized by the optionee as capital gain (long-term or short-term depending on the length of time the stock was held after the stock option was exercised). If, however, the sale price is less than the fair market value at the date of exercise, then the ordinary income recognized by the optionee is generally limited to the excess of the sale price over the option exercise price. In both situations, the tax deduction allowable to the Company is limited to the amount of ordinary income recognized by the optionee. Under current Internal Revenue Service guidelines, the Company is not required to withhold any Federal income tax in the event of a disqualifying disposition.

Different consequences may apply for an optionee subject to the alternative minimum tax.

Stock Appreciation Rights. A non-employee director or employee will not realize taxable income upon the award of stock appreciation rights. Upon the exercise of stock appreciation rights, any cash received and the fair market value on the exercise date of any shares of common stock received would constitute ordinary income to the participant, and the Company would be entitled to a deduction in the amount of such income at the time of exercise.

Restricted Stock and Restricted Performance Stock. A non-employee director or employee who is granted restricted stock or restricted performance stock will not recognize taxable income when the restricted stock or restricted performance stock is granted. In general, a restricted stockholder will recognize ordinary taxable income when the stock is no longer subject to a substantial risk of forfeiture and the Company will receive a corresponding Federal income tax deduction. However, a restricted stockholder may file with the IRS a "section 83(b) election" when the restricted stock or restricted performance stock is granted, as a result of which he or she will recognize taxable ordinary income when the stock is granted. Upon subsequent disposition of the shares, the restricted stockholder will recognize capital gain or loss, long-term or short-term, depending on the length of time the shares are held after the shares were recognized as ordinary income.

Performance Units. A non-employee director or employee normally will not recognize taxable income upon the award of performance units. When the conditions and requirements established with respect to such an award have been satisfied and the payment amount determined, any cash and the fair market value of any shares of our common stock received will constitute ordinary income to the participant in the year in which paid or when no longer subject to a substantial risk of forfeiture, and the Company will be entitled to a deduction in the same amount.

Unrestricted stock. A non-employee director normally will recognize taxable income and the Company will be entitled to a deduction when unrestricted stock is granted.

Deductibility of executive compensation. Section 162(m) of the Internal Revenue Code 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. The limitation applies only to compensation which is 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). 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) and will not have to be taken into account for purposes of the \$1 million limitation. Accordingly, all compensation deemed paid with

respect to those stock options should 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 \$1 million limitation unless the individual award is specifically designed to comply with section 162(m)'s performance-based exemption, or 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).

Impact of Section 409A. Section 409A of the Internal Revenue Code applies to compensation vested or deferred after December 31, 2004. Although final IRS regulations under section 409A have not yet been issued, section 409A may apply to awards under the 2007 Equity Participation Plan.

REQUIRED VOTE AND RECOMMENDATION

Stockholder approval of the 2007 Equity Plan is required (i) under stock exchange rules for listing the shares of common stock reserved under the 2007 Equity Participation Plan and (ii) under the Internal Revenue Code of 1986, as amended, in order for options granted under the 2007 Equity Participation Plan to be considered “incentive stock options” and for awards to qualify as “performance-based” for purposes of Code Section 162(m).

A majority of the votes cast at the annual meeting is required for approval of the 2007 Equity Plan as set forth in this Proposal 2. Abstentions and broker non-votes will have no effect on the vote for this Proposal 2.

The Board of Directors unanimously recommends a vote “FOR” approval of the 2007 Equity Plan.

PROPOSAL 3: RATIFICATION OF APPOINTMENT OF 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 2007 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 Annual Meeting.

AUDIT FEES AND SERVICES

	2006	2005
Audit Fees	\$76,049	\$80,205
Audit – Related Fees	10,500	9,995
Tax Fees	4,436	5,673
All Other Fees	—	—
Total	<u>\$90,985</u>	<u>\$95,873</u>

Audit services of Rowles & Company, LLP for 2006 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 2006 include charges related to the Company’s defined benefit plan audit and the Company’s 401(K) plan audit. “Tax Fees” in 2006 represent income tax return preparation and advice.

Audit services of Rowles & Company, LLP for 2005 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 2005 include charges related to the Company’s 401(K) plan audit. “Tax Fees” in 2005 represent income tax return preparation and advice.

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, 2006, 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 2007 as set forth in this Proposal 3. Abstentions and broker non-votes will have no effect on the vote for this Proposal 3.

The Board of Directors unanimously recommends a vote “FOR” ratification of Rowles and Company, LLP, as the Company’s independent registered public accounting firm for 2007.

SHAREHOLDER PROPOSALS FOR THE 2008 ANNUAL MEETING

Proposals of shareholders to be presented at the 2008 Annual Meeting of the Company's shareholders must be received at the Company's principal executive offices prior to December 15, 2007 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.

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 meeting, 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.

IMPORTANT NOTICE REGARDING DELIVERY OF SECURITY HOLDER DOCUMENTS

The Securities and Exchange Commission 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 Stockholders, 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 Carrollton Bancorp proxy statement, annual report and other future stockholder mailings.

If you do not object to householding, (1) you are agreeing that your household will only receive one copy of future Carrollton Bancorp stockholder mailings, and (2) your consent will be implied and householding will start 60 days after the mailing of this notice, to the extent you have not previously consented to participation in the householding program. Your affirmative or implied consent to householding will remain in effect until you revoke it. Carrollton Bancorp shall begin sending individual copies of applicable security holder communications subject to householding rules to a security holder within 30 days after revocation by the security holder of prior affirmative or implied consent. Your participation in the householding program is encouraged. It will reduce the volume of duplicate information received at your household as well as the cost of us preparing and mailing duplicate materials.

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 stockholders who wish to receive separate copies may do so by contacting their bank or broker or other holder of record.

By Order of the Board of Directors

Allyson Cwiek
Secretary
Baltimore, Maryland
April 13, 2007

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U.S. SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549
FORM 10-K

Annual Report pursuant to Section 13 OR 15(d) of the Securities Exchange Act of 1934 (Fee required)

For the fiscal year ended December 31, 2006

Commission file number: 0-23090

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

<u>Maryland</u> (State or Other Jurisdiction of Incorporation or Organization)	<u>52 1660951</u> (I.R.S. Employer Identification No.)
<u>344 N. Charles St. Baltimore, MD</u> (Address of principal executive offices)	<u>21201</u> (Zip Code)
<u>(410) 536 4600</u> (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 in this form, 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, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer Non-accelerated filer

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 on December 31, 2006 was approximately \$39.4 million. This calculation is based upon the last price known to the registrant at which its Common Stock was sold as of the last business day of the registrant's most recently completed fourth fiscal quarter. As of December 31, 2006, the last known sale price was \$17.16 per share. For the purpose of this calculation, the term "affiliate" refers to all directors and executive officers of the registrant.

On March 9, 2007, 2,819,035 shares of the registrant's common stock were issued and outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

The Company's Proxy Statement for Annual Meeting of Shareholders to be held on May 15, 2007, is incorporated by reference in this Form 10-K in Part III, Item 10, Item 11, Item 12, Item 13, and Item 14.

TABLE OF CONTENTS

PART I

Item 1 —	Business	30
Item 1A —	Risk Factors	37
Item 2 —	Properties	40
Item 3 —	Legal Proceedings	41
Item 4 —	Submission of Matters to a Vote of Security Holders	41

PART II

Item 5 —	Market for Registrant's Common Equity and Related Shareholders Matters	42
Item 6 —	Selected Financial Data	44
Item 7 —	Management's Discussion and Analysis of Financial Condition and Results of Operations	45
Item 7A —	Quantitative and Qualitative Disclosures About Market Risk	59
Item 8 —	Financial Statements and Supplementary Data	60
Item 9 —	Changes in and Disagreements with Accountants on Accounting and Financial Disclosure	86
Item 9A —	Controls and Procedures	86
Item 9B —	Other Information	86

PART III

Item 10 —	Directors, Executive Officers, and Corporate Governance	86
Item 11 —	Executive Compensation	86
Item 12 —	Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters	86
Item 13 —	Certain Relationships and Related Transactions and Director Independence	86
Item 14 —	Principal Accountant Fees and Services	86

PART IV

Item 15 —	Exhibits and Financial Statement Schedules	87
Signatures		88

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 proceeding.

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 2007.

Statement regarding 2007 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 (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, 2006, 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 Company expects its fifth branch to open in Baltimore County in June 2007. 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 also operated a network of ATMs in Maryland, Virginia, and West Virginia and sponsors national retailers who accept ATM cards for purchases in various electronic networks. On September 22, 2005, Wal-Mart notified the Bank of its intention to terminate the agreement for the Bank to provide ATM’s at Wal-Mart, Sam’s Club, and Wal-Mart Supercenters in Maryland, Virginia, and West Virginia. The effective date of the termination was January 22, 2006.

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.

The executive offices of the Company and the principal office of the Bank are located at 344 North Charles Street, Baltimore, Maryland 21201, telephone number (410) 536-4600. 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 “Insider Transactions — SEC Filings” — “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.

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.
- Point of Sale (POS) services.
- 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 low risk based on the type of collateral (residential property) and the underwriting standards used. The Bank experienced no losses and no recoveries on residential mortgage loans in 2006. The Bank experienced no losses and recoveries of \$14,874 in 2005. The Bank experienced losses of \$746 and recoveries of \$8,087 in 2004. There were no residential mortgage loans delinquent more than 90 days at December 31, 2006. There are no discernible delinquency or loss trends relating to residential mortgage loans known to management.

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 low due to the underlying values of the collateral. The Bank experienced no losses or recoveries on home equity loans during 2006. The Bank experienced losses on home equity loans during 2005 of \$0 and recoveries of \$7,700. The Bank experienced losses on home equity loans during 2004 of \$7,000 and recoveries of \$0. There were \$0 of home equity loans delinquent more than 90 days at December 31, 2006. There are no discernible delinquency or loss trends relating to home equity loans known to management.

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 \$59,120 during 2006 and \$0 during 2005 and 2004, respectively. There were \$252,295 of commercial mortgage loans past due more than 90 days at December 31, 2006. There are no known discernible delinquency or loss trends relating to commercial mortgage loans.

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 did not experience any losses or recoveries on construction and land development loans during 2006, 2005, or 2004. There were no construction and land development loans past due more than 90 days at December 31, 2006. There are no discernible delinquency or loss trends relating to construction and land development loans known to management.

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 2006. The Bank had losses of \$123,578 and recoveries of \$130,904 on time demand and loans in 2005. The Bank had losses of \$192,440 and recoveries of \$67,111 on demand and time loans in 2004. There were no demand and time and line of credit loans delinquent more than 90 days at December 31, 2005. There are no discernible delinquency or loss trends relating to demand and time loans or lines of credit known to management.

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 \$11,515, \$0 and \$10,020, in 2006, 2005 and 2004, respectively. There were recoveries of \$608, \$0, and \$14,898, in 2006, 2005, and 2004, respectively. There were no home improvement loans delinquent more than 90 days at December 31, 2005. There are no discernible loss or delinquency trends relating to home improvement loans known to management.

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 losses on automobile loans of \$6,849 in 2006 and no losses in 2005, or 2004, and recoveries of \$1,251, \$0, and \$0, in 2006, 2005 and 2004, respectively. There were no automobile or other vehicle loans past due more than 90 days at December 31, 2005. There are no discernible delinquency or loss trends relating to automobile or other vehicle loans known to management.

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 2006, 2005, and 2004 were \$11,662, \$1,927, and \$43,470, respectively. There were no overdraft loans and other personal loans past due more than 90 days at December 31, 2006. There are no discernible delinquency or loss trends relating to overdraft lines and other personal loans known to management.

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 2006, 2005, or 2004. Recoveries on loans secured by stocks and bonds were \$0, \$0, and \$411 in 2006, 2005, and 2004 respectively. There were no loans secured by savings accounts or stock and bond certificates past due more than 90 days at December 31, 2006. There are no discernible delinquency or loss trends relating to loans secured by savings accounts or stock and bond certificates known to management.

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.

Mulberry Street LLC was established in 2004 for the purpose of disposing of real estate owned.

Investment Activities. – The Company maintains a portfolio of investment securities to provide liquidity and income. The current portfolio amounts to about 16% 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 2006 to 2031, 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 balance of accounts over \$100,000 is not significant, and these accounts are offered principally as accommodations to existing customers.

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.

Brokerage Activities. – CFS provides full service brokerage services for stocks, bonds, mutual funds and annuities. For 2006, commission income totaled \$647,000 and net income was \$152,000.

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 more broad and include areas outside of the Baltimore MSA. CMSI operates in Delaware, Pennsylvania, Virginia and West Virginia in addition to its core Maryland operations.

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, 2006, the Bank and its subsidiaries had 138 full time equivalent employees, 33 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 BHCA 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 Federal Deposit Insurance Corporation ("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. As an FDIC insured institution, deposits of the Bank are currently insured to a maximum of \$100,000 per depositor through the Bank Insurance Fund ("BIF"). For traditional and ROTH IRA's, the federal deposit insurance limit increased from \$100,000 to \$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 currently pays a *de minimus* semi-annual assessment.

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.

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 does not result 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 revises the Bank Holding Company Act of 1956 and repeals 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 Federal Reserve Board, which regulates the national money supply in order to mitigate recessionary and inflationary pressures. Among the techniques available to the Federal Reserve Board 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.

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 judgement. 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, 2006, approximately 78% 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 Bank Holding Company Act of 1956, as amended, and to regulation and supervision by the Federal Deposit Insurance Corporation, or FDIC, and the Office of the Maryland Commissioner of Financial Regulation. 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 Federal Reserve Board 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.

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, 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.

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

Our ability to pay dividends to our shareholders largely depends on Carrollton Bancorp's receipt of dividends from Carrollton Bank. The amount of dividends that Carrollton Bank may pay to Carrollton Bancorp 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 \$14.40 and \$19.45 per share during the last 12 months ended December 31, 2006. 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 \$2.7 million at December 31, 2006:

<i>Location</i>	<i>Description</i>
1740 East Joppa Road Towson, MD 21234	Full service branch with drive thru, Electronic Banking 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	Full service branch with Executive offices, Lending offices and Finance offices

The Company leased the following facilities at an aggregate annual rental of \$937,160 as of December 31, 2006:

<i>Location</i>	<i>Description</i>	<i>Lease Expiration Date*</i>
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	Administrative and operational offices	February 28, 2019
2637-A Old Annapolis Road Hanover, MD 21076	Full service branch	October 1, 2014
Wilkens Beltway Plaza 4658 Wilkens Avenue Baltimore, MD 21229	Limited-service branch	October 21, 2024
8157A Honeygo Boulevard White Marsh, MD 21236	Full service branch	December 31, 2017
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

<i>Location</i>	<i>Description</i>	<i>Lease Expiration Date*</i>
10301 York Road Cockeysville, MD 21030	Full service branch expected to open in the second quarter of 2007	December 1, 2047
2300 York Road Timonium, MD 21093	Mortgage subsidiary offices	January 14, 2010
208 Hickory Avenue Bel Air, MD 21014	Mortgage subsidiary offices	March 31, 2010
8905 Harford Road Baltimore, MD 21234	Mortgage subsidiary offices	June 30, 2007
1 Center Square, Suite 201 Hanover, PA 17331	Mortgage subsidiary offices	June 29, 2007

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

ITEM 3: LEGAL PROCEEDINGS

The Company is involved in various 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 stockholders during the quarter ended December 31, 2006.

PART II

ITEM 5: MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

TRADING AND DIVIDENDS

As of December 31, 2006, there were 391 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 \$0.45 in 2006, \$0.40 in 2005, and \$0.38 in 2004, representing a payout ratio of 48.98% in 2006, 45.97% in 2005, and 121.17% in 2004. 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 Carrollton Bancorp common stock.

During 2006, the Company repurchased and retired 7,518 shares of common stock at an average price of \$17.14. In 2005, the Company repurchased and retired 42,500 shares of common stock at a price of \$14.10 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	
	2006		2005		2006	2005
	Low	High	Low	High		
4th Quarter	\$16.99	\$19.45	\$14.00	\$15.00	\$0.12	\$0.10
3rd Quarter	16.11	18.00	13.95	16.29	0.11	0.10
2nd Quarter	15.64	18.80	14.25	17.00	0.11	0.10
1st Quarter	14.40	15.95	14.12	17.00	0.11	0.10
					<u>\$0.45</u>	<u>\$0.40</u>

As of December 31, 2006, there were approximately 391 common shareholders of record holding an aggregate of 2,806,705 shares. The Company believes there to be in excess of 558 beneficial owners of the Company's Common Stock.

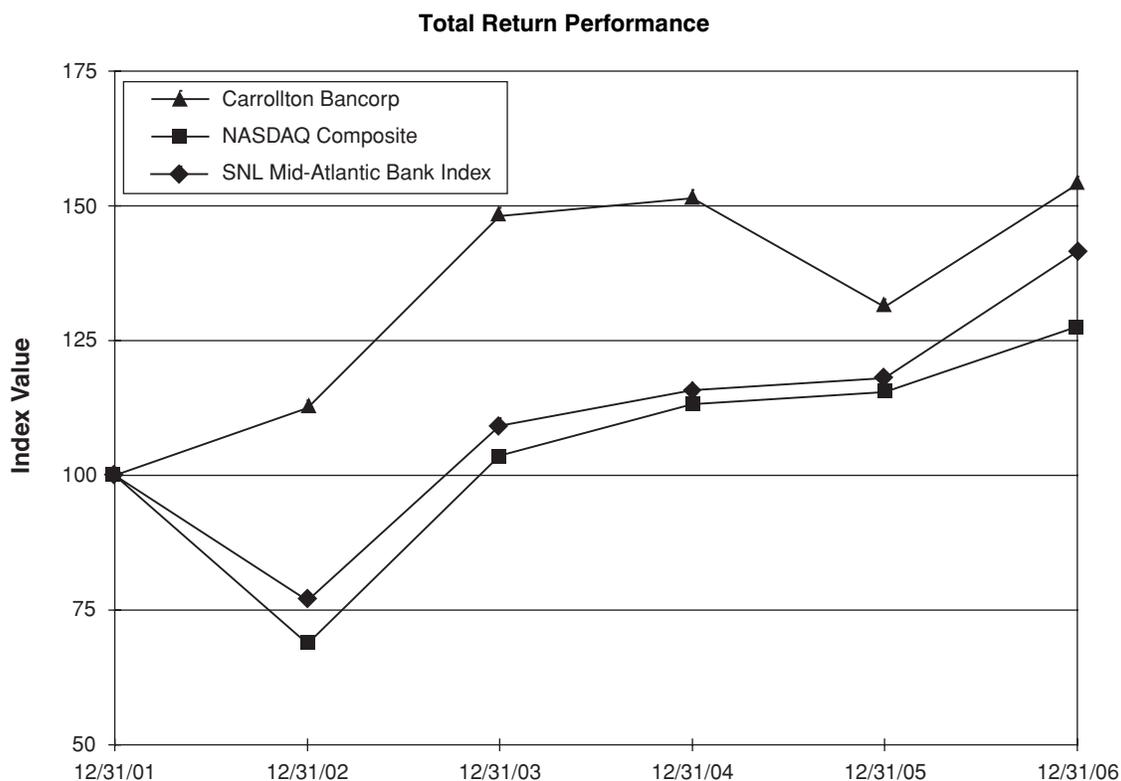
The ability of the Company to pay dividends in the future will be dependent on the earnings, if any, financial condition and business of the Company, as well as other relevant factors, such as regulatory requirements. No assurance can be given either that the Company's future earnings, if any, will be 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.

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, 2001 to December 31, 2006 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, 2001 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.



Index	Period Ending					
	12/31/01	12/31/02	12/31/03	12/31/04	12/31/05	12/31/06
Carrollton Bancorp	100.00	112.33	148.16	151.37	131.18	154.18
NASDAQ Composite	100.00	68.76	103.67	113.16	115.57	127.58
SNL Mid-Atlantic Bank Index	100.00	76.91	109.35	115.82	117.87	141.46

The following table provides information about the Company's outstanding options, warrants and rights under equity compensation plans:

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	229,030	\$ 14.70	34,140
Equity compensation plans not approved by security holders	—	—	—
Total	229,030	\$ 14.70	34,140

ITEM 6: SELECTED FINANCIAL DATA

	2006	2005	2004	2003	2002
CONSOLIDATED INCOME STATEMENT DATA:					
Interest income	\$ 23,127,504	\$ 19,071,379	\$ 15,500,323	\$ 15,935,691	\$ 18,985,364
Interest expense	8,737,450	7,375,083	5,321,622	6,639,734	8,692,320
Net interest income	14,390,054	11,696,296	10,178,701	9,295,957	10,293,044
Provision for loan losses	—	—	—	243,000	526,000
Net interest income after provision for loan losses	14,390,054	11,696,296	10,178,701	9,052,957	9,767,044
Noninterest income	8,898,996	10,718,636	8,781,151	8,268,612	7,534,802
Noninterest expenses	19,381,003	18,634,124	17,751,000	16,058,355	14,536,958
Income before income taxes	3,908,047	3,780,808	1,208,852	1,263,214	2,764,888
Income taxes	1,323,268	1,322,371	320,488	338,500	847,630
Net income	\$ 2,584,779	\$ 2,458,437	\$ 888,364	\$ 924,714	\$ 1,917,258
CONSOLIDATED BALANCE SHEET DATA, AT YEAR END					
Assets	\$349,824,752	\$360,467,146	\$319,123,132	\$302,409,975	\$324,221,615
Gross loans	260,001,314	247,943,073	219,726,294	199,296,561	205,220,126
Deposits	277,903,801	271,626,503	225,846,145	207,056,100	230,264,108
Shareholders' equity	34,711,378	34,640,165	34,215,280	34,124,882	33,691,079
PER SHARE DATA:					
Number of shares of Common Stock outstanding, at year-end	2,806,705	2,809,698	2,834,823	2,828,078	2,821,757
Net income:					
Basic	\$ 0.92	\$ 0.87	\$ 0.31	\$ 0.33	\$ 0.68
Diluted	0.90	0.87	0.31	0.32	0.68
Cash dividends declared	0.45	0.40	0.38	0.36	0.34
Book value, at year end	12.37	12.33	12.07	12.07	11.94
Performance and capital ratios:					
Return on average assets	0.75%	0.72%	0.29%	0.29%	0.57%
Return on average shareholders' equity	7.55%	7.12%	2.61%	2.71%	5.70%
Net interest margin (a)	4.57%	3.89%	3.81%	3.36%	3.47%
Average shareholders' equity to average total assets	9.91%	10.13%	11.11%	10.83%	9.99%
Year-end capital to year-end risk-weighted assets:					
Tier 1	11.92%	11.63%	11.52%	13.75%	13.57%
Total	13.20%	13.51%	12.74%	15.51%	15.07%
Year-end Tier 1 leverage ratio	9.74%	8.96%	9.41%	10.35%	9.54%
Cash dividends declared to net income	48.98%	45.97%	121.17%	109.96%	50.80%
ASSET QUALITY RATIOS:					
Allowance for loan losses, at year-end to:					
Gross loans	1.20%	1.35%	1.59%	1.83%	1.74%
Nonperforming, restructured and past-due loans	54.93%	209.50%	132.05%	151.37%	111.68%
Net charge-offs to average gross loans	0.08%	0.06%	0.08%	0.09%	0.13%
Nonperforming assets as a percent of period-end gross loans and foreclosed real estate	2.19%	0.64%	1.20%	1.26%	1.67%

(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, collectability 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 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 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 Securities and Exchange Commission, including the Quarterly Reports on Form 10-Q to be filed by the Company in 2007.

BUSINESS AND OVERVIEW

The Company is a bank holding company headquartered in Baltimore, Maryland with one wholly-owned subsidiary, Carrollton 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.

The Bank sponsors national retailers who accept ATM cards for purchases in various electronic networks. Effective January 22, 2006, the agreement with Wal-Mart for the Bank to provide ATMs at Wal-Mart, Sam's Club, and Wal-Mart Supercenters in Maryland, Virginia and West Virginia was terminated.

During 2006, total assets decreased \$10.6 million to \$349.8 million due mainly to the a reduction in cash and cash equivalents that was used to pay off \$18.0 million of Federal Home Loan Bank of Atlanta (FHLBA) advances. Partially offsetting this decrease was an \$8.4 million or 5% increase in commercial loans that were funded primarily by the increase in deposits. The Company's loans held for sale portfolio, which consists of residential mortgage loans originated by CMSI and held for sale, usually within 30 days of origination, decreased 45.6% due to the slow down in the residential housing market.

Net income for the year ended December 31, 2006 totaled \$2.6 million compared to \$2.5 million for the prior year, a 5% increase. The earnings were significantly affected by recording 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 \$2.2 million from the sale of equity securities. The earnings for the year ended December 31, 2005 included security gains of \$840,000 from the sale of equity securities, a \$506,000 charge representing a penalty for the prepayment of a \$5 million FHLBA advance at 7.26% maturing May 24, 2010, and the write down and cost of disposal of ATMS totaling \$563,000 related to the termination of the Wal-Mart agreement. Wal-Mart terminated the agreement for Carrollton Bank to provide automated teller machines (ATMs) at Wal-Mart, Sam's Club and Wal-Mart Supercenters in Maryland, Virginia and West Virginia. The Company is asset sensitive and as a result of the increasing interest rate environment of 2006 and the increase in average interest earning assets of \$15.1 million from 2005 to 2006, net interest income increased 23% for 2006 compared to 2005. Noninterest income excluding the gains on the sales of securities of \$2.2 million in 2006 and \$840,000 in 2005 decreased 32% compared to 2005. The decrease was due primarily to the \$3.0 million decrease in ATM and Point of Sale revenue relating to the termination of the Wal-Mart ATM agreement.

The Company expects to open its newest retail branch in Cockeysville, Maryland in the second quarter of 2007.

Based upon current earnings and encouraging prospects for future earnings, the Company paid dividends of \$0.45 per share to shareholders during 2006.

RESULTS OF OPERATIONS

SUMMARY

The Company reported net income for 2006 of \$2.6 million or \$0.90 per diluted share, representing a 5% increase from 2005 net income of \$2.5 million or \$0.87 per share.

The loan portfolio net of the Allowance for Loan Losses and including loans held for sale, increased 2.3% to \$264.4 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 decreased 45.6% to \$7.5 million due to the slow down in the residential housing market. Interest income on loans, including loans held for sale, increased 19.1% due to average loans, including loans held for sale, increasing \$14.9 million and loans repricing to higher rates.

The deposit portfolio increased 2.3% to \$277.9 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 2006, due primarily to a \$24.7 million increase in average interest-bearing deposits and the yield on interest-bearing deposits increasing 96 basis points.

Noninterest income decreased 17.0% in 2006 compared to 2005, due primarily to a \$3.0 million decrease in ATM and Point of Sale revenue relating to the termination of the Wal-Mart ATM agreement and partially offset by the \$1.3 million increase in the gain on the sale of securities.

Noninterest expense increased 4.0% in 2006 compared to 2005. The increase was due to the \$1.8 million charge from the check kiting scheme by one of the Bank's commercial customers and the \$1.7 million increase in the prepayment penalty for restructuring a FHLBA advance partially offset by the elimination of personnel, transaction fees, and other operating expenses as well as a write down of \$563,000 in 2005 related to the termination of the Wal-Mart ATM agreement.

The Company reported net income for 2005 of \$2.5 million or \$0.87 per diluted share, representing a 177% increase from 2004 net income of \$888,000, or \$0.31 per diluted share.

The loan portfolio, including loans held for sale, increased 14.1% during 2005 to \$258.3 million, a result of the Company's continuing efforts to re-align the loan portfolio to be more in line with typical commercial banks. Interest income increased 23.9% due to loans increasing \$31.9 million and loans repricing to higher rates. The deposit portfolio increased 20.3% to \$271.6 million, with the majority of the growth derived from noninterest bearing deposits, money market accounts and certificates of deposit. Interest expense increased during 2005, due primarily to a \$32.5 million increase in interest-bearing deposits and the yield on interest bearing deposits increasing 80 basis points.

Noninterest income increased 22.1% in 2005 compared to 2004, due primarily to a 625% or \$724,000 increase in gains on sales of securities, an increase of 41% or \$788,000 in fees and commissions earned by CMSI, a 3% or \$133,000 increase in the Electronic Banking Division's revenue, and a 14% or \$134,000 increase in service charges.

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 Federal Reserve Board, 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

	2006			2005			2004		
	<i>Average Balance</i>	<i>Interest</i>	<i>Yield</i>	<i>Average Balance</i>	<i>Interest</i>	<i>Yield</i>	<i>Average Balance</i>	<i>Interest</i>	<i>Yield</i>
ASSETS									
Federal funds sold and Federal Home Loan Bank deposit	\$ 7,839,525	\$ 382,625	4.88%	\$ 19,067,206	\$ 623,910	3.27%	\$ 8,606,166	\$ 116,899	1.36%
Federal Home Loan Bank stock	1,742,153	99,046	5.69	2,643,019	109,616	4.15	2,261,207	80,737	3.57
Investment securities: (a)									
U.S. government agency	15,316,293	788,538	5.15	20,306,719	560,887	2.76	28,566,496	674,774	2.36
State and municipal	8,734,211	544,815	6.24	4,027,933	264,620	6.57	4,549,377	287,890	6.33
Mortgage-backed securities	21,554,754	1,170,089	5.43	11,089,402	611,055	5.51	8,747,456	479,546	5.48
Corporate bonds	4,089,963	270,840	6.62	1,277,192	70,749	5.54	4,592,680	274,845	5.98
Other	1,154,060	49,212	4.26	1,877,280	135,232	7.20	3,732,303	175,442	4.70
	<u>50,849,281</u>	<u>2,823,494</u>	5.55	<u>38,578,526</u>	<u>1,642,543</u>	4.26	<u>50,188,312</u>	<u>1,892,497</u>	3.77
Loans:									
Demand and time	73,339,911	5,862,743	7.99	67,134,231	3,554,951	5.30	49,920,788	2,783,558	5.58
Residential mortgage (b)	72,131,409	3,926,413	5.44	74,654,896	4,613,621	6.18	68,431,096	4,090,660	5.98
Commercial mortgage and construction	110,899,759	8,544,541	7.70	97,985,886	8,298,411	8.47	86,429,102	6,193,969	7.17
Installment	1,504,253	80,978	5.38	1,813,896	154,258	8.50	2,414,072	209,275	8.67
Lease financing	1,429,551	80,889	5.66	2,782,231	214,524	7.71	4,024,469	320,885	7.97
	<u>259,304,883</u>	<u>20,044,135</u>	7.73	<u>244,371,140</u>	<u>16,835,765</u>	6.89	<u>211,219,527</u>	<u>13,598,347</u>	6.44
Total interest-earning assets	319,735,842	23,349,301	7.30	304,659,891	19,211,834	6.31	272,275,212	15,688,480	5.76
Noninterest-bearing cash	14,651,700			26,624,448			21,682,244		
Premises and equipment	5,432,452			5,694,687			4,959,453		
Other assets	7,993,335			4,034,529			7,858,307		
Allowance for loan losses	(3,287,376)			(3,472,722)			(3,616,474)		
Unrealized gains on available for sale securities, net	1,065,683			3,412,785			3,174,905		
	<u>\$345,591,636</u>			<u>\$340,953,618</u>			<u>\$306,333,647</u>		
LIABILITIES AND SHAREHOLDERS' EQUITY									
Interest-bearing deposits:									
Savings and NOW	\$ 62,309,713	147,770	0.24%	\$ 67,931,566	162,865	0.24%	\$ 71,404,510	180,741	0.25%
Money market	51,303,354	1,936,266	3.77	40,658,604	998,161	2.45	29,186,544	322,785	1.11
Certificates of deposit	101,071,899	4,521,369	4.47	81,412,306	2,861,697	3.52	61,370,913	1,627,239	2.65
	<u>214,684,966</u>	<u>6,605,404</u>	3.08	<u>190,002,476</u>	<u>4,022,723</u>	2.12	<u>161,961,967</u>	<u>2,130,765</u>	1.32
Borrowed funds	38,900,240	2,132,046	5.48	54,879,637	3,352,360	6.11	56,153,768	3,190,857	5.68
Total interest-bearing liabilities	253,585,206	8,737,451	3.45	244,882,113	7,375,083	3.01	218,115,735	5,321,622	2.44
Noninterest-bearing deposits	56,441,180			59,645,770			51,501,352		
Other liabilities	1,312,259			1,885,164			2,674,734		
Shareholders' equity	<u>34,252,991</u>			<u>34,540,571</u>			<u>34,041,826</u>		
Total liabilities and shareholders' equity	<u>\$345,591,636</u>			<u>\$340,953,618</u>			<u>\$306,333,647</u>		
Net interest margin (c)	<u>\$319,735,842</u>	<u>\$14,611,850</u>	4.57%	<u>\$304,659,891</u>	<u>\$11,836,751</u>	3.89%	<u>\$272,275,212</u>	<u>\$10,366,858</u>	3.81%

(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 7% (or a combined federal and state rate of 38.62%) 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 increased to \$14.6 million for the year ended December 31, 2006 compared to \$11.8 million for 2005. The increase in tax-equivalent net interest income during 2006 was due to a \$15.1 million increase in average interest-earning assets during 2006 compared to 2005 and an increase in the yield on interest-earning assets of 99 basis points.

The \$14.9 million or 6.1% increase in average loans outstanding is attributed to the Company's active business development efforts in its commercial loan portfolio and general economic conditions of the Company's primary service market. The yield on loans increased to 7.73% in 2006 compared to 6.89% for 2005 as lower yielding loans repriced during the year to higher rates. The yield on investment securities also increased to 5.55% in 2006 from 4.26% in 2005. The net impact was a \$4.1 million or 21.5% increase in tax-equivalent interest income for the year ended December 31, 2006 compared to 2005.

In 2005, net interest income on a tax-equivalent basis increased to \$11.8 million for the year ended December 31, 2005 compared to \$10.4 million for 2004. The increase in tax-equivalent net interest income during 2005 was almost entirely due to a \$32.4 million increase in average earning assets during 2005 compared to 2004. An increase in average loans outstanding of \$33.2 million, or 15.7% and average federal funds sold of \$10.5 million or 121.6% was partially offset by a decline in average investment securities outstanding for the year of \$11.6 million.

The increase in average loans outstanding is attributed to the Company's active business development efforts in its commercial loan portfolio and general economic conditions of the Company's primary service market. Targeted short-term interest rates, as established by the Federal Reserve Bank, increased during 2005 resulting in the Company's yield on earning assets increasing 55 basis points to 6.31% for the year ended December 31, 2005 compared to 5.76% for the same period in 2004. The yield on loans increased to 6.89% in 2005 compared to 6.44% for 2004 as lower yielding loans repriced during the year to higher rates. The yield on investment securities also increased to 4.26% in 2005 from 3.77% in 2004. The net impact was a \$3.5 million or 22.4% increase in tax-equivalent interest income for the year ended December 31, 2005 compared to 2004.

Interest expense increased \$1.4 million to \$8.7 million in 2006 from \$7.4 million in 2005. Interest expense increased primarily due to a change in the deposit mix, with an increase in the amount of interest-bearing deposits partially offset by a decrease in borrowings. In addition, the cost of interest-bearing deposits increased from 2.12% in 2005 to 3.08% in 2006.

Interest expense on total interest-bearing liabilities increased \$1.4 million, or 18.5%, for the year ended December 31, 2006. The increase in interest expense was due to an \$8.7 million increase in average interest-bearing liabilities and the cost of interest-bearing liabilities increasing to 3.45% for the year ended December 31, 2006 compared to 3.01% for the same period in 2005.

The following table and the related discussions of interest income and interest expense provide further analysis of the changes in net interest income during 2005 and 2004:

	2006 Compared to 2005			2005 Compared to 2004		
	<i>Change Due to Variance In Rate(b)</i>	<i>Volume(b)</i>	<i>Total</i>	<i>Change Due to Variance In Rates(b)</i>	<i>Volume(b)</i>	<i>Total</i>
INTEREST INCOME						
Federal funds sold and interest-bearing deposits with other banks	\$ 126,216	\$ (367,145)	\$ (240,929)	\$ 364,757	\$ 142,254	\$ 507,011
Investment securities and FHLB stock	682,785	485,348	1,168,133	(55,017)	(166,058)	(221,075)
Loans (a)	<u>2,181,328</u>	<u>1,028,935</u>	<u>3,210,263</u>	<u>1,099,671</u>	<u>2,137,747</u>	<u>3,237,418</u>
TOTAL INTEREST EARNED	<u>2,990,329</u>	<u>1,147,138</u>	<u>4,137,467</u>	<u>1,409,411</u>	<u>2,113,943</u>	<u>3,523,354</u>
INTEREST EXPENSE						
Deposits	2,060,511	523,269	2,583,779	1,501,020	390,938	1,891,958
Borrowings	<u>(245,072)</u>	<u>(976,341)</u>	<u>(1,221,413)</u>	<u>216,307</u>	<u>(54,804)</u>	<u>161,503</u>
TOTAL INTEREST EXPENSE	<u>1,815,439</u>	<u>(453,072)</u>	<u>1,362,367</u>	<u>1,717,327</u>	<u>336,134</u>	<u>2,053,461</u>
NET INTEREST INCOME	<u>\$1,174,890</u>	<u>\$1,600,210</u>	<u>\$ 2,775,100</u>	<u>\$ (307,916)</u>	<u>\$1,777,809</u>	<u>\$1,469,893</u>

(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.

The Company continues to experience strong asset quality in its loan portfolio with a low delinquency rate and a low charge off rate. The Company did not provide for any loan losses for the years ended December 31, 2006 and 2005. Nonaccrual, restructured and delinquent loans over 90 days to total loans increased to 2.19% at the end of 2006 compared to 0.64% in 2005. The ratio of net loan losses to average loans increased in 2006 to 0.08 % compared to 0.06% for 2005.

The Company did not provide for any loan losses for the years ended December 31, 2005 and 2004. Nonaccrual, restructured, and delinquent loans over 90 days to total loans improved to 0.64% at the end of 2005 compared to 1.20% in 2004. The ratio of net loan losses to average loans decreased in 2005 to 0.06% compared to 0.08% for 2004.

NONINTEREST INCOME

Noninterest income decreased from \$10.7 million during 2005 to \$8.9 million in 2006 due primarily to the \$3.0 million decrease in ATM and Point of Sale revenue relating to the termination of the Wal-Mart ATM agreement and partially offset by the \$1.3 million increase in the gain on the sale of securities. The decrease in net gains and fees on sales of mortgage loans corresponded to a decrease in the volume of mortgage loans sold during the year due to a slow down in the residential housing market. 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. Through December 31, 2005, the Company maintained ATMs in Wal-Mart stores in Maryland, Virginia and West Virginia, as well as at its branches. Effective January 22, 2006, the agreement with Wal-Mart for the Bank to provide ATM services at its locations in Maryland, Virginia and West Virginia was terminated. The fees from the ATMs represent approximately 8% of total electronic banking revenue in 2006. 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 78% 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 income increased from \$8.8 million during 2004 to \$10.7 million in 2005 due, in large part, to increases in gains and fees recognized on the sale of mortgage loans, net of costs, gains on security sales, increases in Electronic Banking division's revenues and increases in fees charged for deposit services. Specifically, net gains and fees on sales of mortgage loans increased \$788,000 or 41.1% from 2004 to 2005, gains on sales of securities increased \$724,000 or 625.2%, the Electronic Banking Division's revenue increased \$133,000 or 2.7% and deposit service charges increased by \$134,000 or 14.2%. Brokerage commissions also increased \$44,000 or 7.0%. The increase in net gains and fees on sales of mortgage loans corresponded to an increase in the volume of mortgage loans sold during the year, from \$129.7 million in 2004 to \$183.1 million in 2005. The Company believes that this increase in mortgage loan volume was primarily attributable to the market, in general, and expanding the operations of the mortgage company in 2004. The gain on sale of securities increased \$724,000 due to the Company taking some profits on equity investments in 2005.

Electronic banking income is comprised of three sources: national point of sale ("POS") sponsorships, ATM fees, and check card fees. Through December 31, 2005, the Company maintained ATMs in Wal-Mart stores in Maryland, Virginia and West Virginia, as well as at its branches. The fees from these ATMs represent approximately 39% of total electronic banking revenue in 2005. 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 41% of total electronic banking revenue. Fees from check cards comprise the remaining 20% of electronic banking revenue. On September 22, 2005, Wal-Mart notified the Bank of its intention to terminate the agreement for the Company to provide ATM services at its locations in Maryland, Virginia and West Virginia. The effective date of the termination was January 22, 2006.

During 2004, the Company opened a mortgage subsidiary CMSI. Our mortgage-banking business is structured to provide a source of fee income largely from the process of originating residential mortgage loans for sale on the secondary market, as well as the origination of loans to be held in our loan portfolio. Mortgage-banking products include Federal Housing Administration ("FHA") and the federal Veterans Administration ("VA") loans, conventional and nonconforming first and second mortgages, and construction and permanent financing.

NONINTEREST EXPENSES

Noninterest expense consists primarily of costs associated with personnel, occupancy and equipment, data processing, marketing and professional fees. The Company's noninterest expense for the year ended December 31, 2006 totaled \$19.4 million, representing an increase of \$747,000, or 4.0%, as compared to 2005. The increase was due to the \$1.8 million charge from the check kiting scheme by one of the Bank's commercial customers and the \$1.7 million increase in the prepayment penalty for restructuring a FHLBA advance partially offset by the elimination of personnel, transaction fees, other operating expenses as well as a write down of \$563,000 in 2005 related to the termination of the Wal-Mart agreement.

During 2005 noninterest expenses increased by \$883,000, or 5.0% to \$18.6 million compared to \$17.8 million in 2004.

Salaries, the largest component of noninterest expense increased \$607,000 or 8.9% from 2004 to 2005 due to merit increases and the opening of a new branch in the North Bel Air area of Harford County and were partially offset by a decrease in the average number of fulltime equivalent employees from 165 in 2004 to 157 in 2005. Employee benefits decreased by \$532,000 due to freezing the defined benefit pension plan effective December 31, 2004.

Occupancy costs increased \$247,000 or 15.4% from 2004 to 2005 due to the opening of the new branch in Harford County and normal lease payment escalations and costs to maintain business properties. Furniture and equipment expense decreased \$379,000 or 23.8% due to the original cost of the ATM network being fully depreciated in 2004.

In 2005, the Company had non-recurring charges of \$563,000 related to the termination of the Wal-Mart agreement, and \$506,000 representing a penalty for the prepayment of a \$5.0 million FHLBA advance at 7.26% maturing May 24, 2010. In 2004, there was a non-recurring charge of \$497,000 related to the write down of FHLMC stock.

Other noninterest expense increased \$368,000 or 6.9% from 2003 to 2004 due to increases in marketing expenses related to opening the new branch in Harford County, amortization of software acquired, increased data processing services due to growth in loans and deposits, increased loan expenses related to CMSI, and professional fees partially offset by decreases in various other expenses.

INCOME TAX PROVISION

Income tax expense was \$1.3 million in 2006 and 2005 and \$320,000 in 2004. The effective tax rate was 33.9% in 2006, 35.0% in 2005 and 26.5% in 2004. The effective tax rates fluctuate from year to year due to changes in the mix of tax-exempt loans and investments as a percentage of total loans and investments. During 2005, a lower percentage of the Company's pre-tax income was exempt from taxes compared to 2004. During 2006, the Company purchased additional tax exempt securities, which reduced the effective tax rates.

FINANCIAL CONDITION

SUMMARY

Total assets of the Company decreased by 3.0% to \$349.8 million at December 31, 2006 from \$360.5 million at December 31, 2005. Investment securities increased 15.7% to \$55.1 million at December 31, 2006. Gross loans, excluding loans held for sale, increased by 4.9% to \$260.0 million at December 31, 2006 compared to \$247.9 million at the end of 2005. Interest-earning assets increased \$2.4 million to \$327.1 million and were 93.5% of total assets at December 31, 2006.

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:

	2006	2005	2004	2003	2002
AVAILABLE FOR SALE					
U.S. Government agency	\$ 9,363,760	\$ 10,740,335	\$ 19,913,790	\$ 34,566,285	\$ 44,866,333
Mortgage-backed securities	12,725,553	8,490,125	8,447,886	9,628,267	17,008,728
State and municipal bonds	5,724,959	3,689,859	4,137,433	5,197,716	5,446,260
Corporate bonds	5,621,529	1,514,471	3,036,920	6,820,340	7,962,805
Subtotal	33,709,801	24,434,790	35,536,029	56,212,608	75,284,126
Equity securities	2,224,846	4,660,213	6,952,463	6,246,349	3,502,021
Total available for sale	<u>35,934,647</u>	<u>29,095,003</u>	<u>42,488,492</u>	<u>62,458,957</u>	<u>78,786,147</u>
HELD TO MATURITY					
U.S. Government agency	6,456,069	5,000,000	—	—	—
Mortgage-backed securities	8,761,200	9,575,713	—	—	—
State and municipal bonds	3,912,704	3,912,692	—	—	—
Equity securities	—	—	—	25,000	25,000
Total held to maturity	<u>19,129,973</u>	<u>18,488,405</u>	<u>—</u>	<u>25,000</u>	<u>25,000</u>
Total investment securities	<u>\$55,064,620</u>	<u>\$47,583,408</u>	<u>\$42,488,492</u>	<u>\$62,483,957</u>	<u>\$78,811,147</u>

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, 2006:

Maturing	Available for Sale			Held to Maturity		
	Amortized Cost	Fair Value	Yield	Amortized Cost	Fair Value	Yield
Within one year	\$ 2,000,000	\$ 1,985,620	3.05%	\$ —	\$ —	—%
Over one to five years	4,923,172	4,924,303	4.96	—	—	—
Over five to ten years	3,928,823	3,958,428	4.91	8,414,510	8,324,424	4.93
Over ten years	10,120,600	10,115,897	5.83	1,954,263	1,941,379	5.73
	20,972,595	20,984,248		10,368,773	10,265,803	
Mortgage-backed securities	12,712,231	12,725,553	5.82	8,761,200	8,624,465	4.96
Equity securities	1,140,856	2,224,846	2.40	—	—	—
	<u>\$34,825,682</u>	<u>\$35,934,647</u>		<u>\$19,129,973</u>	<u>\$18,890,268</u>	

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 \$7.5 million to \$55.1 million at December 31, 2006 compared to \$47.6 million at December 31, 2005. The increase was due to purchases of mortgage backed securities and state and municipal bonds. In 2004, the Company recognized a \$497,000 other-than-temporary impairment of the Company's investment in FMLMC preferred stock.

LOANS

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

	2006	2005	2004	2003	2002
Real Estate:					
Residential	\$ 55,057,625	\$ 53,148,211	\$ 55,242,018	\$ 57,586,028	\$ 79,520,154
Commercial	120,397,988	97,909,115	94,858,597	82,856,038	78,500,418
Construction and land development	29,996,306	37,415,478	17,774,874	16,275,828	7,664,367
Demand and time	51,549,802	56,118,527	46,168,587	35,978,633	32,444,790
Lease financing	969,113	1,936,482	3,598,003	4,449,408	4,343,539
Installment	2,030,480	1,415,260	2,084,215	2,150,626	2,746,858
	260,001,314	247,943,073	219,726,294	199,296,561	205,220,126
Allowance for loan losses	3,131,021	3,337,163	3,485,076	3,648,245	3,578,762
Loans, net	<u>\$256,870,293</u>	<u>\$244,605,910</u>	<u>\$216,241,218</u>	<u>\$195,648,316</u>	<u>\$201,641,364</u>

Gross loans, excluding loans held for sale, increased \$12.1 million or 4.9% from \$247.9 million as of December 31, 2005 to \$260.0 million as of December 31, 2006. The increase was primarily in commercial lending including commercial construction and land development. Commercial loans amounted to \$202.9 million at December 31, 2006 and were 78% of total loans. Consumer loans amounted to \$57.1 million and were 22% of total loans.

The following table shows the contractual maturities and interest rate sensitivities of the Company's loans at December 31, 2006. 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						Total
	In one year or less		After 1 through 5 years		After 5 years		
	Fixed	Variable	Fixed	Variable	Fixed	Variable	
Real Estate:							
Residential	\$ 185,032	\$ 741,011	\$ 1,417,229	\$ —	\$ 16,074,707	\$ 36,639,646	\$ 55,057,625
Commercial	13,387,834	11,053,853	73,766,392	841,931	18,693,031	2,654,947	120,397,988
Construction and land development	10,882,428	7,408,186	380,673	4,235,920	6,944,049	145,050	29,996,306
Demand and time	1,335,962	31,720,178	10,735,337	6,036,889	1,142,042	579,394	51,549,802
Lease financing	216,151	—	752,962	—	—	—	969,113
Installment	935,382	15,717	258,766	281,791	301,761	237,063	2,030,480
	<u>\$26,942,789</u>	<u>\$50,938,945</u>	<u>\$87,311,359</u>	<u>\$11,396,531</u>	<u>\$43,155,590</u>	<u>\$40,256,100</u>	<u>\$260,001,314</u>

The following table provides information concerning nonperforming assets and past due loans at December 31, 2006:

	2006	2005	2004	2003	2002
Nonaccrual loans (a)	\$3,699,397	\$1,413,925	\$ 615,394	\$ 712,116	\$ 734,879
Restructured loans	180,686	—	455,864	661,974	568,969
Foreclosed real estate	1,383,163	—	—	100,000	218,654
	<u>\$5,263,246</u>	<u>\$1,413,925</u>	<u>\$1,071,258</u>	<u>\$1,474,090</u>	<u>\$1,522,502</u>
Accruing loans past-due 90 days or more	<u>\$ 436,599</u>	<u>\$ 179,012</u>	<u>\$1,567,919</u>	<u>\$1,036,018</u>	<u>\$1,900,663</u>

(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 \$534,639, \$77,744, and \$143,374 as of December 31, 2006, 2005 and 2004, 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 \$2,001,000, \$2,319,000, and \$2,559,000 as of December 31, 2006, 2005 and 2004, 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, 2002 through 2006, 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.

<i>Description</i>	Years ended December 31				
	<i>2006</i>	<i>2005</i>	<i>2004</i>	<i>2003</i>	<i>2002</i>
Balance at beginning of year	\$3,337,163	\$3,485,076	\$3,648,245	\$3,578,762	\$3,338,807
Charge-offs:					
Demand and time	—	123,578	192,440	200,173	21,904
Lease financing	154,747	168,823	—	—	—
Real estate:					
Residential	—	—	7,746	16,898	160,591
Commercial	59,120	—	—	—	112,718
Construction	—	—	—	—	—
Installment	41,967	22,640	76,936	47,957	85,393
	<u>255,834</u>	<u>315,041</u>	<u>277,122</u>	<u>265,028</u>	<u>380,606</u>
Recoveries:					
Demand and time	—	130,904	67,111	58,034	2,475
Lease financing	16,530	3,980	—	—	—
Real estate:					
Residential	—	14,874	8,087	—	67,705
Commercial	6,290	—	—	—	—
Construction	—	—	—	—	—
Installment	26,872	17,370	38,755	33,477	24,381
	<u>49,692</u>	<u>167,128</u>	<u>113,953</u>	<u>91,511</u>	<u>94,561</u>
Net charge-offs	<u>206,142</u>	<u>147,913</u>	<u>163,169</u>	<u>173,517</u>	<u>286,045</u>
Provision charged to operations	—	—	—	243,000	526,000
Balance at end of the year	<u>\$3,131,021</u>	<u>\$3,337,163</u>	<u>\$3,485,076</u>	<u>\$3,648,245</u>	<u>\$3,578,762</u>
Ratio of net charge-offs to average loans outstanding	<u>0.08%</u>	<u>0.06%</u>	<u>0.08%</u>	<u>0.09%</u>	<u>0.13%</u>

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.

The following table presents the allocation of the allowance for loan losses among the various loan categories at December 31:

<i>Portfolio</i>	<i>2006</i>	<i>2005</i>	<i>2004</i>	<i>2003</i>	<i>2002</i>
Demand and time and lease financing	\$ 922,612	\$ 474,059	\$ 589,053	\$1,226,447	\$ 733,560
Real estate:					
Residential	409,684	718,028	587,292	831,173	754,979
Commercial	923,453	679,002	1,034,546	1,041,834	876,243
Construction and land development	230,072	382,204	342,114	—	—
Installment	49,399	143,318	149,271	133,865	94,162
Unallocated	595,801	940,552	782,800	414,926	1,119,818
	<u>\$3,131,021</u>	<u>\$3,337,163</u>	<u>\$3,485,076</u>	<u>\$3,648,245</u>	<u>\$3,578,762</u>

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

<i>Portfolio</i>	<i>2006</i>	<i>2005</i>	<i>2004</i>	<i>2003</i>	<i>2002</i>
Demand and time and lease financing	20.2%	23.4%	22.7%	20.2%	17.9%
Real estate:					
Residential	21.2	21.4	25.1	28.9	38.8
Commercial	46.3	39.6	43.2	41.6	38.2
Construction and land development	11.5	15.1	8.1	8.2	3.8
Installment	0.8	0.5	0.9	1.1	1.3
	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>

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

At December 31, 2006, the allowance for loan losses was \$3.1 million, a 6.2% decrease from the end of 2005. The ratio of the allowance to total loans was 1.20% at December 31, 2006 and 1.35% at December 31, 2005. The ratio of net loan losses to average loans outstanding for 2006 was 0.08% compared to 0.06% for 2005. The ratio of nonaccrual loans, restructured loans and loans delinquent more than 90 days to total loans increased to 2.19% at December 31, 2006 from 0.64% at the end of 2005. The ratio of real estate loans to total loans increased to 79.0% at the end of 2006 from 76.1% at the end of 2005.

FUNDING SOURCES

DEPOSITS

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

	2006		2005		2004	
	<i>Average Balance</i>	<i>Average Rate</i>	<i>Average Balance</i>	<i>Average Rate</i>	<i>Average Balance</i>	<i>Average Rate</i>
Noninterest-bearing deposits	\$ 56,441,180	—%	\$ 59,645,770	—%	\$ 51,501,352	—%
Interest-bearing deposits:						
NOW accounts	32,038,917	0.21	34,384,963	0.21	35,016,262	0.21
Savings accounts	30,270,796	0.27	33,546,603	0.27	36,388,248	0.29
Money market accounts	51,303,354	3.77	40,658,604	2.45	29,186,544	1.11
Certificates of deposit	101,071,899	4.47	81,412,306	3.52	61,370,913	2.65
	<u>\$271,126,146</u>	<u>2.44</u>	<u>\$249,648,246</u>	<u>1.61</u>	<u>\$213,463,319</u>	<u>1.00</u>

The following table provides the maturities of certificates of deposit of the Company in amounts of \$100,000 or more at December 31, 2006:

Maturing in:	
3 months or less	\$12,945,360
Over 3 months through 6 months	4,514,815
Over 6 months through 12 months	7,588,860
Over 12 months	4,518,886
	<u>\$29,567,921</u>

Total deposits at December 31, 2006 increased by \$6.3 million to \$277.9 million from the end of 2005. Interest bearing accounts increased by \$23.2 million and noninterest-bearing deposits decreased by \$16.9 million.

The Company began offering CDARS deposits to its customers during 2004. This program allows for customers that wish to invest more than the amounts that would normally be covered by FDIC insurance with the Bank. The program is a nationwide one 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. As of December 31, 2006, the Bank had approximately \$9.2 million in CDARS deposits, a decrease of \$12.2 million from December 31, 2005.

BORROWED FUNDS

Borrowed funds consist of securities sold under repurchase agreements, federal funds purchased and borrowings from the FHLB and notes payable-U.S. Treasury. 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. Notes payable-U.S. Treasury are U.S. Treasury and Federal Treasury Tax and Loan deposits accepted by the Bank from its customers to be remitted to the Federal Reserve on a periodic basis.

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

	<i>Maturity Date</i>	<i>2006</i>	<i>2005</i>	<i>2004</i>
Amount outstanding at year-end:				
Federal Home Loan Bank	March 26, 2008	\$ 5,000,000	\$ 5,000,000	\$ 5,000,000
Federal Home Loan Bank	February 2, 2010	—	35,000,000	35,000,000
Federal Home Loan Bank	May 24, 2010	—	—	5,000,000
Federal Home Loan Bank	Daily Rate Credit	17,000,000	—	—
		<u>\$22,000,000</u>	<u>\$40,000,000</u>	<u>\$45,000,000</u>
Federal funds purchased and securities sold under repurchase agreements				
		\$ 13,405,463	\$ 9,280,348	\$ 10,183,951
Notes-payable — U.S. Treasury				
		—	\$ 1,932,124	\$ 1,984,714
Weighted average interest rate at year-end:				
Advances from the FHLB		5.43%	6.67%	6.84%
Federal funds purchased and securities sold under repurchase agreements				
		4.86%	3.59%	1.91%
Notes payable — U.S. Treasury				
		—	4.17%	1.97%
Maximum outstanding at any month-end:				
Advances from the FHLB		\$40,000,000	\$45,000,000	\$45,000,000
Federal funds purchased and securities sold under repurchase agreements				
		13,405,463	11,742,108	13,540,231
Notes payable — U.S. Treasury				
		1,432,463	1,958,750	2,008,989
Average balance outstanding during the year:				
Advances from the FHLB		\$24,603,287	\$44,876,712	\$45,000,000
Federal funds purchased and securities sold under repurchase agreements				
		9,040,071	8,986,714	10,102,501
Notes payable — U.S. Treasury				
		185,067	1,016,211	1,051,267
Weighted average interest rate during the year:				
Advances from the FHLB		5.38%	6.84%	6.84%
Federal funds purchased and securities sold under repurchase agreements				
		4.66%	2.66%	0.96%
Notes payable — U.S. Treasury				
		4.18%	3.06%	1.10%

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%. Debt retirement expense of \$505,839 was incurred in 2005 due to the prepayment of a \$5.0 million FHLB advance that had a maturity date of May 24, 2010 and an interest rate of 7.26%.

The Company may borrow under available unsecured federal funds lines 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, 2006 and 2005. These lines bear interest at the current federal funds rate of the correspondent bank.

CAPITAL

Bank holding companies and banks are required by the Federal Reserve 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 Federal Reserve 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, 2006 and 2005. 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
	<i>Minimum</i>	<i>2006</i>	<i>2006</i>
Leverage ratio	4%	9.74%	9.30%
Risk-based capital:			
Tier 1 (Core)	4%	11.92%	11.48%
Total	8%	13.20%	12.60%

Total shareholders' equity increased 0.2% to \$34.7 million at December 31, 2006. Earnings of the Company of \$2.6 million for the year ended December 31, 2006 and the proceeds and the tax benefit from the exercise of stock options of \$52,000 were offset by dividends of \$1.3 million, repurchase of shares totaling \$129,000, and the reduction in unrealized gains on available for sale securities of \$1.2 million due to the realization of the \$2.2 million gain on the sale of equity securities.

LIQUIDITY AND CAPITAL EXPENDITURES

CAPITAL EXPENDITURES

Capital expenditures were approximately \$901,000 in 2006, \$902,000 in 2005, and \$1.9 million in 2004. 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 in 2005 were due to renovations at several branches and normal business activity. The capital expenditures in 2004 were principally due to the expenditures required to open the Company's new branch in January 2005.

Capital expenditures are projected to be approximately \$1.2 million for fiscal year 2007 for renovations at five of the Company's branch locations and the costs to complete construction of a new branch.

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 \$43.8 million or 12.5% of total assets at December 31, 2006.

The borrowing requirements of customers include commitments to extend credit and the unused portion of lines of credit, which totaled \$132.0 million at December 31, 2006. Of this total, management places a high probability of required funding within one year on approximately \$72.6 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 established lines of credit totaling \$80.0 million with the Federal Home Loan Bank of Atlanta (the "FHLB") as an additional source of liquidity. At December 31, 2006, the Company had \$22.0 million outstanding with the FHLB and had \$50.1 million collateral available to borrow under the line of credit. Additionally, the Company has available unsecured federal funds lines of credit of \$5.0 million and a secured

federal funds line of credit of \$5.0 million with other institutions. There was no balance outstanding under these lines at December 31, 2006. The lines bear interest at the current federal funds rate of the correspondent bank.

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, 2006, 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 US 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, 2005. 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, 2006 in which assets and liabilities reprice:

<i>(Dollars in thousands)</i>	<i>0 to 90</i> <i>days</i>	<i>91 to 365</i> <i>days</i>	<i>1 to 2</i> <i>years</i>	<i>3 to 5</i> <i>years</i>	<i>> 5</i> <i>years</i>
ASSETS:					
Short term investments	\$ 3,990	\$ —	\$ —	\$ —	\$ —
Investment securities	9,329	5,374	5,082	15,403	19,876
Loans held for sale	7,489	—	—	—	—
Loans:					
Residential real estate	30,682	1,915	3,088	6,105	13,268
Commercial real estate	20,570	13,436	22,983	50,357	13,052
Construction and land development	16,545	6,178	301	79	6,893
Demand and time	35,606	840	738	9,998	4,368
Lease financing	19	197	325	428	—
Installment	487	38	72	212	1,221
	<u>\$124,717</u>	<u>\$ 27,978</u>	<u>\$ 32,589</u>	<u>\$ 82,582</u>	<u>\$ 58,678</u>
LIABILITIES:					
Deposits	\$ 93,786	\$ 53,327	\$ 13,866	\$ 7,665	\$109,259
Borrowings	30,405	—	5,000	—	—
	<u>\$124,191</u>	<u>\$ 53,327</u>	<u>\$ 18,866</u>	<u>\$ 7,665</u>	<u>\$109,259</u>
Gap position					
Period	\$ (526)	\$ (25,349)	\$ 13,723	\$ 74,917	\$ (50,581)
% of assets	(0.15)%	(7.25)%	3.92%	21.42%	(14.46)%
Cumulative	\$ (526)	\$ (24,823)	\$ (11,100)	\$ 63,817	\$ 13,236
% of assets	(0.15)%	(7.10)%	(3.17)%	18.24%	3.78%
Cumulative risk sensitive assets to risk sensitive liabilities	100.42%	52.46%	172.74%	1,077.39%	53.71%

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 2006, 2005, and 2004.

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, 2006:

Loan commitments	\$40,463,996
Unused lines of credit	91,563,387
Letters of credit	2,223,755

CONTRACTURAL OBLIGATIONS

The Company enters into contractual obligations in the normal course of business. Among these obligations are short and long-term FHLB 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, 2006.

<i>Contractual Obligations (Dollars in thousands)</i>	<i>Total</i>	<i>Less than 1 year</i>	<i>One to three years</i>	<i>Three to five years</i>	<i>More than five years</i>
Federal Home Loan Bank	\$22,000	\$17,000	\$5,000	\$ —	\$ —
Federal fund purchased and securities sold under agreement to repurchase	13,405	13,405	—	—	—
Operating lease obligations	8,451	959	1,534	1,258	4,700
Purchase obligations(1)	1,971	987	595	389	—
Total	<u>\$45,827</u>	<u>\$32,351</u>	<u>\$7,129</u>	<u>\$1,647</u>	<u>\$4,700</u>

(1) Represents payments required under contract, based on average monthly charges for 2006 and assuming a growth rate of 3%, with the Company's current data processing service provider that expires in March 2011. Also includes estimated cost to complete construction of a new branch.

NEW ACCOUNTING PRONOUNCEMENTS

In February 2006, FASB issued SFAS 155, "Accounting for Certain Hybrid Financial Instruments", which permits, but does not require, fair value accounting for any hybrid financial instrument that contains an embedded derivative that would otherwise require bifurcation in accordance with SFAS 133, "Accounting for Derivative Instruments and Hedging Activities". The statement also subjects beneficial interests in securitized financial assets to the requirements of SFAS 133. This statement is effective for all financial instruments acquired, issued, or subject to remeasurement for fiscal years beginning after September 15, 2006. The Company does not expect that the adoption of this Statement will have a material impact on its financial position, results of operations or cash flows.

In March 2006, the FASB issued SFAS No. 156, "Accounting for Servicing of Financial Assets, and an amendment of FASB Statement No. 140." The statement amends SFAS No. 140 by (1) requiring the separate accounting for servicing assets and servicing liabilities, which arise from the sale of financial assets; (2) requiring all separately recognized serving assets and servicing liabilities to be initially measured at fair value, if practicable; and (3) permitting an entity to choose between an amortization method or a fair value method for subsequent

measurement for each class of separately recognized servicing assets and servicing liabilities. This statement is effective for fiscal years beginning after September 15, 2006, with earlier adoption permitted. The Company does not expect that the adoption of this Statement will have a material impact on its financial position, results of operations or cash flows.

In June 2006, the FASB issued FASB Interpretation No. 48 ("FIN 48"), *"Accounting for Uncertainty in Income Taxes."* This interpretation applies to all tax positions accounted for in accordance with SFAS No. 109, *"Accounting for Income Taxes."* FIN 48 clarifies the application of SFAS No. 109 by defining the criteria that an individual tax position must meet in order for the position to be recognized within the financial statements and provides guidance on measurement, de-recognition, classification, interest and penalties, accounting in interim periods, disclosure and transition for tax positions. This interpretation is effective for fiscal years beginning after December 15, 2006, with earlier adoption permitted. The Company has evaluated the impact of the adoption of this interpretation and has determined that it will not have a material impact on its financial position, results of operations or cash flows.

In September 2006, the FASB issued SFAS No. 157, *"Fair Value Measurements"*. This Statement defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. It clarifies that fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants in the market in which the reporting entity transacts. This Statement does not require any new fair value measurements, but rather, it provides enhanced guidance to other pronouncements that require or permit assets or liabilities to be measured at fair value. This Statement is effective for fiscal years beginning after November 15, 2007, with earlier adoption permitted. The Company does not expect that the adoption of this Statement will have a material impact on its financial position, results of operations or cash flows.

At its September 2006 meeting, the Emerging Issues Task Force ("EITF") reached a final consensus on Issue 06-04, *"Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements."* The consensus stipulates that an agreement by an employer to share a portion of the proceeds of a life insurance policy with an employee during the postretirement period is a postretirement benefit arrangement required to be accounted for under SFAS No. 106 or Accounting Principles Board Opinion ("APB") No. 12, "Omnibus Opinion - 1967." The consensus concludes that the purchase of a split-dollar life insurance policy does not constitute a settlement under SFAS No. 106 and, therefore, a liability for the postretirement obligation must be recognized under SFAS No. 106 if the benefit is offered under an arrangement that constitutes a plan or under APB No. 12, if it is not part of a plan. Issue 06-04 is effective for annual or interim reporting periods beginning after December 15, 2007. The Company does not have split-dollar life insurance policies and the adoption of this statement will not have a material effect on its financial position, results of operations or cash flows.

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, 2006 and 2005, and the related consolidated statements of income, changes in shareholders' equity, and cash flows for each of the three years ended December 31, 2006. 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, 2006 and 2005, and the results of their operations and their cash flows for each of the three years ended December 31, 2006, 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



Baltimore, Maryland
February 23, 2007

CONSOLIDATED BALANCE SHEETS

	December 31,	
	2006	2005
ASSETS		
Cash and due from banks	\$ 9,632,763	\$ 27,235,233
Federal funds sold and Federal Home Loan Bank deposit	3,990,003	11,855,332
Federal Home Loan Bank stock, at cost	1,704,500	2,431,600
Investment securities		
Available for sale	35,934,647	29,095,003
Held to maturity	19,129,973	18,488,405
Loans held for sale	7,489,290	13,767,109
Loans, less allowance for loan losses of \$3,131,021 and \$3,337,163	256,870,293	244,605,910
Premises and equipment	5,599,988	5,433,628
Accrued interest receivable	1,713,653	1,418,829
Prepaid income taxes	—	256,482
Bank owned life insurance	4,279,830	4,123,544
Other real estate owned	1,383,163	—
Other assets	2,096,649	1,756,071
	<u>\$349,824,752</u>	<u>\$360,467,146</u>
LIABILITIES AND SHAREHOLDERS' EQUITY		
Deposits		
Noninterest-bearing	\$ 50,069,560	\$ 67,010,985
Interest-bearing	227,834,241	204,615,518
Total deposits	<u>277,903,801</u>	<u>271,626,503</u>
Federal funds purchased and securities sold under agreements to repurchase	13,405,463	9,280,348
Notes payable — U.S. Treasury	—	1,932,124
Advances from the Federal Home Loan Bank	22,000,000	40,000,000
Accrued interest payable	214,565	581,863
Other liabilities	1,589,545	2,406,143
	<u>315,113,374</u>	<u>325,826,981</u>
Shareholders' equity		
Common stock, par \$1.00 per share; authorized 10,000,000 shares; issued and outstanding 2,806,705 in 2006 and 2,809,698 in 2005	2,806,705	2,809,698
Additional paid-in capital	18,372,351	18,425,528
Retained earnings	12,886,247	11,567,531
Accumulated other comprehensive income	646,075	1,837,408
	<u>34,711,378</u>	<u>34,640,165</u>
	<u>\$349,824,752</u>	<u>\$360,467,146</u>

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

CONSOLIDATED STATEMENTS OF INCOME

	Years Ended December 31,		
	2006	2005	2004
INTEREST INCOME			
Interest and fees on loans	\$ 20,041,704	\$ 16,826,955	\$ 13,584,677
Interest and dividends on securities			
Taxable interest income	2,197,049	1,201,016	1,399,879
Nontaxable interest income	357,867	174,649	188,296
Dividends	148,259	244,849	210,572
Interest on federal funds sold and other interest income	382,625	623,910	116,899
Total interest income	<u>23,127,504</u>	<u>19,071,379</u>	<u>15,500,323</u>
INTEREST EXPENSE			
Deposits	6,624,327	4,022,723	2,130,765
Borrowings	2,113,123	3,352,360	3,190,857
Total interest expense	<u>8,737,450</u>	<u>7,375,083</u>	<u>5,321,622</u>
Net interest income	14,390,054	11,696,296	10,178,701
PROVISION FOR LOAN LOSSES			
Net interest income after provision for loan losses	<u>14,390,054</u>	<u>11,696,296</u>	<u>10,178,701</u>
NONINTEREST INCOME			
Service charges on deposit accounts	1,121,271	1,082,568	948,386
Brokerage commissions	647,301	667,510	623,923
Electronic Banking fees	2,045,618	4,975,646	4,841,303
Mortgage banking fees and gains	2,465,814	2,705,785	1,917,883
Other fees and commissions	461,841	447,268	333,846
Gains on security sales	2,157,151	839,859	115,810
Total noninterest income	<u>8,898,996</u>	<u>10,718,636</u>	<u>8,781,151</u>
NONINTEREST EXPENSES			
Salaries	7,001,847	7,444,463	6,837,035
Employee benefits	1,500,820	1,344,092	1,876,248
Occupancy	1,794,873	1,848,168	1,601,321
Furniture and equipment	633,004	1,211,349	1,590,436
Prepayment penalty	2,251,971	505,839	—
Check kiting loss	1,833,733	—	—
Write down of impaired securities	—	—	497,313
(Recovery) Impairment of ATM network	(106,221)	563,400	—
Other noninterest expenses	4,470,976	5,716,813	5,348,647
Total noninterest expenses	<u>19,381,003</u>	<u>18,634,124</u>	<u>17,751,000</u>
Income before income taxes	3,908,047	3,780,808	1,208,852
INCOME TAXES			
	<u>1,323,268</u>	<u>1,322,371</u>	<u>320,488</u>
NET INCOME	<u>\$ 2,584,779</u>	<u>\$ 2,458,437</u>	<u>\$ 888,364</u>
NET INCOME PER SHARE — BASIC	<u>\$ 0.92</u>	<u>\$ 0.87</u>	<u>\$ 0.31</u>
NET INCOME PER SHARE — DILUTED	<u>\$ 0.90</u>	<u>\$ 0.87</u>	<u>\$ 0.31</u>

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

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
YEARS ENDED DECEMBER 31, 2006, 2005 AND 2004

	<i>Common Stock</i>	<i>Additional Paid-In Capital</i>	<i>Retained Earnings</i>	<i>Accumulated Other Comprehensive Income</i>	<i>Comprehensive Income</i>
BALANCE, DECEMBER 31, 2003	\$2,828,078	\$18,682,387	\$10,427,425	\$2,186,992	
Net Income	—	—	888,364	—	\$888,364
Changes in net unrealized gains (losses) on available for sale securities, net of tax	—	—	—	179,661	<u>179,661</u>
Comprehensive Income					<u>\$1,068,025</u>
Stock options exercised, including tax benefit of \$21,293	8,845	122,616	—	—	
Shares acquired and cancelled	(2,100)	(30,555)	—	—	
Cash dividends, \$0.38 per share	—	—	(1,076,433)	—	
BALANCE, DECEMBER 31, 2004	<u>2,834,823</u>	<u>18,774,448</u>	<u>10,239,356</u>	<u>2,366,653</u>	
Net Income	—	—	2,458,437	—	\$2,458,437
Changes in net unrealized gains (losses) on available for sale securities, net of tax	—	—	—	(529,245)	<u>(529,245)</u>
Comprehensive income					<u>\$1,929,192</u>
Shares acquired and cancelled	(42,500)	(556,750)	—	—	
Stock options exercised including tax benefit of \$18,166	17,375	207,830	—	—	
Cash dividends, \$0.40 per share	—	—	(1,130,262)	—	
BALANCE, DECEMBER 31, 2005	<u>2,809,698</u>	<u>18,425,528</u>	<u>11,567,531</u>	<u>1,837,408</u>	
Net Income	—	—	2,584,779	—	\$2,584,779
Changes in net unrealized gains (losses) on available for sale securities, net of tax	—	—	—	(1,191,817)	(1,191,817)
Adjustment to initially apply SFAS 158, net of tax effects of \$306	—	—	—	484	<u>484</u>
Comprehensive income					<u>\$1,393,446</u>
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	<u>\$2,806,705</u>	<u>\$18,372,351</u>	<u>\$12,886,247</u>	<u>\$646,075</u>	

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

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Years Ended December 31,		
	2006	2005	2004
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net income	\$ 2,584,779	\$ 2,458,437	\$ 888,364
ADJUSTMENTS TO RECONCILE NET INCOME TO NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES:			
Provision for loan losses	—	—	—
Depreciation and amortization	763,749	937,570	1,255,340
Deferred income taxes	60,631	153,209	(198,755)
Amortization of premiums and discounts	(57,411)	80,719	230,676
Gains on disposal of securities	(2,157,176)	(839,859)	(115,810)
(Recovery) impairment of ATM network	(106,221)	563,400	—
Write down of impaired securities	—	—	497,313
Loans held for sale made, net of principal sold	6,277,819	(3,547,380)	(7,978,146)
Gains on sale and write-down of premises and equipment	—	(6,246)	(18,941)
(Gains) losses on sale of foreclosed real estate	—	—	11,548
Write-down of foreclosed real estate	—	—	8,077
Stock based compensation expense	13,447	—	—
(Increase) decrease in:			
Accrued interest receivable	(294,824)	(123,110)	125,835
Prepaid income taxes	256,482	(61,871)	(160,701)
Cash surrender value of bank owned life insurance	(156,286)	(70,896)	(52,949)
Other assets	226,026	582,001	(547,860)
Increase (decrease) in:			
Accrued interest payable	(367,298)	88,684	42,124
Deferred loan origination fees	(33,566)	144,907	134,343
Other liabilities	1,288	622,669	(315,427)
Net cash provided by (used in) operating activities	<u>7,011,464</u>	<u>982,234</u>	<u>(6,194,969)</u>
CASH FLOWS FROM INVESTING ACTIVITIES:			
Proceeds from sales of securities available for sale	2,766,852	2,461,757	2,518,491
Proceeds from maturities of securities available for sale	3,554,884	19,174,448	30,660,807
Proceeds from maturities of securities held to maturity	1,353,243	541,881	25,000
Redemption (purchase) of Federal Home Loan Bank stock, net	727,100	191,300	(372,900)
Purchase of securities available for sale	(15,030,741)	(8,354,638)	(13,528,310)
Purchase of securities held to maturity	(1,952,570)	(19,021,466)	—
Loans made, net of principal collected	(12,230,817)	(28,509,599)	(20,811,745)
Purchase of premises and equipment	(801,823)	(902,943)	(1,935,364)
Proceeds from sale of premises and equipment	—	15,189	361,582
Proceeds from sale of foreclosed real estate	—	—	164,876
Net cash (used in) investing activities	<u>(21,613,872)</u>	<u>(34,404,071)</u>	<u>(2,917,563)</u>
CASH FLOWS FROM FINANCING ACTIVITIES:			
Net increase (decrease) in time deposits	25,486,897	20,085,651	7,124,050
Net increase (decrease) in other deposits	(19,209,599)	25,694,707	11,665,996
Payment of Federal Home Loan Bank advance	(18,000,000)	(5,000,000)	—
Net increase (decrease) in other borrowed funds	2,192,991	(956,193)	(1,808,269)
Common stock repurchase and retirement	(128,850)	(599,250)	(32,655)
Stock options exercised	52,219	207,039	110,168
Income tax benefit from exercise of stock options	7,014	18,166	21,293
Dividends paid	(1,266,063)	(1,130,262)	(1,076,433)
Net cash provided by (used in) financing activities	<u>(10,865,391)</u>	<u>38,319,858</u>	<u>16,004,150</u>
Net increase (decrease) in cash and cash equivalents	(25,467,799)	4,898,021	6,891,618
Cash and cash equivalents at beginning of year	39,090,565	34,192,544	27,300,926
Cash and cash equivalents at end of year	<u>\$ 13,622,766</u>	<u>\$ 39,090,565</u>	<u>\$ 34,192,544</u>
SUPPLEMENTAL INFORMATION:			
Interest paid on deposits and borrowings	<u>\$ 9,104,758</u>	<u>\$ 7,286,399</u>	<u>\$ 5,279,498</u>
Income taxes paid	<u>\$ 837,661</u>	<u>\$ 1,525,204</u>	<u>\$ 545,609</u>
NONCASH ACTIVITY:			
Transfer of loans to foreclosed real estate	<u>\$ 1,383,163</u>	<u>\$ —</u>	<u>\$ 84,500</u>

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 2006. 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.

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

I. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (*Continued*)

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.

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* ("SFAS No. 114"), 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 No. 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 economic and market conditions on borrowers. Loan losses are charged against the Allowance when management believes the uncollectibility of the loan balance is confirmed. Subsequent recoveries, if any, are credited to the Allowance.

I. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (*Continued*)

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.

Any gain or loss on the sale of an asset is treated as an adjustment to the basis of its replacement, if traded in, or as an income or expense item, if sold. Leases are accounted for as operating leases since none meet the criteria for capitalization.

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, 2006 and 2005 was \$431,110 and \$554,284, respectively. Amortization expense was \$123,180 for 2006, 2005, and 2004, 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 FASB Statement No. 133 ("FASB 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 US 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

I. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (*Continued*)

(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 Statement of Financial Accounting Standards No. 158, "Employees Accounting for Defined Benefit Pension and Other Post Retirement Plans" ("SFAS No. 158") 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

On January 1, 2006, the Company adopted the provisions of Financial Accounting Standards Board ("FASB") Statement No. 123 (R), *Share-Based Payment*, ("SFAS No. 123R"), which requires companies to recognize expense related to the fair value of our stock-based compensation. Prior to January 1, 2006, the Company accounted for stock-based compensation under the recognition and measurement provisions of Accounting Principle Board ("APB") Opinion No. 25, Accounting for Stock Issued to Employees ("APB No. 25"), and related Interpretations, as permitted by FASB Statement No. 123, Accounting for Stock-Based Compensation ("SFAS No. 123"). 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 No. 123R 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 No. 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 No. 123R. 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 \$13,447 during 2006. As of December 31, 2006, there was \$10,928 of unrecognized compensation expense related to nonvested stock options, which will be recognized over the remaining vesting period.

The following illustrates the effect on the net income and earnings per share if the Company had applied the fair value method of SFAS No. 123, "Accounting for Stock-Based Compensation," prior to January 1, 2006:

	2005	2004
Net Income:		
As reported	\$2,458,437	\$ 888,364
Additional compensation	(162,222)	(133,288)
Income tax benefit on additional compensation	62,650	51,476
Pro forma	<u>\$2,358,865</u>	<u>\$ 806,552</u>
Basic Earnings Per Share:		
As reported	\$ 0.87	\$ 0.31
Pro forma	0.83	0.28
Diluted Earnings Per Share:		
As reported	0.87	0.31
Pro forma	0.83	0.28

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, 2006 and 2005, the required reserve balances were \$1.4 million and \$323,000, respectively. The Company sells federal funds on an unsecured basis to its correspondent banks. Average balances sold were \$6.7 million in 2006 and \$12.9 million in 2005.

3. INVESTMENT SECURITIES

Investment securities are summarized as follows:

	<i>Amortized cost</i>	<i>Unrealized gains</i>	<i>Unrealized losses</i>	<i>Fair value</i>
December 31, 2006				
AVAILABLE FOR SALE				
U.S. government agency	\$ 9,642,252	\$ 24,405	\$ (28,897)	\$ 9,637,760
Mortgage-backed securities	12,712,231	129,674	(116,352)	12,725,553
State and municipal	5,691,067	42,133	(8,241)	5,724,959
Corporate bonds	<u>5,639,276</u>	<u>—</u>	<u>(17,747)</u>	<u>5,621,529</u>
	33,684,826	196,212	(171,237)	33,709,801
Equity securities	<u>1,140,856</u>	<u>1,090,934</u>	<u>(6,944)</u>	<u>2,224,846</u>
	<u>\$34,825,682</u>	<u>\$1,287,146</u>	<u>\$(178,181)</u>	<u>\$35,934,647</u>
HELD TO MATURITY				
U.S. government agency	\$ 6,456,069	\$ —	\$ (89,979)	\$ 6,366,090
Mortgage-backed securities	8,761,200	—	(136,735)	8,624,465
State and municipal	<u>3,912,704</u>	<u>3,528</u>	<u>(16,519)</u>	<u>3,899,713</u>
	<u>\$19,129,973</u>	<u>\$ 3,528</u>	<u>\$(243,233)</u>	<u>\$18,890,268</u>
December 31, 2005				
AVAILABLE FOR SALE				
U.S. government agency	\$10,786,412	\$ 3,225	\$ (49,302)	\$10,740,335
Mortgage-backed securities	8,551,994	34,005	(95,874)	8,490,125
State and municipal	3,613,458	76,401	—	3,689,859
Corporate bonds	<u>1,516,345</u>	<u>—</u>	<u>(1,874)</u>	<u>1,514,471</u>
	24,468,209	113,631	(147,050)	24,434,790
Equity securities	<u>1,633,298</u>	<u>3,030,815</u>	<u>(3,900)</u>	<u>4,660,213</u>
	<u>\$26,101,507</u>	<u>\$3,144,446</u>	<u>\$(150,950)</u>	<u>\$29,095,003</u>
HELD TO MATURITY				
U.S. government agency	\$ 5,000,000	\$ —	\$ (64,050)	\$ 4,935,950
Mortgage-backed securities	9,575,713	29,016	(98,260)	9,506,469
State and municipal	<u>3,912,692</u>	<u>—</u>	<u>(49,832)</u>	<u>3,862,860</u>
	<u>\$18,488,405</u>	<u>\$ 29,016</u>	<u>\$(212,142)</u>	<u>\$18,305,279</u>

Information related to unrealized losses in the portfolio as of December 31, 2006 follows:

	Less than 12 months		12 months or longer		Total	
	<i>Fair Value</i>	<i>Unrealized Losses</i>	<i>Fair Value</i>	<i>Unrealized Losses</i>	<i>Fair Value</i>	<i>Unrealized Losses</i>
U.S. government agency	\$ 1,985,619	\$ (14,380)	\$ 10,533,310	\$ (104,496)	\$ 12,518,929	\$ (118,876)
Mortgage-backed securities	—	—	15,167,237	(253,087)	15,167,237	(253,087)
State and municipal	—	—	5,373,469	(24,760)	5,373,469	(24,760)
Corporate bonds	—	—	5,016,250	(17,748)	5,016,250	(17,748)
Equity securities	—	—	125,790	(6,944)	125,790	(6,944)
	<u>\$ 1,985,619</u>	<u>\$ (14,380)</u>	<u>\$ 36,216,056</u>	<u>\$ (407,035)</u>	<u>\$ 38,201,675</u>	<u>\$ (421,415)</u>

3. INVESTMENT SECURITIES (CONTINUED)

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, 2006, five marketable equity securities had unrealized losses of approximately \$6,944 from the Company's cost basis. At December 31, 2005, one marketable equity security had an unrealized loss with aggregate depreciation of approximately \$3,900 from the Company's cost basis. During 2004, the Company wrote down its FHLMC preferred stock securities by \$497,313 to fair value to reflect what the Company considered to be an other-than-temporary impairment of those securities. No credit issues 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, 2006 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.

Contractual maturities of debt securities at December 31, 2006 and 2005 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, 2006			
	Available for sale		Held to maturity	
	<i>Amortized Cost</i>	<i>Fair Value</i>	<i>Amortized Cost</i>	<i>Fair Value</i>
<i>Maturing</i>				
Within one year	\$ 2,000,000	\$ 1,985,620	\$ —	\$ —
Over one to five years	4,923,172	4,924,303	—	—
Over five to ten years	3,928,823	3,958,428	8,414,510	8,324,424
Over ten years	10,120,600	10,115,898	1,954,263	1,941,379
Mortgage-backed securities	12,712,231	12,725,553	8,761,200	8,624,465
	<u>\$33,684,826</u>	<u>\$33,709,802</u>	<u>\$19,129,973</u>	<u>\$18,890,268</u>
	December 31, 2005			
	Available for sale		Held to maturity	
	<i>Amortized Cost</i>	<i>Fair Value</i>	<i>Amortized Cost</i>	<i>Fair Value</i>
<i>Maturing</i>				
Within one year	\$ 250,000	\$ 250,161	\$ 250,000	\$ 250,161
Over one to five years	9,767,684	9,744,231	9,767,684	9,744,231
Over five to ten years	5,899,059	5,950,273	5,899,059	5,950,273
Mortgage-backed securities	8,551,466	8,490,125	8,551,466	8,490,125
	<u>\$24,468,209</u>	<u>\$24,434,790</u>	<u>\$24,468,209</u>	<u>\$24,434,790</u>

At December 31, 2006 and 2005, securities with an amortized cost of \$17.9 million (fair value of \$17.9 million) and \$32.8 million (fair value of \$32.6 million), respectively, were pledged as collateral for government deposits, securities sold under repurchase agreements, and advances from the Federal Home Loan Bank.

In 2006, 2005, and 2004, the Company realized gross gains on sales of securities of \$2.2 million, \$839,859, and \$115,810, respectively. During 2004, the Company recognized an other than temporary impairment of \$497,313. There were no realized losses in 2006 or 2005. Income taxes (benefit) on net security gains (losses) were \$730,413, \$293,783, and \$(147,336), in 2006, 2005 and 2004, respectively.

4. LOANS

Major classifications of loans at December 31 are as follows:

	2006	2005
Real estate:		
Residential	\$ 55,057,625	\$ 53,148,211
Commercial	120,397,988	97,909,115
Construction and land development	29,996,306	37,415,478
Demand and time	51,549,802	56,118,527
Lease financing	969,113	1,936,482
Installment	<u>2,030,480</u>	<u>1,415,260</u>
	260,001,314	247,943,073
Allowance for loan losses	<u>3,131,021</u>	<u>3,337,163</u>
Loans, net	<u>\$256,870,293</u>	<u>\$244,605,910</u>

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:

	2006	2005
Repricing or maturing within one year	\$ 77,881,735	\$139,326,825
Maturing over one to five years	98,707,890	91,219,788
Maturing over five years	<u>83,411,689</u>	<u>17,396,460</u>
	<u>\$260,001,314</u>	<u>\$247,943,073</u>

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

	2006	2005
Deferred origination costs and premiums	\$ 538,554	\$ 392,075
Deferred origination fees and unearned discounts	(854,549)	(741,636)
Net deferred fees	<u>\$(315,995)</u>	<u>\$(349,561)</u>

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

	2006	2005	2004
Beginning balance	\$3,337,163	\$3,485,076	\$3,648,245
Provision charged to operations	—	—	—
Recoveries	<u>49,692</u>	<u>167,128</u>	<u>113,953</u>
	3,386,855	3,652,204	3,762,198
Loans charged off	<u>255,834</u>	<u>315,041</u>	<u>277,122</u>
Ending balance	<u>\$3,131,021</u>	<u>\$3,337,163</u>	<u>\$3,485,076</u>

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

	2006	2005	2004
Nonaccrual loans	\$3,699,397	\$1,413,925	\$ 615,394
Restructured loans	180,686	—	455,864
Foreclosed real estate	<u>1,383,163</u>	<u>—</u>	<u>—</u>
Total nonperforming assets	<u>\$5,263,246</u>	<u>\$1,413,925</u>	<u>\$1,071,258</u>
Accruing loans past-due 90 days or more	<u>\$ 436,599</u>	<u>\$ 179,012</u>	<u>\$1,567,919</u>
Unrecorded interest on nonaccrual loans	<u>\$ 76,044</u>	<u>\$ 111,413</u>	<u>\$ 64,037</u>
Interest income recognized on nonaccrual loans	<u>\$ 300,650</u>	<u>\$ 58,718</u>	<u>\$ 32,318</u>

At December 31, 2006 and 2005, there were no impaired loans.

At December 31, 2004, the Company had one impaired loan to the same borrower amounting to \$455,864, which was classified as impaired because it had been restructured to accept interest only payments for a period of

4. LOANS (CONTINUED)

time. The average balance of impaired loans amounted to \$298,406 and \$530,680 in 2005 and 2004, respectively. During 2005 and 2004, the Company received total payments on impaired loans of \$601,323 and \$341,857, respectively. Of these amounts, \$24,583 and \$75,938, were recorded as interest income for 2005 and 2004, respectively. The remainder was applied to reduce principal and recovery of professional fees. There was no specific allowance for this loan since the fair value of the collateral securing the loan was considered adequate to cover all principal and interest due. The Company also continued to accrue interest on this loan due to the adequacy of the collateral value.

Loans with a balance of approximately \$86.6 million and \$86.2 million were pledged as collateral to the Federal Home Loan Bank of Atlanta as of December 31, 2006 and 2005, respectively. At December 31, 2006 and 2005, the Company serviced loans for others totaling \$1.1million and \$1.6 million, respectively.

5. CREDIT COMMITMENTS

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

	2006	2005	2004
LOAN COMMITMENTS			
Mortgage loans	\$ 4,122,697	\$ 4,066,223	\$ 8,899,836
Construction and land development	29,501,299	14,913,344	9,438,961
Commercial loans	6,840,000	7,058,000	13,812,780
	<u>\$40,463,996</u>	<u>\$26,037,567</u>	<u>\$32,151,577</u>
UNUSED LINES OF CREDIT			
Home equity lines	\$46,199,911	\$52,194,528	\$55,883,051
Commercial lines	44,279,428	26,095,802	25,467,308
Unsecured consumer lines	1,084,048	1,410,270	1,405,075
	<u>\$91,563,387</u>	<u>\$79,700,600</u>	<u>\$82,755,434</u>
LETTERS OF CREDIT			
	<u>\$ 2,223,755</u>	<u>\$ 2,606,061</u>	<u>\$ 2,910,330</u>

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, 2006, 2005 and 2004, transactions in related party loans were as follows:

	2006	2005	2004
Beginning balance	\$ 1,894,784	\$ 1,820,717	\$ 3,209,200
Additions	7,918,876	179,452	1,040,580
Repayments	(1,837,046)	(105,385)	(2,429,063)
Ending balance	<u>\$ 7,976,614</u>	<u>\$ 1,894,784</u>	<u>\$ 1,820,717</u>

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, 2006, 2005, and 2004, amounts paid to the law firm in connection with those services were \$195,000, \$220,000, and \$249,000, respectively.

6. RELATED PARTY TRANSACTIONS (CONTINUED)

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, 2006, 2005, and 2004, amounts paid to the insurance brokerage for insurance premiums were \$282,000, \$215,000, and \$192,000, 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 2006, 2005 or 2004.

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 amounting to \$356,000 in 2006, \$169,000 in 2005, and \$739,000 in 2004.

7. PREMISES AND EQUIPMENT

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

	2006	2005
Land and improvements	\$ 909,544	\$ 909,544
Buildings	2,995,117	2,885,994
Leasehold improvements	3,523,947	3,137,550
Equipment and fixtures	<u>4,521,052</u>	<u>5,341,396</u>
	11,949,660	12,274,484
Accumulated depreciation and amortization	<u>(6,349,672)</u>	<u>(6,840,856)</u>
	<u>\$ 5,599,988</u>	<u>\$ 5,433,628</u>

Depreciation and amortization of premises and equipment was \$611,658, \$673,022, and \$1.1 million, for 2006, 2005, and 2004, respectively. Amortization of software was \$108,364, \$141,368, and \$72,962 for 2006, 2005, and 2004, respectively.

On September 22, 2005, Wal-Mart notified the Bank of its intention to terminate the agreement for the Bank to provide ATMs at Wal-Mart, Sam's Club, and Wal-Mart supercenters in Maryland, Virginia and West Virginia. An impairment of \$563,400 was recorded for the write down and cost of disposal of the ATM network. The ATMs were assets of the Electronic Banking division.

8. DEPOSITS

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

	2006	2005
NOW and Super NOW	\$ 33,112,772	\$ 33,396,380
Money market	52,072,965	50,482,662
Savings	27,608,013	31,182,882
Certificates of deposit of \$100,000 or more	29,567,921	14,990,576
Other time deposits	<u>85,472,570</u>	<u>74,563,018</u>
	<u>\$227,834,241</u>	<u>\$204,615,518</u>

Time deposits mature as follows:

	December 31,	
	2006	2005
Maturing within one year	\$ 92,053,740	\$67,555,717
Maturing over one to two years	13,479,273	12,087,661
Maturing over two to three years	5,197,865	3,353,809
Maturing over three to four years	3,503,735	2,445,906
Maturing over four to five years	<u>805,878</u>	<u>4,110,501</u>
	<u>\$115,040,491</u>	<u>\$89,553,594</u>

9. BORROWED FUNDS

Borrowed funds consist of securities sold under repurchase agreements, federal funds purchased, borrowings from the FHLB and notes payable-U.S. Treasury. Notes payable-U.S. Treasury are U.S. Treasury and Federal Treasury Tax and Loan deposits accepted by the Bank from its customers to be remitted to the Federal Reserve on a periodic basis. 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:

	<i>Maturity Date</i>	<i>2006</i>	<i>2005</i>	<i>2004</i>
Amount outstanding at year-end:				
Federal Home Loan Bank	March 26, 2008	\$ 5,000,000	\$ 5,000,000	\$ 5,000,000
Federal Home Loan Bank	February 2, 2010	—	35,000,000	35,000,000
Federal Home Loan Bank	May 24, 2010	—	—	5,000,000
Federal Home Loan Bank	Daily Rate Credit	17,000,000	—	—
Federal Home Loan Bank		<u>\$22,000,000</u>	<u>\$40,000,000</u>	<u>\$45,000,000</u>
Federal funds purchased and securities sold under repurchase agreements				
		\$13,405,463	\$ 9,280,348	\$10,183,951
Notes-payable — U.S. Treasury				
		—	\$ 1,932,124	\$ 1,984,714
Weighted average interest rate at year-end:				
Advances from the FHLB		5.43%	6.67%	6.84%
Federal funds purchased and securities sold under repurchase agreements		4.86%	3.59%	1.91%
Notes payable — U.S. Treasury		—	4.17%	1.97%
Maximum outstanding at any month-end:				
Advances from the FHLB		\$40,000,000	\$45,000,000	\$45,000,000
Federal funds purchased and securities sold under repurchase agreements		13,405,463	11,742,108	13,540,231
Notes payable — U.S. Treasury		1,432,423	1,958,750	2,008,989
Average balance outstanding during the year:				
Advances from the FHLB		\$24,603,287	\$44,876,712	\$45,000,000
Federal funds purchased and securities sold under repurchase agreements		9,040,071	8,986,714	10,102,501
Notes payable — U.S. Treasury		185,067	1,016,211	1,051,267
Weighted average interest rate during the year:				
Advances from the FHLB		5.38%	6.84%	6.84%
Federal funds purchased and securities sold under repurchase agreements		4.66%	2.66%	0.96%
Notes payable — U.S. Treasury		4.18%	3.06%	1.10%

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%. Debt retirement expense of \$505,839 was incurred in 2005 due to the prepayment of a \$5.0 million FHLB advance that had a maturity date of May 24, 2010 and an interest rate of 7.26%.

The Company has available unsecured federal funds lines 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, 2005 and 2004. 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:

	2006	2005	2004
Data processing services	\$ 815,056	\$ 807,314	\$ 719,445
Professional services	521,231	226,965	187,784
Employee-related expenses	384,128	345,203	306,678
Marketing	303,903	355,921	287,343
Directors' fees	238,850	173,050	165,950
Carrier service	210,703	496,714	479,131
Liability insurance	205,516	214,579	216,890
Printing, stationary, and supplies	202,541	257,865	282,914
Loan expenses	195,844	354,864	215,570
Postage and freight	164,606	167,681	228,030
Telephone	162,808	189,990	195,867
Deposit premium amortization	123,180	123,180	123,180
Shareholder expense	111,768	111,273	91,283
Software amortization	108,364	141,368	72,962
Coin/Currency service	103,480	84,429	80,201
ATM services	77,704	1,057,794	1,134,848
Bank account charges	51,643	80,592	88,134
Other	383,430	528,031	472,437
	<u>\$4,364,755</u>	<u>\$5,716,813</u>	<u>\$5,348,647</u>

11. STOCK OPTIONS

The Company adopted a stock option incentive plan in 1998, which provides 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 contain a serial feature whereby one third of the options granted vest and can be exercised after each year. Option prices are 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.

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

	2006		2005		2004	
	<i>Shares</i>	<i>Option Price Range</i>	<i>Shares</i>	<i>Option Price Range</i>	<i>Shares</i>	<i>Option Price Range</i>
Outstanding at beginning of year	227,130		193,470		174,785	
Granted	12,430	\$ 15.35 to \$17.16	53,930	\$ 14.45 to \$14.85	32,430	\$ 16.02 to \$16.22
Exercised	(4,525)	\$ 10.94 to \$15.36	(17,375)	\$ 9.71 to \$14.50	(8,845)	\$ 9.71 to \$15.42
Expired/Canceled	<u>(6,005)</u>	\$ 10.94 to \$16.02	<u>(2,895)</u>	\$ 12.67 to \$15.48	<u>(4,900)</u>	\$ 10.94 to \$18.10
Outstanding at end of year	<u>229,030</u>	\$ 9.71 to \$18.10	<u>227,130</u>	\$ 9.71 to \$18.10	<u>193,470</u>	\$ 9.71 to \$18.10
Exercisable at December 31	<u>209,670</u>		<u>213,550</u>		<u>143,919</u>	
Aggregate intrinsic value at year end	<u>\$558,473</u>					

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 \$13,447 during 2006. As of December 31, 2006, there was \$10,928 of unrecognized compensation expense related to nonvested stock options, which will be recognized over the remaining vesting period. The total intrinsic value of options exercised during the year ended December 31, 2006 and 2005 was approximately \$18,000 and \$47,000, respectively.

11. STOCK OPTIONS (CONTINUED)

A summary of information about stock options outstanding is as follows at December 31, 2006:

<i>Weighted Average Exercise Price</i>	<i>Shares</i>	<i>Weighted Average Remaining Life (Years)</i>	<i>Shares Underlying Options Currently Exercisable</i>
\$ 9.71	2,940	4.33	2,940
10.54	630	4.16	630
10.94	19,950	4.42	19,950
12.11	4,620	5.33	4,620
12.14	630	5.16	630
12.67	21,000	5.58	21,000
13.45	14,700	3.58	14,700
13.45	3,150	3.33	3,150
14.45	6,930	8.29	2,310
14.50	5,670	6.33	5,670
14.50	39,500	8.96	39,500
14.85	5,000	8.43	5,000
15.35	500	9.15	—
15.36	2,930	2.33	2,930
15.42	26,670	2.35	26,670
16.02	24,000	7.58	24,000
16.22	6,930	7.33	4,620
16.31	6,930	9.29	—
16.70	3,150	1.16	3,150
17.16	5,000	10.0	—
17.75	3,000	6.92	3,000
17.79	22,050	1.35	22,050
18.10	3,150	1.33	3,150
14.70	<u>229,030</u>	5.41	<u>209,670</u>

As of December 31, 2006, the weighted average exercise price of shares underlying options currently exercisable is \$14.58 per share.

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, 2006, 2005 and 2004:

	2006	2005	2004
Dividend yield	2.67%	2.67%	2.25%
Expected volatility	24.76%	26.94%	18.15%
Risk free rate	4.91% to 4.99%	3.96% to 4.47%	4.43%
Estimated life	10 years	10 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:

	2006	2005	2004
Weighted average common shares outstanding	2,812,289	2,827,747	2,831,880
Stock option adjustment	58,953	14,140	28,366
Weighted average common shares outstanding-diluted	<u>2,871,242</u>	<u>2,841,887</u>	<u>2,860,246</u>
Net income (applicable to common stock)	<u>\$2,584,779</u>	<u>\$2,458,437</u>	<u>\$ 888,364</u>
Basic net income per share	<u>\$ 0.92</u>	<u>\$ 0.87</u>	<u>\$ 0.31</u>
Diluted net income per share	<u>\$ 0.90</u>	<u>\$ 0.87</u>	<u>\$ 0.31</u>

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 the adjustment for the adoption of SFAS 158 related to the funded status of the defined benefit plan. These items, net of taxes, will be accumulated with net income in determining comprehensive income. Presented below is a reconciliation of net income to comprehensive income for the years ended December 31:

	2006	2005	2004
Net Income	\$ 2,584,779	\$ 2,458,437	\$ 888,364
Other comprehensive income:			
Unrealized holding gains (losses) during the period	215,449	(22,384)	(88,800)
Add: Security impairment write down	—	—	497,313
Adoption of SFAS 158	790	—	—
Less: Adjustment for security gains	(2,157,151)	(839,859)	(115,810)
Other comprehensive income before tax	(1,940,912)	(862,243)	292,703
Income taxes on comprehensive income	749,579	332,998	(113,042)
Other comprehensive income after tax	(1,191,333)	(529,245)	179,661
Comprehensive income	<u>\$ 1,393,446</u>	<u>\$ 1,929,192</u>	<u>\$ 1,068,025</u>

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, 2006, that the Bank meets all capital adequacy requirements to which it is subject. As of December 31, 2006, 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	
	<i>Amount</i>	<i>Ratio</i>	<i>Amount</i>	<i>Ratio</i>	<i>Amount</i>	<i>Ratio</i>
DECEMBER 31, 2006						
Total Capital (to risk-weighted assets)						
Consolidated	\$37,253,000	13.20%	\$22,573,000	8.0%	\$28,217,000	10.0%
Carrollton Bank	35,313,000	12.60%	22,428,000	8.0%	28,035,000	10.0%
Tier 1 Capital (to risk-weighted assets)						
Consolidated	33,634,000	11.92%	\$11,287,000	4.0%	16,930,000	6.0%
Carrollton Bank	32,182,000	11.48%	11,214,000	4.0%	16,821,000	6.0%
Tier 1 Capital (to average assets)						
Consolidated	33,634,000	9.74%	\$13,824,000	4.0%	17,280,000	5.0%
Carrollton Bank	32,182,000	9.30%	13,849,000	4.0%	17,311,000	5.0%
DECEMBER 31, 2005						
Total Capital (to risk-weighted assets)						
Consolidated	\$37,447,000	13.51%	\$22,176,000	8.0%	\$27,720,000	10.0%
Carrollton Bank	34,338,000	12.52%	21,945,000	8.0%	27,432,000	10.0%
Tier 1 Capital (to risk-weighted assets)						
Consolidated	32,250,000	11.63%	11,088,000	4.0%	16,632,000	6.0%
Carrollton Bank	31,001,000	11.30%	10,973,000	4.0%	16,459,000	6.0%
Tier 1 Capital (to average assets)						
Consolidated	32,250,000	8.96%	14,937,000	4.0%	17,996,000	5.0%
Carrollton Bank	31,001,000	8.72%	14,223,000	4.0%	17,779,000	5.0%

15. RETIREMENT PLANS

In the year ended December 31, 2006, the Company adopted Statement of Financial Accounting Standards No. 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans" ("SFAS 158"), 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. The Company's 2005 and 2004 disclosures have not been changed as SFAS 158 prohibits retrospective application.

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:

	2006	2005	2004
CHANGE IN BENEFIT OBLIGATION:			
Benefit obligation at beginning of year	\$7,944,785	\$7,739,006	\$ 8,820,583
Service cost	—	—	528,407
Interest cost	469,361	477,203	545,710
Actuarial gain	230,830	61,831	69,083
Benefits paid	(354,637)	(333,255)	(331,542)
Adjustment for special event — curtailment	—	—	(1,893,235)
Benefit obligation at end of year	<u>8,290,339</u>	<u>7,944,785</u>	<u>7,739,006</u>
CHANGE IN PLAN ASSETS:			
Fair value of plan assets at beginning of year	7,952,987	7,730,718	7,399,746
Actual return on plan assets	767,957	591,608	271,153
Employer contribution	—	—	450,000
Benefits paid and administrative expenses	(429,815)	(369,339)	(390,181)
Fair value of plan assets at end of year	<u>8,291,129</u>	<u>7,952,987</u>	<u>7,730,718</u>
Funded status			
Status of plan overfunded (underfunded)	790	8,202	(8,288)
Unrecognized net actuarial (gain) loss	256,285	45,450	(15,901)
Prepaid (accrued) benefit cost before the adoption of SFAS 158	<u>\$ 257,075</u>	<u>\$ 53,652</u>	<u>\$ (24,189)</u>
Amounts Recognized in the Consolidated Balance Sheets:			
Prepaid benefit cost	<u>\$ 257,075</u>	<u>\$ 53,652</u>	<u>\$ (24,189)</u>
Net amount recognized	<u>\$ 257,075</u>	<u>\$ 53,652</u>	<u>\$ (24,189)</u>
After the adoption of SFAS 158:			
Other assets	<u>\$ 790</u>	<u>\$ —</u>	<u>\$ —</u>
Net amount recognized	<u>\$ 790</u>	<u>\$ —</u>	<u>\$ —</u>
Amounts recognized in accumulated other comprehensive income consist of:			
Net loss	<u>\$ 256,285</u>	<u>\$ —</u>	<u>\$ —</u>
Net amount recognized (before tax effect)	<u>\$ 256,285</u>	<u>\$ —</u>	<u>\$ —</u>

The incremental effect of applying FASB Statement No. 158 on individual items in the consolidated balance sheet as of December 31, 2006 is as follows:

	Before Application of Statement 158		After Application of Statement 158	
	<i>Debit</i>	<i>Credit</i>	<i>Debit</i>	<i>Credit</i>
Other assets, excluding prepaid pension cost and deferred taxes	\$ 1,338,781	\$ —	\$ —	\$ 1,338,781
Prepaid pension costs	257,075	—	(256,285)	790
Deferred taxes	599,770	157,308	—	757,078
Total other assets	<u>\$ 2,195,626</u>	<u>\$157,308</u>	<u>\$ (256,285)</u>	<u>\$ 2,096,649</u>
Total assets	<u>\$349,923,729</u>	<u>\$157,308</u>	<u>\$ (256,285)</u>	<u>\$349,824,752</u>
Accumulated other comprehensive loss	<u>\$ (745,052)</u>	<u>\$ 98,977</u>	<u>\$ —</u>	<u>\$ (646,075)</u>
Total stockholders' equity	<u>\$ (34,810,355)</u>	<u>\$ 98,977</u>	<u>\$ —</u>	<u>\$ (34,711,378)</u>

15. RETIREMENT PLANS *(Continued)*

	2006	2005	2004
ASSUMPTIONS USED IN MEASURING THE PROJECTED BENEFIT OBLIGATION			
WERE AS FOLLOWS FOR THE YEARS ENDED DECEMBER 31:			
Discount rates	5.82%	6.25%	6.25%
Rates of increase in compensation levels	N/A	N/A	4.25%
Long-term rate of return on assets	8.00%	8.00%	8.00%
NET PERIODIC PENSION EXPENSE INCLUDES THE FOLLOWING			
COMPONENTS:			
Service cost	\$ —	\$ —	\$ 528,407
Interest cost	469,361	477,203	545,710
Expected return on plan assets	(622,784)	(555,044)	(558,384)
Net amortization and deferral	—	—	148,670
Net periodic pension expense (benefit)	<u>\$ (153,423)</u>	<u>\$ (77,841)</u>	<u>\$ 664,403</u>
ACCUMULATED BENEFIT OBLIGATION AT YEAR END	<u>\$8,290,339</u>	<u>\$7,944,785</u>	<u>\$7,739,006</u>
ALLOCATION OF ASSETS			
Equity securities	\$4,361,023	\$4,102,673	\$3,715,646
Fixed income-guaranteed fund	<u>3,930,106</u>	<u>3,850,314</u>	<u>4,015,072</u>
	<u>\$8,291,129</u>	<u>\$7,952,987</u>	<u>\$7,730,718</u>

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:

<i>Year</i>	<i>Amount</i>
2007	\$ 340,417
2008	363,113
2009	362,976
2010	390,677
2011	406,123
2012-2016	2,524,509

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 quarterly 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 \$319,453, \$292,080, and \$92,485, for 2006, 2005, and 2004, 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

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

	2006	2005	2004
CURRENT			
Federal	\$1,082,628	\$ 989,907	\$ 428,205
State	<u>180,009</u>	<u>179,255</u>	<u>91,038</u>
	1,262,637	1,169,162	519,243
DEFERRED			
	<u>60,631</u>	<u>153,209</u>	<u>(198,755)</u>
	<u>\$1,323,268</u>	<u>\$1,322,371</u>	<u>\$ 320,488</u>

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

	2006	2005	2004
Provision for loan losses	\$ 79,612	\$ 57,124	\$ 62,425
Deferred loan origination costs	(20,427)	(4,812)	6,794
Deferred compensation plan	16,466	(227)	3,128
Depreciation	522	(120,334)	7,004
Discount accretion	5,178	(666)	(2,140)
Retirement benefits	(20,720)	30,062	(83,904)
Impairment loss provisions	—	192,062	(192,062)
	<u>\$ 60,631</u>	<u>\$ 153,209</u>	<u>\$(198,755)</u>

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

	2006	2005	2004
DEFERRED TAX ASSETS			
Allowance for loan losses	\$ 974,066	\$1,053,678	\$1,110,802
Deferred compensation plan	190,426	206,892	206,665
Depreciation	27,000	27,522	—
Accrued retirement benefits	—	—	9,342
	<u>1,191,492</u>	<u>1,288,092</u>	<u>1,326,809</u>
DEFERRED TAX LIABILITIES			
Prepaid retirement benefits	—	20,720	—
	106,645	127,072	131,884
Unrealized gains on available for sale investment securities	317,406	1,156,088	1,297,024
Depreciation	—	—	92,812
Discount accretion	8,344	3,166	3,832
FHLB Stock dividends	<u>2,019</u>	<u>2,019</u>	<u>2,019</u>
	<u>434,414</u>	<u>1,309,065</u>	<u>1,527,571</u>
NET DEFERRED TAX ASSET (LIABILITY)	<u>\$ 757,078</u>	<u>\$ (20,973)</u>	<u>\$ (200,762)</u>

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

	2006	2005	2004
Statutory federal income tax rate	34.0%	34.0%	34.0%
Increase (Decrease) resulting from:			
Tax-exempt income	(4.5)	(3.4)	(10.2)
State income taxes, net of federal income tax benefit	3.8	4.0	1.9
Nondeductible expense	<u>0.6</u>	<u>0.4</u>	<u>0.8</u>
	<u>33.9%</u>	<u>35.0%</u>	<u>26.5%</u>

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 \$937,160, \$947,957, and \$779,709, for 2006, 2005, and 2004, respectively.

Lease obligations will require minimum rent payments as follows:

<i>Period</i>	<i>Minimum rentals</i>
2007	\$ 959,293
2008	810,397
2009	723,251
2010	710,115
2011	547,557
Remaining years	<u>4,700,487</u>
	<u>\$8,451,100</u>

19. PARENT COMPANY FINANCIAL INFORMATION

The balance sheets as of December 31, 2006 and 2005 and statements of income and cash flows for Carrollton Bancorp (Parent Only) for 2006, 2005, and 2004, are presented below:

BALANCE SHEETS

	December 31,	
	2006	2005
ASSETS		
Cash	\$ 6,293	\$ 22,094
Interest-bearing deposits in subsidiary	956,518	217,679
Investment in subsidiary	32,593,361	31,536,069
Investment securities available for sale	2,224,846	4,660,213
Other assets	<u>28,270</u>	<u>25,813</u>
	<u>\$35,809,288</u>	<u>\$36,461,868</u>
LIABILITIES AND SHAREHOLDERS' EQUITY		
Liabilities	1,097,910	\$ 1,821,703
Shareholders' Equity		
Common Stock	2,806,705	2,809,698
Additional Paid-in Capital	18,372,351	18,425,528
Retained earnings	12,886,247	11,567,531
Accumulated other comprehensive income	<u>646,075</u>	<u>1,837,408</u>
	<u>34,711,378</u>	<u>34,640,165</u>
	<u>\$35,809,288</u>	<u>\$36,461,868</u>

19. PARENT COMPANY FINANCIAL INFORMATION (Continued)

STATEMENTS OF INCOME

	Years ended December 31,		
	2006	2005	2004
INCOME			
Dividends from subsidiary	\$ 258,840	\$ 608,827	\$ 588,273
Interest and dividends	73,720	138,592	132,490
Security gains	<u>2,157,151</u>	<u>766,772</u>	<u>—</u>
	2,489,711	1,514,191	720,763
EXPENSES			
Income before income taxes and equity in undistributed net income of subsidiary	<u>161,751</u>	<u>163,639</u>	<u>105,403</u>
Income tax expense (benefit)	2,327,960	1,350,552	615,360
	<u>785,790</u>	<u>249,895</u>	<u>(21,691)</u>
	1,542,170	1,100,657	637,051
Equity in undistributed net income of subsidiary	<u>1,042,609</u>	<u>1,357,780</u>	<u>251,313</u>
Net Income	<u>\$2,584,779</u>	<u>\$2,458,437</u>	<u>\$888,364</u>

STATEMENTS OF CASH FLOWS

	Years ended December 31,		
	2006	2005	2004
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net income	\$ 2,584,779	\$ 2,458,437	\$ 888,364
ADJUSTMENTS TO RECONCILE NET INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES:			
Equity in undistributed net income of subsidiary	(1,042,609)	(1,357,780)	(251,313)
Gains on disposal of securities	(2,157,151)	(766,772)	—
Stock based compensation expense	13,447	—	—
Decrease (increase) in other assets	(2,457)	(74)	662
Increase (decrease) in other liabilities	<u>13,126</u>	<u>309,958</u>	<u>(99,454)</u>
Net cash (used in) provided by operating activities	(590,865)	661,935	559,552
Cash Flows from Investing Activities:			
Purchase of securities available for sale	117,259	—	(100,000)
Proceeds from sales of securities available for sale	<u>2,766,852</u>	<u>1,016,133</u>	<u>—</u>
Net cash provided by (used in) investing activities	2,649,593	1,016,133	(100,000)
CASH FLOWS FROM FINANCING ACTIVITIES:			
Dividends paid	(1,266,063)	(1,130,262)	(1,076,433)
Common stock repurchase and retirement	(128,850)	(599,250)	(32,655)
Stock options exercised	52,219	207,039	110,168
Income tax benefit from exercise of stock options	<u>7,014</u>	<u>18,166</u>	<u>21,293</u>
Net cash used in financing activities	<u>(1,335,690)</u>	<u>(1,522,473)</u>	<u>(998,920)</u>
Net increase (decrease) in cash	723,038	155,595	(539,368)
Cash and cash equivalents at beginning of year	<u>239,773</u>	<u>84,178</u>	<u>623,546</u>
Cash and cash equivalents at end of year	<u>\$ 962,811</u>	<u>\$ 239,773</u>	<u>\$ 84,178</u>
Noncash Activities:			
Income taxes paid, net of cash received from subsidiaries	<u>\$ 769,473</u>	<u>\$ 36,615</u>	<u>\$ 53,475</u>

20. FAIR VALUE OF FINANCIAL INSTRUMENTS

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.

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.

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, 2006		December 31, 2005	
	<i>Carrying amount</i>	<i>Fair value</i>	<i>Carrying amount</i>	<i>Fair value</i>
FINANCIAL ASSETS				
Cash and cash equivalents	\$ 13,622,766	\$ 13,622,766	\$ 39,090,565	\$ 39,090,565
Investment securities (total)	55,064,620	54,824,915	47,583,408	47,400,282
Federal Home Loan Bank stock	1,704,500	1,704,500	2,431,600	2,431,600
Loans held for sale	7,489,290	7,524,363	13,767,109	13,798,773
Loans, net	256,870,293	258,073,223	244,605,910	245,175,511
FINANCIAL LIABILITIES				
Noninterest-bearing deposits	50,069,560	50,069,560	67,010,985	67,010,985
Interest-bearing deposits	227,834,241	227,711,750	204,615,518	204,132,515
Federal funds purchased and securities sold under agreements to repurchase	13,405,463	13,405,463	9,280,348	9,280,348
Notes payable — U.S. Treasury	—	—	1,932,124	1,932,124
Advances from the Federal Home Loan Bank	22,000,000	21,995,650	40,000,000	42,069,827

21. SEGMENT INFORMATION

The Company has reportable segments that are strategic business units offering complimentary products and services to the core business of banking. The accounting policies of the segments are the same as those described in the summary of significant accounting policies. The Company provides the accounting for all segments and charges a management fee for this service to the other segments. The Company has also lent money to various segments with terms similar to those offered third parties.

The Commercial/Retail Bank segment provides full service retail and business banking services, including lending and deposit services, investment activities and other customary services associated with a bank.

The Electronic Banking segment provides national point of sale transaction originations, home banking, and debit card transaction processing.

The Brokerage segment provides full service brokerage services for stocks, bonds, mutual funds and annuities.

The Mortgage Unit segment provides residential mortgage lending products and services.

Segment information for the Company for 2006 is as follows:

	<i>Commercial/ Retail Bank</i>	<i>Electronic Banking</i>	<i>Brokerage</i>	<i>Mortgage Unit</i>	<i>Segment Totals</i>	<i>Eliminations</i>	<i>Consolidated</i>
Interest income	\$ 22,680,213	\$ —	\$ —	\$ 1,222,566	\$ 23,902,779	\$ (775,275)	\$ 23,127,504
Interest expense	(9,512,725)	—	—	—	(9,512,725)	775,275	8,737,450
Net interest income	13,167,488	—	—	1,222,566	14,390,054	—	14,390,054
Provision for loan losses	—	—	—	—	—	—	—
Noninterest income	3,779,786	2,013,943	647,301	2,457,966	8,898,996	—	8,898,996
Intersegment income	793,360	23,285	1,398	(724,140)	93,903	(93,903)	—
Noninterest expenses	(16,102,581)	(701,085)	(402,917)	(2,268,323)	(19,474,906)	93,903	19,381,003
Income before income taxes	1,638,053	1,336,143	245,782	688,069	3,908,047	—	3,908,047
Income taxes	(441,553)	(516,018)	(93,441)	(272,276)	(1,323,268)	—	(1,323,268)
Net income	<u>\$ 1,196,520</u>	<u>\$ 820,125</u>	<u>\$ 152,341</u>	<u>\$ 415,793</u>	<u>\$ 2,584,779</u>	<u>\$ —</u>	<u>\$ 2,584,779</u>
Segment assets	\$ 348,578,067	\$ 15,848	\$ 26,702	\$ 17,736,965	\$ 366,357,582	\$ (16,532,830)	\$ 349,824,752
Expenditures for segment purchases of premises, equipment and software	\$ 885,945	\$ —	\$ —	\$ 15,456	\$ 901,401	\$ —	\$ 901,401

A reconciliation of total segment assets to consolidated total assets follows as of December 31, 2006:

Total segment assets	\$ 366,357,582
Elimination of intersegment loans	(14,934,950)
Elimination of intersegment deposit accounts	(1,597,880)
	<u>\$ 349,824,752</u>

Segment information for the Company for 2005 is as follows:

	<i>Commercial/ Retail Bank</i>	<i>Electronic Banking</i>	<i>Brokerage</i>	<i>Mortgage Unit</i>	<i>Segment Totals</i>	<i>Eliminations</i>	<i>Consolidated</i>
Interest income	\$ 17,177,300	\$ —	\$ —	\$ 1,366,403	\$ 18,543,703	\$ 527,676	\$ 19,071,379
Interest expense	(6,741,963)	(105,444)	—	—	(6,847,407)	(527,676)	(7,375,083)
Net interest income	10,435,337	(105,444)	—	1,366,403	11,696,296	—	11,696,296
Provision for loan losses	—	—	—	—	—	—	—
Noninterest income	2,466,304	4,871,076	667,510	2,713,746	10,718,636	—	10,718,636
Intersegment income	598,180	—	2,906	(512,785)	88,301	(88,301)	—
Noninterest expenses	(11,919,891)	(3,727,831)	(412,222)	(2,662,481)	(18,722,425)	88,301	(18,634,124)
Income before income taxes	1,579,930	1,037,801	258,194	904,883	3,780,808	—	3,780,808
Income taxes	(472,393)	(400,798)	(99,714)	(349,466)	(1,322,371)	—	(1,322,371)
Net income	<u>\$ 1,107,537</u>	<u>\$ 637,003</u>	<u>\$ 158,480</u>	<u>\$ 555,417</u>	<u>\$ 2,458,437</u>	<u>\$ —</u>	<u>\$ 2,458,437</u>
Segment assets	\$ 358,760,082	\$ 3,691,629	\$ 82,512	\$ 23,749,243	\$ 386,283,466	\$ (25,816,320)	\$ 360,467,146
Expenditures for segment purchases of premises, equipment and software	\$ 655,832	\$ 211,910	\$ —	\$ 35,201	\$ 902,943	\$ —	\$ 902,943

A reconciliation of total segment assets to consolidated total assets follows as of December 31, 2005:

Total segment assets	\$ 386,283,466
Elimination of intersegment loans	(25,065,528)
Elimination of intersegment deposit accounts	(750,792)
	<u>\$360,467,146</u>

22. CONSOLIDATED QUARTERLY RESULTS OF OPERATIONS (UNAUDITED)

	Year Ended December 31, 2006			
	<i>First Quarter</i>	<i>Second Quarter</i>	<i>Third Quarter</i>	<i>Fourth Quarter</i>
Interest income	\$ 5,566,706	\$5,652,219	\$5,855,415	\$6,053,164
Interest expense	<u>2,082,985</u>	<u>2,052,221</u>	<u>2,237,219</u>	<u>2,365,025</u>
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	<u>6,088,968</u>	<u>5,558,716</u>	<u>3,859,040</u>	<u>3,874,280</u>
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	<u>\$ 867,858</u>	<u>\$ 58,370</u>	<u>\$ 855,111</u>	<u>\$ 803,440</u>
Net income per share — basic	<u>\$ 0.31</u>	<u>\$ 0.02</u>	<u>\$ 0.30</u>	<u>\$ 0.29</u>
Cash dividends per share	<u>\$ 0.11</u>	<u>\$ 0.11</u>	<u>\$ 0.11</u>	<u>\$ 0.12</u>
Market prices: high	<u>\$ 15.95</u>	<u>\$ 18.80</u>	<u>\$ 18.00</u>	<u>\$ 19.45</u>
low	<u>\$ 14.40</u>	<u>\$ 15.64</u>	<u>\$ 16.11</u>	<u>\$ 16.99</u>

	Year Ended December 31, 2005			
	<i>First Quarter</i>	<i>Second Quarter</i>	<i>Third Quarter</i>	<i>Fourth Quarter</i>
Interest income	\$ 4,275,029	\$ 4,512,073	\$ 4,957,555	\$ 5,326,722
Interest expense	<u>(1,555,268)</u>	<u>(1,766,890)</u>	<u>(1,937,526)</u>	<u>(2,115,399)</u>
Net interest income	2,719,761	2,745,183	3,020,029	3,211,323
Gains on security sales	73,087	—	766,772	—
Other noninterest income	2,255,502	2,649,218	2,615,235	2,358,822
Noninterest expenses	<u>(4,367,243)</u>	<u>(4,435,408)</u>	<u>(4,736,498)</u>	<u>(5,094,975)</u>
Income before income taxes	681,107	958,993	1,665,538	475,170
Income taxes	(268,511)	(324,661)	(629,609)	(99,590)
Net income	<u>\$ 412,596</u>	<u>\$ 634,332</u>	<u>\$ 1,035,929</u>	<u>\$ 375,580</u>
Net income per share — basic	<u>\$ 0.15</u>	<u>\$ 0.22</u>	<u>\$ 0.37</u>	<u>\$ 0.13</u>
Cash dividends per share	<u>\$ 0.10</u>	<u>\$ 0.10</u>	<u>\$ 0.10</u>	<u>\$ 0.10</u>
Market prices: high	<u>\$ 17.00</u>	<u>\$ 17.00</u>	<u>\$ 16.29</u>	<u>\$ 15.00</u>
low	<u>\$ 14.12</u>	<u>\$ 14.25</u>	<u>\$ 13.95</u>	<u>\$ 14.00</u>

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 2006.

ITEM 9A: CONTROLS AND PROCEDURES

The Company's principal executive officer and principal financial officer have concluded that the Company's disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934) are effective based on the evaluation of these controls and procedures by the Company's management, including our principal executive and principal financial officers, as of December 31, 2006. There were no changes in the Company's internal controls over financial reporting that occurred during the fourth fiscal quarter of 2006 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

ITEM 9B: OTHER INFORMATION

None.

PART III

ITEM 10: DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

The information required by this Item is incorporated by reference into this Item 10 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 15, 2007.

ITEM 11: EXECUTIVE COMPENSATION

The information required by this Item is incorporated by reference to the information appearing under the captions "Executive Compensation," "Long-Term Incentive Plan," and "Retirement Plans" in the Company's definitive Proxy Statement for the Annual Meeting of Shareholders to be held on May 15, 2007.

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 Certain Beneficial Owners and Management" in the Company's definitive Proxy Statement for the Annual Meeting of Shareholders to be held on May 15, 2007.

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 Relationships and Related Transactions" in the Company's definitive Proxy Statement for the Annual meeting of Shareholders to be held on May 15, 2007.

ITEM 14: PRINCIPAL ACCOUNTANT 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 15, 2007.

PART IV

ITEM 15: EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

1. Financial Statements

Carrollton Bancorp and Subsidiaries:

Report of Independent Registered Public Accounting Firm
 Consolidated Balance Sheets as of December 31, 2006 and 2005
 Consolidated Statements of Income for the years ended December 31, 2006, 2005, and 2004
 Consolidated Statements of Changes in Shareholders' Equity for the years ended December 31, 2006, 2005, and 2004
 Consolidated Statements of Cash Flows for the years ended December 31, 2006, 2005, and 2004
 Notes to Consolidated Financial Statements

2. Financial Statement Schedules

None

3. Exhibits

Exhibit

<i>Number</i>	<i>Description</i>
3(i)	Articles of Incorporation of Carrollton Bancorp*
3(ii)	By-Laws of Carrollton Bancorp*
10.1	Lease dated January 24, 1989 by and between Hill Management Services, Inc. and The Carrollton Bank of Baltimore.*
10.2	Lease dated July 21, 1989 by and between Hill Management Services, Inc. and The Carrollton Bank of Baltimore.*
10.4	Lease dated August 3, 1976 between Amcap, Inc. and The Carrollton Bank of Baltimore.*
10.7	Lease dated July 19, 1988 by and between Northway Limited Partnership and The Carrollton Bank of Baltimore.*
10.8	Lease dated August 11, 1994 by and between KIMCO and Carrollton Bank.**
10.9	Lease dated October 11, 1994 by and between Ridgeview Associates Limited Partnership and Carrollton Bank.**
10.10	Employment agreement with Robert A. Altieri***
10.11	Employment agreement with Gary M. Jewell***
10.12	Lease dated January 15, 2004 by and between Turf Village Offices and Carrollton Bank (2300 York Road, Suite 114, 115, 116)
10.13	Lease dated June 17, 2004 by and between Turf Village Offices and Carrollton Bank (2300 York Road, Suite 211)
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
10.19	Lease dated October 31, 1997 between The Avenue at White Marsh, 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
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

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

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

*** Incorporated by reference from Quarterly Report on Form 10-Q for the quarter ended September 30, 2004 (1934 Act 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 1, 2007 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 1, 2007 By: /s/ Robert A. Altieri
Robert A. Altieri
President and Chief Executive Officer

PRINCIPAL FINANCIAL AND ACCOUNTING OFFICER

March 1, 2007 By: /s/ James M. Uveges
James M. Uveges
(Principal financial and accounting officer)
Senior Vice President and Chief Financial Officer

Board of Directors

March 1, 2007 By: /s/ Robert J. Aumiller
Robert J. Aumiller
Director

March 1, 2007 By: /s/ Steven K. Breeden
Steven K. Breeden
Director

March 1, 2007 By: /s/ Albert R. Counselman
Albert R. Counselman
Chairman of the Board

March 1, 2007 By: /s/ Harold I. Hackerman
Harold I. Hackerman
Director

March 1, 2007 By: /s/ William L. Hermann
William L. Hermann
Director

March 1, 2007 By: /s/ David P. Hessler
David P. Hessler
Director

March 1, 2007 By: /s/ Howard S. Klein
Howard S. Klein
Director

March 1, 2007 By: /s/ Ben F. Mason
Ben F. Mason
Director

March 1, 2007 By: /s/ Charles E. Moore, Jr.
Charles E. Moore, Jr.
Director

March 1, 2007 By: /s/ John Paul Rogers
John Paul Rogers
Director

March 1, 2007 By: /s/ William C. Rogers, Jr.
William C. Rogers, Jr.
Director

March 1, 2007 By: /s/ Francis X. Ryan
Francis X. Ryan
Director

EXHIBIT INDEX

<i>Exhibit Number</i>	<i>Description</i>	<i>Sequentially Numbered Page</i>
3(i)	Articles of Incorporation of Carrollton Bancorp	*
3(ii)	By-Laws of Carrollton Bancorp	*
10.1	Lease dated January 24, 1989 by and between Hill Management Services, Inc. and The Carrollton Bank of Baltimore.	*
10.2	Lease dated July 21, 1989 by and between Hill Management Services, Inc. and The Carrollton Bank of Baltimore.	*
10.4	Lease dated August 3, 1976 between Amcap, Inc. and The Carrollton Bank of Baltimore.	*
10.7	Lease dated July 19, 1988 by and between Northway Limited Partnership and The Carrollton Bank of Baltimore.	*
10.8	Lease dated August 11, 1994 by and between KIMCO and Carrollton Bank.	**
10.9	Lease dated October 11, 1994 by and between Ridgeview Associates Limited Partnership and Carrollton Bank.	**
10.10	Employment agreement with Robert A. Altieri	***
10.11	Employment agreement with Gary M. Jewell	***
10.12	Lease dated January 15, 2004 by and between Turf Village Offices and Carrollton Bank (2300 York Road, Suite 114, 115, 116)	
10.13	Lease dated June 17, 2004 by and between Turf Village Offices and Carrollton Bank (2300 York Road, Suite 211)	
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	
10.19	Lease dated October 31, 1997 between The Avenue at White Marsh, 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	
21.1	Subsidiaries of Carrollton Bancorp	
23.1	Consent of Independent Registered Public Accounting Firm required by Exchange Act Rule 13-a-14(a)	
31.1	Certification by the Principal Executive Officer required by Exchange Act Rule 13a-14(a)	
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	

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

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

*** Incorporated by reference from Quarterly Report on Form 10-Q for the quarter ended September 30, 2004 (1934 Act File No.: 000-23090)

EXHIBIT 21.1

<i>Subsidiaries of Carrollton Bancorp</i>	<i>State of Incorporation</i>	<i>Owned by</i>	<i>Percentage Ownership</i>
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 February 23, 2007 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
February 23, 2007

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 the 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 officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15-15(c) 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 controls 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 principals;
 - (c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of this 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 fourth fiscal quarter 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 officers and I have disclosed to the registrant's auditors and the registrant's audit committee of the board of directors:
 - (a) all significant deficiencies and material weaknesses in the design or operation of internal controls over financial reporting which could 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 controls over financial reporting.

/s/ ROBERT A. ALTIERI

Robert A. Altieri

President and Chief Executive Officer

Date: March 1, 2007

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 in order 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 officers 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)) 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 controls 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 principals;
 - (c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of this 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 fourth fiscal quarter 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 officers and I have disclosed to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent function):
 - (a) all significant deficiencies and material weaknesses in the design or operation of internal controls over financial reporting which are reasonably like 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 1, 2007

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, 2006, 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, 2006, 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 1, 2007

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, 2006, 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, 2006, 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 1, 2007

DIRECTORS AND OFFICERS AS OF MARCH 30, 2007

DIRECTORS (1)

Robert J. Aumiller
Executive Vice President
MacKenzie Commercial Real Estate Services

Steven K. Breedon
Managing Member
Security Development, LLC

Albert R. Counselman
President and Chief Executive Officer
Riggs, Counselman, Michaels & Downes, Inc.

Harold I. Hackerman
Vice President
Ellin & Tucker, Chartered

William L. Hermann
President and CEO
William L. Hermann, Inc.

David P. Hessler
President and CEO
Eastern Sales and Engineering Co.

Howard S. Klein
Vice President and General Counsel
Klein's Super Markets

Ben F. Mason
Director Of Institutional Education
Sojourner-Douglass College

Charles E. Moore, Jr.
President and CFO
TelAtlantic Communications, Inc.

John Paul Rogers
Attorney

William C. Rogers, Jr.
Attorney

Francis X. Ryan
President
F.X. Ryan & Associates

William McCallister
Director Emeritus

(1) Effective January 26, John P. Hauswald resigned as Director from the Company

CARROLLTON MORTGAGE SERVICES, INC.

Robert A. Altieri
President

Ron Antrim
Vice President

Brian Bogdan
Vice President

Melanie Cox
Vice President

James M. Uveges
Treasurer

OFFICERS

CARROLLTON BANCORP

Albert R. Counselman
Chairman of the Board

Robert A. Altieri
President and Chief Executive Officer

Allyson Cwiek—*Vice President and Secretary*

James M. Uveges—*Senior Vice President and Chief Financial Officer*

CARROLLTON BANK

John Paul Rogers
Chairman of the Board

Robert A. Altieri
President and Chief Executive Officer

Allyson Cwiek—*Vice President and Secretary*

Senior Vice Presidents: (2)

Edward R. Bootey—*Operations*

Michael J. Camiel—*Credit*

William D. Sherman—*Lending*

Gary M. Jewell—*Electronic Banking*

Deanna L. Lintz—*Branch Administration*

Lola B. Stokes—*CRA/Compliance*

James M. Uveges—*Chief Financial Officer*

Vice Presidents:

Kevin Carter—*Commercial Lending*

Leroy J. Cummins—*Audit*

Stephen G. Hyman—*Commercial Lending*

Julia Kaufman—*Loan Servicing*

Robert J. Morales—*Operations*

Joyce F. Murphy—*Electronic Banking*

Cathy Regan—*Human Resources*

Harry Schultheis—*Commercial Lending*

Rosemarie Schwartz—*Controller*

Mark Sergi—*Commercial Lending*

Gary Smith—*Commercial Lending*

Eunice W. Taylor—*Electronic Banking*

Victor Zubar—*MIS*

Assistant Vice Presidents:

Gary Allgeier—*Finance*

William Brown—*Data Processing*

Patricia Harris—*Branch Administration*

Tari Mitchell—*Commercial Lending*

Lori Ratzburg—*Credit*

Donna Smith—*Customer Service*

Robert J. Tolson—*Loan Servicing*

(2) Effective January 26, 2007, Robert J. Hickey resigned as Senior Vice President, Branch Administration. Effective March 23, 2007, John A. Giovanazi resigned as Senior Vice President, Lending.

CARROLLTON FINANCIAL SERVICES, INC.

Brian J. Culloty
Chairman of the Board and President

Steven Moore
Vice President and Secretary

CARROLLTON COMMUNITY DEVELOPMENT CORPORATION

William D. Sherman
President

SHAREHOLDER INFORMATION

BUSINESS SUMMARY

Carrollton Bancorp (the Company) is a bank holding company registered under the Bank Holding Company Act of 1956, and was organized on January 11, 1990. Carrollton Bank is a Maryland State chartered commercial bank and the principal subsidiary of the Company. The Bank was incorporated under the laws of the State of Maryland in 1903 and is engaged in a general commercial and retail banking business. Carrollton Financial Services, Inc., a subsidiary of the Bank, provides full service brokerage services for stocks, bonds, mutual funds and annuities. Carrollton Mortgage Services, Inc., also a subsidiary of the Bank, is a residential mortgage lender.

The Bank operates 10 full service branch offices in Baltimore County, Baltimore City, Anne Arundel, and Harford County, Maryland. The Bank offers a wide range of both personal and commercial deposit and loan services. The Bank expects to open a new full service branch in Cockeysville in May or June 2007.

The Bank and its subsidiaries currently have 138 full time equivalent employees. Management considers its relationship with its employees to be good.

The Bank faces strong competition in its market area. Its most direct competition for deposits comes from other commercial banks, savings banks, savings and loan associations and credit unions. It also competes for deposits with brokerage houses, mutual funds and, to a lesser extent, the securities markets. The Bank also competes with the same banking entities for loans, as well as with mortgage banking companies and other institutional lenders. Some of the Bank's competitors have assets and operating capacity which exceed that of the Bank.

The Company is subject to regulation and examination by the Federal Reserve Board, and is required to file periodic reports and any additional information that the Federal Reserve Board may require. The Bank is subject to supervision, regulation and examination by the Department of Labor, Licensing and Regulation of the State of Maryland and the Federal Deposit Insurance Corporation.

CORPORATE HEADQUARTERS:
344 North Charles Street, Suite 300
Baltimore, Maryland 21201
Phone: (410) 536-4600
Internet: www.carrolltonbank.com

INVESTMENT SUBSIDIARY:
Carrollton Financial Services, Inc.
The Avenue at White Marsh
8157A Honeygo Blvd.
White Marsh, Maryland 21236
Phone: (410) 242-6418
(800) 851-0851

MORTGAGE SUBSIDIARY:
Carrollton Mortgage Services, Inc.
2300 York Road, Suite 115
Timonium, Maryland 21093

ANNUAL MEETING NOTICE:
The annual meeting of shareholders of Carrollton Bancorp will be held on Tuesday, May 15, 2007 at 10 a.m. at the Corporate Headquarters, 344 North Charles Street, Baltimore, Maryland.

STOCK LISTING:
The common stock of Carrollton Bancorp trades on the NASDAQ National Market tier of The NASDAQ Stock Market under the symbol "CRRB". There were 390 record holders of stock at December 31, 2006.

TRANSFER AGENT AND REGISTRAR:
American Stock Transfer & Trust Company
59 Maiden Lane
New York, New York 10038
Phone: (800) 937-5449
(212) 936-5100
Internet: www.amstock.com

DIVIDEND REINVESTMENT:

Carrollton Bancorp offers a Dividend Reinvestment Plan that provides automatic reinvestment of dividends in additional shares of Carrollton Bancorp common stock. For more information contact:

American Stock Transfer & Trust Company
59 Maiden Lane
New York, New York 10038
Phone: (800) 937-5449
(212) 936-5100
Internet: www.amstock.com

INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM:

Rowles & Company, LLP
101 E. Chesapeake Avenue, Suite 300
Baltimore, Maryland 21286

During 2006 and 2005, there were no disagreements with the Company's accountants on accounting matters or financial disclosure.

ADDITIONAL INFORMATION:

The Company files an annual report with the Securities and Exchange Commission on Form 10-K. Any shareholder may obtain a copy, without charge, upon request to the Company's Chief Financial Officer.

ANALYSTS, INVESTORS, AND OTHERS SEEKING FINANCIAL INFORMATION ABOUT THE COMPANY ARE INVITED TO CONTACT:

James M. Uveges
Chief Financial Officer
Carrollton Bancorp
344 North Charles Street
Baltimore, Maryland 21201
Phone: (410) 536-7308
Email: juveges@carrolltonbank.com

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