2013 ANNUAL REPORT

Lotus Bancorp, Inc.

BOARD OF DIRECTORS

Sreenivas Cherukuri
Director, SC Industries

Vasudev Garlapaty
Physician, Oakwood Hospital

Vinaya Gavini, MD
Physician, Providence Hospital

Armanath Gowda
Attorney

Ravindranath Gullapalli
Real Estate Investor

Murali Guthikonda, MD
Physician, DMC Harper Hospital

Lynn Jerath
President, Bedrock Investments, LLC

Mayur Joshi
Realtor, Max Broock Realtors

Shubha Kolachalam,
Kolachalam, MDPC

V.S. Lingam
Chief of Clinical Affairs, Reuther Psychiatric Hospital

Krishna M. Malempati
Vice President, Om Ventures, Inc.

Jitendra B. Patel
President, Michigan Inns, Inc.

Haranath Policherla, MD
Physician, Bon Secours Hospital

Neal J. Searle
President & CEO, Lotus Bancorp, Inc.

Bala Setty, MD
Physician, Oakwood Hospital

Jay Shah
Vice President, Somat Engineering

Venkat Talasila, MD
Physician, Health Source Saginaw

CORPORATE OFFICERS

Bala Setty, Chairman of the Board
Neal J. Searle, President and Chief Executive Officer
Richard E. Bauer, Executive Vice President and
Chief Financial Officer
John W. Westerheide, Senior Vice President and
Chief Lending Officer

CORPORATE HEADQUARTERS
INVESTOR RELATIONS

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44350 West Twelve Mile Road
Novi, Michigan 48377

(248) 735-1000
www.lotusbank.com www.lotusinvestor.com

STOCK TRANSFER AGENT AND REGISTRAR

Broadridge Corporate Issuer Services, Inc.
51 Mercedes Way
Edgewood, NY 11717

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LAW FIRM

Howard & Howard
450 West Fourth Street
Royal Oak, Michigan 48067

(248) 645-1483
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February 28, 2014

To our Shareholders:
On behalf of the Board of Directors of Lotus Bancorp, Inc. and our wholly owned subsidiary Lotus Bank, we are pleased to share with you our financial performance as of December 31, 2013. It has been another milestone year with outstanding asset growth, continued outstanding credit quality and the very successful expansion of our organization into our Farmington Hills office. We continue our 5 Star BauerFinancial Rating (the highest possible rating of a bank's stability and financial strength) for the 3rd consecutive year, and were rated #14 in the nation for Banks < $100 million in assets by the ABA Banking Journal in 2013.

Additionally, as of the date of this letter, your bank has reached its 7th year Anniversary. While not typically a memorable year in our personal lives, it is a momentous day in the life of Lotus Bank. We have officially exited the regulatory stage called "de novo" (*Latin* meaning from the beginning). Essentially, the Bank has aged sufficiently in the industry. Over time, this will result in reduced regulatory oversight costs, opportunities to bring new services to our clientele more quickly, and generally allow the Bank to be more agile in the market.
The following are financial highlights of our excellent performance:

- Asset Growth was $11M for a growth rate of 13%;
- Gross Loan Growth was $13.0M for a growth rate of 23%;
- Deposit Growth was $10M for a growth rate of 14%;
- A .88% Return on Assets, which is slightly below our peer group and reflects the costs associated with our branch expansion; and
- A 7% Return on Equity

Earnings per share for 2013 are substantially below 2012, and an explanation is in order. As you look at our income statement, you will note Earnings per Share were $.46 vs. $1.53. This was caused by 2 factors: 1) a large tax benefit in 2012 and the start-up costs of our large Farmington Hills location in 2013. Note the similarity of Net Income before Tax for both years. Lotus now generates taxable income going forward which directly impacts EPS. See Note 8 of the financial statement footnotes for further details on the tax calculation.

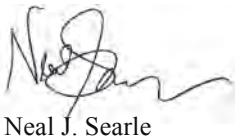
These performance metrics are an illustration of the strength of the organization and our ability to continue to grow and serve a larger client base. The Lotus Bank name is becoming better known, and with that comes more opportunities to meet the needs within the market. While the Board at present does not have a new office slated for 2014, we continue to keep an eye on the key communities on our future expansion list.

Ever-increasing regulation and increased competition will be our largest challenges in the year-ahead. Further implementation of the Dodd-Frank Act, new regulations from the Consumer Financial Protection Agency, and larger banks who have quickly forgotten the 2008-2010 financial debacles will be the focus of our attention. We are committed to consistent, conservative growth focused on our core strategic objectives:

Highly Capitalized
Profitability / Return on Equity
Shareholder Value over the long-term
Indian-centric
Independence
Effective Risk Management
Accountability

We believe we have a great team, a dynamic and fully-engaged Board of Directors, a valuable clientele, and supportive shareholders. This is what makes Lotus Bank / Lotus Bancorp, Inc. unique in the market. Our 2014 plan is aggressive, and we can achieve it as a result of your support. We believe we have set Lotus Bancorp, Inc. on the right path and hope that you will share our excitement for the future of our company.

Best regards,



Neal J. Searle
President and Chief Executive Officer

plante moran

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Independent Auditor's Report

The Board of Directors
Lotus Bancorp, Inc.

We have audited the accompanying consolidated financial statements of Lotus Bancorp, Inc. and its subsidiary, which comprise the consolidated balance sheet as of December 31, 2013 and 2012 and the related statements of income, comprehensive income, stockholders' equity, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements

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

Auditor's Responsibility

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

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

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Lotus Bancorp, Inc. and its subsidiary as of December 31, 2013 and 2012 and the consolidated results of its operations and its cash flows for the years then ended, in accordance with accounting principles generally accepted in the United States of America.

Plante & Moran, PLLC

February 21, 2014

Praxity
MEMBER
GLOBAL ALLIANCE OF INDEPENDENT FIRMS

LOTUS BANCORP, INC.
AND SUBSIDIARY
CONSOLIDATED BALANCE SHEETS

ASSETS

	December 31	
	2013	2012
Cash and Cash Equivalents		
Cash and due from banks	$ 980,256	$ 1,274,534
Federal funds sold	8,213,143	10,385,116
Total cash and cash equivalents	9,193,399	11,659,650
Securities - available for sale (Note 2)	9,816,006	9,249,903
Loans, less allowance for loan losses of $1,285,899 and $1,351,470 at December 31, 2013 and 2012, respectively (Note 3)	70,759,513	57,348,935
Property and equipment, net of depreciation (Note 7)	3,065,829	2,975,805
Accrued interest receivable and other assets	1,213,427	1,326,367
Total assets	$ 94,048,174	$ 82,560,660

LIABILITIES AND STOCKHOLDERS' EQUITY

	December 31	
	2013	2012
Deposits (Note 5)		
Non-interest bearing	$ 15,322,270	$ 12,022,846
Interest bearing	63,610,408	57,850,749
Total deposits	78,932,678	69,873,595
Borrowed Funds (Note 10)	1,900,000	-
Accrued interest payable and other liabilities	604,788	480,894
Total liabilities	81,437,466	70,354,489
Stockholders' equity		
Common stock, $0.01 par value Authorized –8,000,000 shares Issued and outstanding – 1,400,478 shares at December 31, 2013 and 1,390,365 shares at December 31, 2012	14,005	13,904
Additional paid-in capital	14,240,863	14,123,027
Unearned Compensation	(59,194)	-
Accumulated deficit	(1,454,654)	(2,100,259)
Accumulated other comprehensive income (loss)	(130,312)	169,499
Total stockholders' equity	12,610,708	12,206,171
Total liabilities and stockholders' equity	$ 94,048,174	$ 82,560,660

See Notes to Financial Statements

LOTUS BANCORP, INC.
AND SUBSIDIARY
CONSOLIDATED STATEMENT OF INCOME

	For the Year Ended December 31	
	2013	2012
Interest income:		
Loans receivable, including fees	$ 3,840,796	$ 3,683,290
Federal funds sold	13,242	17,339
Securities	253,528	207,415
Other	2,383	2,069
Total interest income	4,109,949	3,910,113
Interest expense	514,515	524,534
Net interest income	3,595,434	3,385,579
Provision for loan losses (Note 3)	-	-
Net interest income after provision for loan losses	3,595,434	3,385,579
Non-interest income		
Service charges on deposit accounts	53,490	45,789
Gain on sale of securities	-	5,971
Gain on sale of loans	108,600	-
Other income	192,985	132,756
Total non-interest income	355,075	184,516
Non-interest expense		
Salary and benefits (Note 14)	1,570,485	1,272,682
Occupancy and equipment expense	455,909	332,200
Stock-based compensation (Note 9)	29,137	25,997
Professional fees	230,920	194,331
Advertising and public relations	103,415	54,857
Data processing expenses	164,318	149,480
Insurances	71,470	108,874
Loan costs	39,859	36,084
Travel and entertainment	51,115	33,921
Printing and office supplies	50,969	30,685
Dues and memberships	11,355	11,394
Outside office services	68,221	56,273
Michigan business tax	24,000	16,800
Other expense	97,659	94,815
Total non-interest expense	2,968,832	2,418,393
Net income before income taxes	981,677	1,151,702
Income tax expense (benefit) (Note 8)	336,072	(981,140)
Net income	$ 645,605	$ 2,132,842
Basic earnings per share	$ 0.46	$ 1.53
Diluted earnings per share	$ 0.46	$ 1.53
Weighted average shares	1,400,478	1,390,365

See Notes to Financial Statements

LOTUS BANCORP, INC.
AND SUBSIDIARY
CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

	For the Year Ended December 31	
	2013	2012
Net income	$ 645,605	$ 2,132,842
Other comprehensive (loss)		
Unrealized loss on securities		
Change in unrealized gain arising during the year	(366,942)	(7,150)
Total unrealized loss on securities	(366,942)	(7,150)
Tax effect	67,131	-
Other comprehensive (loss) income	(299,811)	(7,150)
Comprehensive income	$ 345,794	$ 2,125,692

LOTUS BANCORP, INC.
AND SUBSIDIARY
CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY

	Common Stock	Paid-in Capital	Accumulated Deficit	Unearned Compensation	Accumulated Other Comprehensive Income (loss)	Total
Balance January 1, 2012	$ 13,904	$ 14,097,030	$ (4,233,101)	$ -	$ 176,649	$ 10,054,482
Comprehensive loss:						
Net income	-	-	2,132,842	-	-	2,132,842
Change in unrealized gain on securities available for sale	-	-	-	-	(7,150)	(7,150)
Total comprehensive income						2,125,692
Options expense	-	25,997	-	-	-	25,997
Balance December 31, 2012	13,904	14,123,027	(2,100,259)	-	169,499	12,206,171
Comprehensive income:						
Net income	-	-	645,605	-	-	645,605
Change in unrealized gain on securities available for sale – net of tax	-	-	-	-	(299,811)	(299,811)
Total comprehensive income						345,794
Restricted stock issued	101	88,699	-	(88,800)	-	-
Restricted stock compensation	-	-	-	29,606	-	29,606
Options expense	-	29,137	-	-	-	29,137
Balance December 31, 2013	$ 14,005	$ 14,240,863	$ (1,454,654)	$ (59,194)	$ (130,312)	$ 12,610,708

See Notes to Financial Statements

LOTUS BANCORP, INC.
AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS

	For the Year Ended December 31	
	2013	2012
CASH FLOWS FROM OPERATING ACTIVITIES		
Adjustments to reconcile net income to net cash from operating activities		
Net income	$ 645,605	$ 2,132,842
Stock option expense	29,137	25,997
Restricted stock compensation	29,606	-
Depreciation	169,734	158,940
Amortization of securities	34,717	30,655
(Increase) decrease in other assets	180,071	(840,294)
Increase in other liabilities	123,894	234,579
Net cash provided by operating activities	1,212,764	1,742,719
CASH FLOWS FROM INVESTING ACTIVITIES		
Net increase in loans	(13,410,578)	(6,083,348)
Purchases of securities	(1,464,811)	(6,569,613)
Maturities of securities	497,049	5,784,053
Gain on sale of securities	-	(5,971)
Purchase of equipment	(259,758)	(198,395)
Net cash used in investing activities	(14,638,098)	(7,073,274)
CASH FLOWS FROM FINANCING ACTIVITIES		
Increase in non-interest bearing deposits	3,299,424	4,150,528
Increase in interest bearing deposits	5,759,659	6,235,234
Increase in FHLB Advances	1,900,000	-
Net cash provided by financing activities	10,959,083	10,385,762
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(2,466,251)	5,055,207
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	11,659,650	6,604,443
CASH AND CASH EQUIVALENTS AT END OF YEAR	$ 9,193,399	$ 11,659,650
Supplemental Disclosure of Non-cash Activity:		
Cash paid for interest	$ 508,194	$ 508,444
Cash paid for income taxes	$ -	$ -

See Notes to Financial Statements

LOTUS BANCORP, INC.
AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING PRINCIPLES

Basis of Financial Statement Presentation – The accompanying consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America.

Principles of Consolidation - The consolidated financial statements include the accounts of Lotus Bancorp, Inc. (the "Company") and its wholly owned subsidiary, Lotus Bank (the "Bank"). All significant inter-company accounts and transactions have been eliminated.

Organization – Lotus Bancorp, Inc. (the "Company") was incorporated as De Novo Holdings, Inc. on October 27, 2004 for the purpose of becoming a bank holding company under the Bank Holding Company Act of 1956, as amended. The Company subsequently changed its name to Lotus Bancorp, Inc. The Company received the required regulatory approvals to purchase the common stock of Lotus Bank (the "Bank") on February 2, 2007. The Company withdrew common stock subscription funds totaling $12,582,050 from its escrow account on February 27, 2007 and capitalized the Bank with $10,500,000 on that same date. The Bank commenced operations on February 28, 2007. The Company completed the public offering of its common stock on June 30, 2007. The Company raised a total of $13,899,650 in capital. Direct costs relating to the offering of common stock totaled approximately $487,000 and were capitalized and netted against the offering proceeds.

On March 5, 2010, the Company filed Form 15 to terminate the registration of its common stock with the Securities and Exchange Commission, which ended the Company's obligation to file periodic and annual reports with the Commission.

On August 30, 2012, the Company down-streamed an additional $1,000,000 in capital to the Bank, primarily for legal lending limit and loan concentration purposes.

Use of Estimates – The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates and assumptions. Material estimates that are particularly susceptible to significant change in the near term include the determination of the allowance for loan losses, valuation of investment securities, and the valuation of deferred tax assets.

Cash and Cash Equivalents – Cash and cash equivalents are comprised of highly liquid investments with purchase maturities of three months or less. Cash equivalents are carried at cost, which approximates fair value. At times bank balances may be in excess of insured limits. Management has deemed this a normal business risk.

Securities – Securities are classified as "available-for-sale" and are recorded at fair value, with unrealized gains and losses excluded from earnings and reported in other comprehensive income. Purchase premiums and discounts are recognized in interest income using the interest method over the terms of the securities. Declines in the fair value of held-to-maturity and available-for-sale securities below their cost is deemed to be other than temporary are reflected in earnings as realized losses. In estimating other than temporary impairment losses, management considers (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near term prospects of the issuer, and (3) the intent and ability of the Company to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value. Gains and losses on the securities are recorded on the settlement date and are determined using the specific identification method.

Loans – The Company grants mortgage, commercial and consumer loans to customers. A large portion of the loan portfolio is represented by commercial and commercial real estate loans in Oakland County, Michigan and elsewhere. The ability of the Company's debtors to honor their contracts is dependent upon the real estate and general economic conditions in those areas.

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or pay-off are reported at their outstanding unpaid principal balances adjusted for charge-offs, the allowance for loan losses, and any deferred fees or costs on originated loans. Interest income is accrued on the unpaid principal balance. Loan origination fees, net of certain direct origination costs, are deferred and recognized as an adjustment of the related loan yield using either the straight-line or interest method.

The accrual of interest on loans is discontinued at the time the loan is 90 days delinquent unless the credit is well secured and in the process of collection. In all cases, loans are placed on nonaccrual or charged off at an earlier date if collection of principal or interest is considered doubtful.

All interest accrued but not collected for loans that are placed in nonaccrual or charged off is reversed against interest income. The interest on these loans is accounted for on the cash basis or cost-recovery method, until qualifying for return to accrual. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

Allowance for Loan Losses – The allowance for loan losses is established as losses are estimated to have occurred through a provision for loan losses charged to earnings. Actual loan losses are charged against the allowance when management believes the uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance.

The allowance for loan losses is evaluated on a regular basis by management and is based upon management's periodic review of the collectability of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral, and prevailing economic conditions. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available.

The allowance consists of specific, general and unallocated components. The specific component relates to loans that are classified as either doubtful or substandard. For such loans that are also classified as impaired, an allowance is established when the discounted cash flows (or collateral value or observable market price) of the impaired loan is lower than the carrying value of that loan. The general component covers non-classified loans and is based on historical loss experience adjusted for qualitative factors. An unallocated component is maintained to cover uncertainties that could affect management's estimates of probable losses. The unallocated component of the allowance reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating specific and general losses in the portfolio.

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

Large groups of homogeneous loans are collectively evaluated for impairment.

During the first seven years of operation, the Bank will maintain an allowance for loan losses at or above a minimum level of 1.00% of loans as established by the Federal Deposit Insurance Corporation and the State of Michigan Office of Financial and Insurance Regulation pursuant to their orders granting the Bank authority to commence activity as a de novo financial institution.

Troubled Debt Restructurings – Troubled debt restructuring of loans is undertaken to improve the likelihood that the loan will be repaid in full under the modified terms in accordance with a reasonable repayment schedule. All modified loans are evaluated to determine whether the loans should be reported as a Troubled Debt Restructure (TDR). A loan is a TDR when the Company, for economic or legal reasons related to the borrower's financial difficulties, grants a concession to the borrower by modifying or renewing a loan that the Company would not otherwise consider. To make this determination, the Company must determine whether (a) the borrower is experiencing financial difficulties and (b) the Company granted the borrower a concession. This determination required consideration of all the facts and circumstances surrounding the modification. An overall general decline in the economy or some deterioration in a borrower's financial condition does not automatically mean the borrower is experiencing financial difficulties.

Off-balance-sheet Instruments – In the ordinary course of business, the Company has entered into commitments under commercial lines of credit and standby letters of credit. Such financial instruments are recorded when they are funded.

Property and Equipment – Equipment is stated at cost. Depreciation is computed for financial reporting purposes using the straight-line method over the useful lives of the assets.

Income Taxes – Deferred income tax assets and liabilities are determined using the liability (or balance sheet) method. Under this method, the net deferred tax asset or liability is determined based on the tax effect of the various temporary differences between the book value and tax basis of the various balance sheet assets and liabilities, and requires the current recognition of changes in tax rates and laws. Valuation allowances are established, when necessary, to reduce deferred tax assets to the amount expected to be realized.

Net Income per Share – Basic income per share has been computed by dividing the net income by the weighted-average number of common shares outstanding for the period. The Company uses the treasury stock method to compute diluted earnings per share, which assumes the proceeds from an assumed exercise of stock options would be used to purchase common stock at the average market price during the period.

Comprehensive Income – Accounting principles generally require that recognized revenues, expenses, gains and losses be included in net income. Although certain changes in assets and liabilities, such as unrealized gains and losses on available-for-sale securities, are reported as a separate component of the equity section of the consolidated balance sheet, such items, along with net income (loss), are components of comprehensive income.

Reclassification – Certain amounts appearing in the prior year's financial statements have been reclassified to conform to the current year's financial statements.

Subsequent Events – The consolidated financial statements and related disclosures include evaluation of events up through and including February 21, 2014, which is the date the consolidated financial statements were issued.

Recent Accounting Pronouncements

Definition of a Public Entity – In 2013 the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2013-12, Definition of a Public Company – An Addition to the Master Glossary. The Update defines a public business entity. The Accounting Standards Codification includes multiple definitions of the terms nonpublic entity and public entity. The amendment provides a single definition of public business entity for use in future financial accounting and reporting guidance and does not affect existing requirements. The amendment defines a public company as 1) An entity that is required by the SEC to file or furnish financial statements with the SEC, or does file or furnish financial statements with the SEC, is considered a public business entity, 2) A consolidated subsidiary of a public company is not considered a public business entity for purposes of its standalone financial statements other than those included in an SEC filing by its parent, or 3) A business entity that has securities that are not subject to contractual restrictions on transfer and that is by law, contract, or regulation required to prepare U.S. GAAP financial statements (including footnotes) and make them publicly available on a periodic basis is considered a public business entity.

Reporting of Amounts Reclassified out of Accumulated Other Comprehensive Income – In 2013 the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2013-02, The Reporting of Amounts Reclassified out of Accumulated Other Comprehensive Income. The Update does not change the current requirements for reporting net income or other comprehensive income in financial statements. However, the amendments require an entity to provide information about the amounts reclassified out of accumulated other comprehensive income (AOCI) by component. In addition, an entity is required to present, either on the face of the statement where net income is presented (or in the notes), significant amounts reclassified out of AOCI by the respective line items on net income but only if the amount reclassified is required under U.S. GAAP to be reclassified to net income in its entirety in the same repowering period. For other amounts that are not required under U.S. GAAP to be reclassified in their entirety to net income, an entity is required to cross-reference to other disclosures required under U.S. GAAP that provide additional detail about those amounts. This standard is effective for reporting periods beginning after December 15, 2013.

NOTE 2 - SECURITIES

The amortized cost and fair value of available-for-sale securities, with gross unrealized gains and losses, at December 31, 2013 are as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. government and federal agency	$ 3,594,211	$ -	$ (202,551)	$ 3,391,660
Corporate	701,812	1,875	(26,961)	676,726
Municipal	5,717,426	110,173	(79,979)	5,747,620
Total available-for-sale Securities	$ 10,013,449	$ 112,048	$ (309,491)	$ 9,816,006

The amortized cost and fair value of available-for-sale securities, with gross unrealized gains and losses, at December 31, 2012 are as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. government and federal agency	$ 2,562,400	$ 2,363	$ (16,729)	$ 2,548,034
Corporate	606,994	7,503	-	614,497
Municipal	5,911,010	182,086	(5,724)	6,087,372
Total available-for-sale Securities	$ 9,080,404	$ 191,952	$ (22,453)	$ 9,249,903

At December 31, 2013 and 2012, no securities were pledged to secure borrowing public deposits and for other purposes or permitted by law.

The amortized cost and fair value of available-for-sale securities by contractual maturity at December 31, 2013 are as follows:

	Amortized Cost	Fair Value
Due in one year or less	$ 3,273,633	$ 3,196,223
Due in one through five years	3,737,407	3,799,488
Due after five years through ten years	3,002,409	2,820,295
Total	$ 10,013,449	$ 9,816,006

Information pertaining to available-for-sale securities with gross unrealized losses at December 31, 2013, aggregated by investment category and length of time that individual securities have been in a continuous loss position, follows:

	Less Than Twelve Months		Over Twelve Months	
	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value
U.S. government and agency	$ 83,344	$ 1,916,656	$ 119,207	$ 1,380,004
Corporate	26,961	524,619	-	-
Municipal	69,318	1,441,082	10,661	199,634
Total available-for-sale securities	$ 179,623	$ 3,882,357	$ 129,868	$ 1,579,638

Information pertaining to available-for-sale securities with gross unrealized losses at December 31, 2012, aggregated by investment category and length of time that individual securities have been in a continuous loss position, follows:

	Less Than Twelve Months		Over Twelve Months	
	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value
U.S. government and agency	$ 16,729	$ 1,482,402	$ -	$ -
Corporate	-	-	-	-
Municipal	5,724	206,620	-	-
Total available-for-sale securities	$ 22,453	$ 1,689,022	$ -	$ -

Unrealized losses on securities have not been recognized into income because the issuer's bonds are of high credit quality, the Company has the intent and ability to hold the securities for the foreseeable future, and the decline in fair value is primarily due to increased market interest rates. The fair value is expected to recover as the bonds approach the maturity date.

NOTE 3 – LOANS

A summary of the balances of loans as of December 31, 2013 and 2012, respectively, is as follows.

	2013	2012
Mortgage loans on real estate:		
Residential 1 to 4 family	$ 8,406,895	$ 3,695,289
Commercial	48,670,989	43,144,945
Second mortgage	110,405	166,639
Equity lines of credit	1,042,350	808,864
Total mortgage loans on real estate	58,230,639	47,815,737
Commercial loans	13,584,119	10,674,664
Consumer installment loans	274,903	273,009
Total loans	72,089,661	58,763,410
Less:		
Allowance for loan losses	1,285,899	1,351,470
Net deferred loan fees	44,249	63,005
Net loans	$ 70,759,513	$ 57,348,935

An analysis of the allowance for loan losses follows:

	2013	2012
Balance at beginning of year	$ 1,351,470	$ 1,388,238
Provision for loan losses	-	-
Loans charged off	(65,571)	(41,818)
Recoveries on loans previously charged off	-	5,050
Balance at end of year	$ 1,285,899	$ 1,351,470

In the ordinary course of business, the Bank has granted loans to executive officers and directors and their affiliates amounting to $3,113,328 at December 31, 2013 and $1,485,625 at December 31, 2012. During the year ended December 31, 2013, total principal additions were $1,863,480 and total principal payments were $235,777.

NOTE 4 – LOANS and ALLOWANCE FOR LOAN LOSSES

Loans and the allowance for loan losses are disaggregated by segment as of and for the year ended December 31, 2013 as follows:

Allowance:	Real estate-construction	Real estate-residential	Real estate-commercial	Commercial and industrial	Consumer	Unallocated	Total
Beginning balance	$ 21,050	$ 90,311	$1,065,484	$ 171,364	$ 2,265	$ 996	$1,351,470
Charge-offs	-	-	(65,571)	-	-	-	(65,571)
Recoveries	-	-	-	-	-	-	-
Provision	(6,853)	24,692	9,828	(27,848)	1,177	(996)	-
Ending balance	$ 14,197	$ 115,003	$ 1,009,741	$ 143,516	$ 3,442	$ -	$ 1,285,899
Ending allowance balance							
Attributable to loans:							
Individually evaluated for impairment	$ -	$ -	$ 75,224	$ -	$ -	$ -	$ 75,224
Collectively evaluated for impairment	14,197	115,003	934,517	143,516	3,442	-	1,210,675
Ending balance	$ 14,197	$ 115,003	$ 1,009,741	$ 143,516	$ 3,442	$ -	$1,285,899

Loans and leases:	Real estate-construction	Real estate-residential	Real estate-commercial	Commercial and industrial	Consumer	Total
Individually evaluated for impairment	$ -	$ -	$ 1,391,312	$ -	$ -	$ 1,391,312
Collectively evaluated for impairment	1,107,199	9,559,650	46,172,478	13,584,119	274,903	70,698,349
Ending loan balance	$ 1,107,199	$ 9,559,650	$ 47,563,790	$ 13,584,119	$ 274,903	$ 72,089,661

Loans and the allowance for loan losses are disaggregated by segment as of and for the year ended December 31, 2012 as follows:

Allowance:	Real estate-construction	Real estate-residential	Real estate-commercial	Commercial and industrial	Consumer	Unallocated	Total
Beginning balance	$ 21,050	$ 132,129	$ 1,065,484	$ 166,314	$ 2,265	$ 996	$ 1,388,238
Charge-offs	-	(41,818)	-	-	-	-	(41,818)
Recoveries	-	-	-	5,050	-	-	5,050
Provision	-	-	-	-	-	-	-
Ending balance	$ 21,050	$ 90,311	$ 1,065,484	$ 171,364	$ 2,265	$ 996	$ 1,351,470
Ending allowance balance							
Attributable to loans:							
Individually evaluated for impairment	$ -	$ -	$ 77,010	$ -	$ -	$ -	$ 77,010
Collectively evaluated for impairment	21,050	90,311	988,474	171,364	2,265	996	1,274,460
Ending balance	$ 21,050	$ 90,311	$ 1,065,484	$ 171,364	$ 2,265	$ 996	$1,351,470

Loans and leases:	Real estate-construction	Real estate-residential	Real estate-commercial	Commercial and industrial	Consumer	Total
Individually evaluated for impairment	$ -	$ 294,750	$ 1,369,065	$ -	$ -	$ 1,663,815
Collectively evaluated for impairment	1,010,466	4,376,043	40,765,413	10,674,664	273,009	57,099,595
Ending loan balance	$ 1,010,466	$ 4,670,793	$ 42,134,478	$ 10,674,664	$ 273,009	$ 58,763,410

Credit Risk Grading

The Company utilizes a loan rating system as a means of identifying problem and potential problem loans. The Company assigned the following loan ratings as of December 31, 2013:

	Pass (1 – 4)	Pass with Caution (5)	Special Mention (6)	Substandard (7)	Doubtful (8)	Total
Real estate-construction:						
1-4 family residential	$ 713,193	$ -	$ -	$ -	$ -	$ 713,193
Other construction, land development and land loans	394,006	-	-	-	-	394,006
Real estate-residential:						
Revolving lines of credit	1,042,350	-	-	-	-	1,042,350
1-4 family residential	8,517,300	-	-	-	-	8,517,300
Real estate-commercial						
Multifamily	2,156,219	-	-	-	-	2,156,219
Nonfarm nonresidential	41,180,460	814,579	2,021,220	1,337,312	54,000	45,407,571
Commercial and industrial	12,544,872	858,688	180,559	-	-	13,584,119
Consumer	274,903	-	-	-	-	274,903
Total	$ 66,823,303	$ 1,673,267	$ 2,201,779	$ 1,337,312	$ 54,000	$ 72,089,661

The Company utilizes a loan rating system as a means of identifying problem and potential problem loans. The Company assigned the following loan ratings as of December 31, 2012:

	Pass (1 – 4)	Pass with Caution (5)	Special Mention (6)	Substandard (7)	Total
Real estate-construction:					
1-4 family residential	$ 1,010,466	$ -	$ -	$ -	$ 1,010,466
Other construction, land development and land loans	-	-	-	-	-
Real estate-residential:					
Revolving lines of credit	808,864	-	-	-	808,864
1-4 family residential	3,567,179	-	-	294,750	3,861,929
Real estate-commercial					
Multifamily	1,981,276	-	-	-	1,981,276
Nonfarm nonresidential	33,580,186	2,945,628	2,258,323	1,369,065	40,153,202
Commercial and industrial	10,547,228	127,436	-	-	10,674,664
Consumer	273,009	-	-	-	273,009
Total	$ 51,768,208	$ 3,073,064	$ 2,258,323	$ 1,663,815	$ 58,763,410

The Company assigned each loan into credit risk categories based on current financial information, overall debt service coverage, comparison against industry averages, collateral coverage, historical payment experience, and current economic trends. The Company uses the following definitions for credit risk ratings:

Superior (1): Loans to borrowers with unquestionable strength and a solid earnings history. This category includes loans collateralized by cash or other highly liquid collateral where such collateral is held by the bank and is substantially risk-free.

Good (2): Assets of this grade conform to all the bank's underwriting criteria and evidence a below level of credit risk. Borrower's paying capacity is strong, with stable trends. If the borrower is a company, its earnings, liquidity and capitalization compare favorably to typical companies in its industry. Secondary sources of repayment are considered to be good. Borrower's repayment capacity is good and borrower consistently complies with all major covenants.

Average (3): Assets of this grade conform to substantially all the bank's underwriting criteria and evidence an average level of credit risk. However, such assets display more susceptibility to economic, technological or political changes since they lack the above average credit strength of credits rated Good. Borrower's repayment capacity is considered to be adequate. Credit is appropriately structured and serviced, payment history is satisfactory.

Acceptable (4): Assets of this grade conform to most of the bank's underwriting criteria and evidence an acceptable, though higher than Average level of credit risk. Loans in this category require an above average level of servicing and show more reliance on collateral and guaranties to preclude a loss to the bank should adverse trends develop. If the borrower is a company, its earnings, liquidity and capitalization are slightly below average when compared to peers.

Pass with Caution (5): These loans generally have the same characteristics as those in the Acceptable (4) category. The distinguishing characteristics that cause a loan to be considered a Grade 5 loan would be a major occurrence or condition, either actual or anticipated, the consequences of which are not yet evident, which would materially increase the level of risk in the credit. The loan warrants closer monitoring by the loan officer than does a Grade 4 credit. In addition, loans in this category require a more proactive stance on the part of the loan officer in order to improve the credit's weaknesses and thus prevent the level of credit risk from increasing to a point where a more severe risk rating is justified.

Special Mention (6): Assets included in this category are currently protected but are potentially weak. These assets constitute an undue and unwarranted credit risk but do not presently expose the bank to a sufficient degree of risk to justify adverse classification. Close management attention is required.

Substandard (7): Substandard assets are inadequately protected by the current net worth and financial capacity of the borrower or the collateral pledged. Assets so classified must have well-defined weaknesses or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the bank will sustain some loss if the deficiencies are not corrected. Loss potential, while existing in the aggregate amount of Substandard assets, does not have to exist in individual assets classified as Substandard. Loans in this category will generally require a loan loss reserve allocation which will be determined by the Chief Lending Officer in compliance with ASC Topic 310.

Doubtful (8): Doubtful assets have all the inherent weaknesses as those classified as Substandard, with the added characteristic that the weaknesses make collection in full, on the basis of currently existing facts, conditions and values highly questionable and improbable. Probability of loss is extremely high, but because of certain important and reasonably specific pending factors which may work to strengthen (or weaken) the asset, its classification as an estimated loss is deferred until its more exact status may be determined. Pending factors that may necessitate a Doubtful classification include proposed merger, acquisition or liquidation procedures, capital injection, perfecting liens on additional collateral and refinancing plans. Loans in this category will generally require a loan loss reserve factor which will be determined by the Chief Lending Officer in compliance with SFAS 114.

Age Analysis of Past Due Loans

Delinquent loans were as follows at December 31, 2013:

	30 – 89 Days Past Due	Over 90 Days Past Due	Total Past Due	Current	Total Financing Receivables
Real estate-construction:					
1-4 family residential	$ -	$ -	$ -	$ 713,193	$ 713,193
Other construction, land development and land loans	-	-	-	394,006	394,006
Real estate-residential:					
Revolving lines of credit	-	-	-	1,042,350	1,042,350
1-4 family residential	-	-	-	8,517,300	8,517,300
Real estate-commercial					
Multifamily	-	-	-	2,156,219	2,156,219
Nonfarm nonresidential	-	54,000	54,000	45,353,571	45,407,571
Commercial and industrial	1,782	-	1,782	13,582,337	13,584,119
Consumer	-	-	-	274,903	274,903
Total	$ 1,782	$ 54,000	$ 55,782	$ 72,033,879	$ 72,089,661

Delinquent loans were as follows at December 31, 2012:

	30 – 89 Days Past Due	Over 90 Days Past Due	Total Past Due	Current	Total Financing Receivables
Real estate-construction:					
1-4 family residential	$ -	$ -	$ -	$ 1,010,466	$ 1,010,466
Other construction, land development and land loans	-	-	-	-	-
Real estate-residential:					
Revolving lines of credit	-	-	-	808,864	808,864
1-4 family residential	36,518	294,750	331,268	3,530,661	3,861,929
Real estate-commercial					
Multifamily	-	-	-	1,981,276	1,981,276
Nonfarm nonresidential	-	-	-	40,153,202	40,153,202
Commercial and industrial	55,625	-	55,625	10,619,039	10,674,664
Consumer	-	-	-	273,009	273,009
Total	$ 92,143	$ 294,750	$ 386,893	$ 58,376,517	$ 58,763,410

Impaired Loans

Impaired loans were as follows at December 31, 2013:

	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment for 2013 Net of Allowance	Interest Income Recognized in 2013
With an allowance recorded:					
Real estate-commercial					
Nonfarm nonresidential	$ 1,316,088	$ 1,391,312	$ 75,224	$ 1,354,690	$ 98,971
Total	$ 1,316,088	$ 1,391,312	$ 75,224	$ 1,447,853	$ 98,971

Impaired loans were as follows at December 31, 2012:

	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment for 2012 Net of Allowance	Interest Income Recognized in 2012
With an allowance recorded:					
Real estate-residential					
1-4 family residential	$ 294,750	$ 336,568	$ -	$ 305,205	$ -
Real estate-commercial					
Nonfarm nonresidential	1,292,055	1,369,065	77,010	1,385,493	115,276
Total	$ 1,586,805	$ 1,705,633	$ 77,010	$ 1,690,698	$ 115,276

Loans are considered impaired when, based on current information and events, it is probable the Company will be unable to collect all amounts due in accordance with the original contractual terms of the loan agreement, including scheduled principal and interest payments. Impairment is evaluated on an individual loans basis for all loans. If a loan is impaired, a specific valuation allowance is allocated, if necessary, so that the loan is reported net, at the present value of expected future cash flows using the loans existing rate or at the fair value of collateral if repayment is expected solely from the collateral. Interest payments on impaired loans are typically applied to principal unless collectability of the principal amount is reasonably assured, in which case interest is recognized on a cash basis. Impaired loans, or portions

thereof, are charged off when deemed uncollectible. Recorded Investment is the Unpaid Principal balance less Related Allowance and any related charge-offs (if applicable).

Nonaccrual Loans

Nonaccrual loans were as follows at December 31, 2013 and 2012, respectively:

	2013	2012
Real estate-residential – 1-4 family residential	$ 54,000	$ 294,750

Loans on which interest and/or principal is 90 days or more past due are placed on nonaccrual status and any previously accrued but uncollected interest is reversed against income (current year) or charged to the allowance for credit losses (prior year). Such loans will remain on a cash basis for the recognition of income until such time as the loan has remained current for a period of not less than six months and it is determined an adequate propensity for timely payment to occur in the future. Past due is measured from the date through which interest is due or on which principal payment is due irrespective of the date on which the billing may have been rendered. Unless otherwise specified in the note or loan agreement, demand notes shall, for the purpose of measuring past due status, have an interest due date no less frequently than once each calendar quarter.

There were no troubled debt restructurings as of December 31, 2013 and 2012, or during the year, respectively.

NOTE 5 – DEPOSITS

The following is a summary of the distribution of deposits as of December 31, 2013 and 2012:

	2013	2012
Noninterest bearing deposits	$ 15,322,270	$ 12,022,846
NOW Accounts	1,679,528	1,017,238
Savings and money market accounts	25,920,255	25,351,435
Certificates of deposit less than $100,000	10,222,927	9,428,945
Certificates of deposit greater than $100,000	25,787,698	22,053,131
Total	$ 78,932,678	$ 69,873,595

At December 31, 2013, the scheduled maturities of time deposits are as follows:

	Less than $100,000	Greater than $100,000	Total
2014	$ 5,648,841	$ 18,132,040	$ 23,780,881
2015	860,968	4,798,977	5,659,945
2016	3,672,248	2,749,994	6,422,242
2017	40,870	106,687	147,557
2018	-	-	-
Total	$ 10,222,927	$ 25,787,698	$ 36,010,625

NOTE 6 – OFF-BALANCE SHEET ARRANGEMENTS

Credit-Related Financial Instruments – The Bank is a party to credit-related financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit, standby letters of credit, and undisbursed lines of credit. Such commitments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the consolidated balance sheet.

The Bank's exposure to credit loss is represented by the contractual amount of these commitments. The Bank follows the same credit policies in making commitments as it does for on-balance-sheet instruments.

The contractual amounts of commitments to extend credit, standby letters of credit, and undisbursed lines of credit as of December 31, 2013 and 2012, respectively are shown below:

	December 31, 2013	December 31, 2012
Commitments to extend credit	$ 2,167,500	$ 3,890,750
Standby letters of credit	141,213	153,481
Undisbursed lines of credit	6,840,501	6,381,229
Total	$ 9,149,214	$ 10,425,460

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require repayment of a fee. The commitments for equity lines of credit may expire without being drawn upon. Therefore, the total commitment amounts do not necessarily

represent future cash requirements. The amount of collateral obtained, if it is deemed necessary by the Company, is based on management's credit evaluation of the customer.

Undisbursed lines of credit under commercial lines of credit, revolving credit lines, and overdraft protection agreements are commitments for possible future extensions of credit to existing customers. These lines of credit can be collateralized and may not be drawn upon to the total extent to which the Company is committed.

Standby letters of credit are conditional commitments issued by the Company to guarantee the performance of a customer to a third party. Those letters of credit are used primarily to support public and private borrowing arrangements. Essentially all letters of credit issued have expiration dates within one year. The credit risk involved is extending loan facilities to those customers. The Company generally holds collateral supporting those commitments if deemed necessary.

Collateral Requirements – To reduce credit risk related to the use of credit-related financial instruments, the Company might deem it necessary to obtain collateral. The amount and nature of the collateral obtained are based on the Company's evaluation of the customer. Collateral held varies but may include cash, securities, accounts receivable, inventory, property, plant, and equipment, and real estate.

If the counterparty does not have the right and the ability to redeem the collateral or the Company is permitted to sell or repledge the collateral on short notice, the Company records the collateral on its consolidated balance sheet at fair value with a corresponding obligation to return it.

Legal Contingencies – The Company is a defendant in a lawsuit that was filed during the year. The litigation is currently in the discovery phase and the Company plans on vigorously contesting the lawsuit. An estimate of the potential loss, if any, is unknown at this time.

NOTE 7 – PROPERTY AND EQUIPMENT

Property and equipment consist of the following:

	December 31, 2013	December 31, 2012
Building and Improvements	$ 2,225,802	$ 2,223,081
Land	854,233	854,233
Office Equipment	1,045,891	859,629
Leasehold Improvements	105,914	-
	4,231,840	3,936,943
Less: Accumulated depreciation	1,166,011	961,138
Property and equipment net of depreciation	$ 3,065,829	$ 2,975,805

NOTE 8 – INCOME TAXES

The components of the Company's provision for income taxes for the years ended December 31, 2013 and 2012 are as follows:

	December 31	
	2013	2012
Income tax expense at statutory rate of 34%	$ 333,770	$ 391,578
Change in valuation allowance	-	(1,386,446)
Effect of nondeductible expenses and other – net	2,302	13,728
Net income tax expense (benefit)	$ 336,072	$ (981,140)

Components of the Company's deferred tax assets at December 31 are summarized as follows:

Deferred tax asset:	2013	2012
Assets:		
Bad debt reserve	$ 422,814	$ 400,923
Nonaccrual loan interest	962	-
Stock warrant expense	187,833	187,833
Organizational costs	166,198	186,638
Net operating loss	-	205,363
Fixed assets	27,761	31,037
Net unrealized loss on securities available for sale	67,131	-
Contribution carryover	-	6,883
Total assets	872,699	1,018,677
Liabilities:		
Deferred loan costs/fees	(66,161)	(37,537)
Total liabilities	(66,161)	(37,537)
Valuation allowance	-	-

Net deferred tax asset	$ 806,538	$ 981,140

The allocation of income taxes between current and deferred is as follows:

	2013	2012
Current income tax expense	$ 94,339	$ -
Deferred income tax expense	241,733	405,306
Valuation allowance	-	(1,386,446)
Total income tax (benefit)	$ 336,072	$ (981,140)

The Company's deferred tax asset ("DTA") is included in other assets on the balance sheet. A valuation reserve is required when it is more likely than not that a portion of all of the benefit related to the asset will not be realized. Since inception, the Company had provided a valuation reserve for the full amount of the DTA balance due to cumulative losses, but this was reversed in 2012. The Company believes there is sufficient evidence that it will be able to recognize the benefits of the DTA based on improved earnings, positive performance trends and future projections demonstrating sustainable profitability. As a result, no valuation reserve is required as of December 31, 2013.

NOTE 9 – STOCK-BASED COMPENSATION

Options - At the Company's Annual Meeting of Shareholders held May 21, 2008, its shareholders approved the 2008 Stock Incentive Plan, which had previously been approved by the Board of Directors. Under the Company's stock-based incentive plan, the Company may grant stock options to its directors, officers and employees for up to 166,795 shares of common stock. Effective January 1, 2007, the Company adopted the fair value recognition provisions of ASC 718-20, *Share Based Payments*. ASC 718-20 established a fair value method of accounting for stock options whereby compensation expense is recognized based on the computed fair value of the options on the grant date. At December 31, 2013, stock options outstanding had a weighted average remaining contractual life of 6.5 years. The following table summarizes stock options outstanding and aggregate intrinsic value as of December 31, 2013:

		Weighted Average		
Exercise Price	Number Outstanding	Remaining Contractual Life	Exercise Price	Aggregate Intrinsic Value
$ 10.00	38,224	6.5 yrs	$ 10.00	-

The Company granted 59,024 incentive options to purchase common stock to certain officers of the Company during 2008. The fair value of the stock options granted during 2008 was $3.66 per share. No options were granted in 2013or 2012. The Company uses historical data to estimate option expense and employee termination within the valuation model. The risk-free rate for periods within the contractual life of the option is based on the U.S. Treasury yield curve in effect at the time of grant. During 2013 and 2012, no options were cancelled.

The stock options have an exercise price of $10.00 per share. The options vest ratably over a three-year term. All of the options expire 10 years following the date of grant.

As of December 31, 2013, there was $20,675 of total unrecognized pre-tax compensation expense related to nonvested stock options outstanding. The weighted average term over which this expense will be recognized is .9 years. Common shares issued upon exercise of stock options result in new shares issued by the Company from authorized but unissued shares.

Warrants- In conjunction with its initial public offering, the Company has issued a total of 277,993 warrants to initial shareholders in the ratio of one warrant to every five shares purchased in the offering. These warrants had a strike price of $12.50 per share and expired at noon on February 26, 2010. Additionally, the Company has issued 142,500 warrants to its organizers. These warrants have a strike price of $10.00 per share and expire February 26, 2017. A total of 142,500 warrants to purchase the Company's common stock were issued and outstanding as of December 31, 2013 and 2012.

Restricted Stock Awards – On January 1, 2013, 10,113 restricted shares were awarded to certain key executives in accordance with the Lotus Bancorp, Inc. 2013 Stock Compensation Plan. As of December 31, 2013, zero shares were vested. The remaining shares will vest as follows:

Date	Shares Vesting
January 1, 2014	3,372
January 1, 2015	3,372
January 1, 2016	3,369

A summary of the Company's nonvested restricted stock awards as of December 31, 2013 and changes during the year then ended is as follows:

Restricted Stock Awards	2013
Nonvested at December 31, 2012	0
Granted	10,113
Vested	-

Forfeited	-
Nonvested at December 31, 2013	10,113

There was $29,606 of expense recorded for the restricted stock awards in 2013. The amount of unrecognized compensation costs related to the nonvested restricted stock awards under the plan was $59,194 as of December 31, 2013.

NOTE 10– BORROWINGS

In 2008, the Bank entered into a discount window loan agreement with the Federal Reserve Bank of Chicago. The borrower-in-custody arrangement allows for secured advances based on the pledging of assets such as loans, investment securities and other assets. The interest rate on the advances is based on the quoted federal reserve discount window rates (effective rate of 0.75 percent as of December 31, 2013). At December 31, 2013 and 2012, the Bank had $0 outstanding in the advances.

The Bank had available credit lines with Comerica Bank and Great Lakes Bankers Bank as of December 31, 2013. The lines allow for advances of up to $3,000,000 and are unsecured. At December 31, 2013 and 2012, the Bank had $0 outstanding on the lines.

The Bank has advances from the Federal Home Loan Bank of Indianapolis. Interest rates range from 0.77% to 1.86%. At December 31, 2013, the weighted average interest rate on fixed-rate borrowings was 1.63%. Interest is payable monthly. These advances contain varying maturity dates through September 5, 2017, with an average maturity of 42 months. The advances are collateralized by pooled mortgage-related assets of the Bank with a fair value of $9,355,000 as of December 31, 2013, under a blanket collateral arrangement. The outstanding balance of advances was $1,900,000 and $0 as of December 31, 2013 and 2012, respectively.

Future maturities of borrowings are as follows as of December 31, 2013:

2014	$ -
2015	-
2016	400,000
2017	1,500,000
Total	$ 1,900,000

NOTE 11 – MINIMUM REGULATORY CAPITAL REQUIREMENTS

Banks are subject to regulatory capital requirements administered by federal banking authorities. Capital adequacy guidelines and prompt corrective action regulations involve quantitative measures of assets, liabilities and certain off-balance-sheet items calculated under regulatory accounting policies. Capital amounts and classifications are also subject to qualitative judgments by regulators. Failure to meet capital requirements can initiate regulatory action. The prompt corrective action regulations provide four classifications: well capitalized, adequately capitalized, undercapitalized and critically undercapitalized, although these terms are not used to represent overall financial condition. If adequately capitalized, regulatory approval is required to accept brokered deposits. If undercapitalized, capital distributions are limited, as is asset growth and expansion, and plans for capital restoration are required. The Bank was well capitalized as of December 31, 2013 and 2012.

The Bank's actual capital amounts and ratios as of December 31, 2013 and 2012 are represented in the following table (dollars in thousands):

	Actual		For Capital Adequacy Purposes		To Be Well Capitalized	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2013:						
Total Risk Based Capital To Risk Weighted Assets						
Lotus Bank	$ 11,983	15.37%	$ 6,237	8.00%	$ 7,796	10.00%
Tier One Capital to Risk Weighted Assets						
Lotus Bank	$ 11,008	14.12%	$ 3,118	4.00%	$ 4,678	6.00%
Tier One Capital to Total Average Assets						
Lotus Bank	$ 11,008	12.20%	$ 3,609	4.00%	$ 4,511	5.00%

As of December 31, 2012:						
Total Risk Based Capital To Risk Weighted Assets						
Lotus Bank	$ 11,439	17.21%	$ 5,319	8.00%	$ 6,648	10.00%
Tier One Capital to Risk Weighted Assets						
Lotus Bank	$ 10,689	16.08%	$ 2,659	4.00%	$ 3,989	6.00%
Tier One Capital to Total Average Assets						
Lotus Bank	$ 10,689	13.45%	$ 3,178	4.00%	$ 3,972	5.00%

NOTE 12 – RESTRICTIONS ON DIVIDENDS, LOANS AND ADVANCES

Banking regulations place certain restrictions on dividends paid and loans or advances made by the Bank to the Company.

Prior approval of the Bank's federal regulator is required if the total dividends declared by the Bank in a calendar year exceed the sum of the net profits of the Bank for the preceding three years, less any required transfers to surplus. In addition, dividends paid by the Bank would be prohibited if the effect thereof would cause the Bank's capital to be reduced below applicable minimum standards. Because of the Bank's de novo status and its startup losses, at December 31, 2013, the Bank's retained earnings available for the payment of dividends, without approval from regulators, was $0. Accordingly, all of the Company's investment in the Bank was restricted at December 31, 2013.

Loans or advances made by the Bank to the Company are generally limited to 10 percent of the Bank's capital and surplus. The Federal Reserve Bank of Chicago, which is the Company's regulator, however, has restricted borrowings by the Company during its first seven years of operation without its prior approval.

NOTE 13 – FAIR VALUE OF FINANCIAL INSTRUMENTS

The fair value of a financial instrument is the current amount that would be exchanged between willing parties, other than in a forced liquidation. Fair value is best determined based upon quoted market prices. However, in many instances, there are no quoted market prices for the Company's various financial instruments. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. Accordingly, the fair value estimates may not be realized in an immediate settlement of the instrument. ASC Topic 825 excludes certain financial instruments and all nonfinancial instruments from its disclosure requirements. Accordingly, the aggregate fair value amounts presented may not necessarily represent the underlying fair value of the Company.

The following methods and assumptions were used by the Company in estimating fair value disclosures for financial instruments:

Cash and Cash Equivalents – the carrying amounts of cash and cash equivalents approximate fair value.

Loans Receivable – for variable rate loans that reprice frequently and with no significant change in credit risk, fair values are based on carrying values. Fair values for other loans are estimated using discounted cash flow analyses, using interest rates currently being offered for loans with similar terms to borrowers of similar credit quality. Fair values of nonperforming loans are estimated using discounted cash flow analyses or underlying collateral values, where applicable.

Securities – the fair values of securities are based on quoted market prices. If a quoted market price is not available, fair value is estimated using quoted market prices for similar securities.

Deposit Liabilities – the fair values disclosed for demand deposits are, by definition, equal to the amount payable on demand at the reporting date (i.e., their carrying amounts). The carrying amounts also approximate the fair value for money market deposit, other savings, and variable rate certificate of deposit accounts. Fair values for fixed rate certificates of deposit are estimated using a discounted cash flow calculation that applies interest rates currently being offered on certificates of deposit to a schedule of aggregated expected monthly maturities on time deposits.

FHLB Advances – Fair values for Federal Home Loan Bank Advance borrowings are based on rates currently in effect for borrowings with similar terms, rates and maturities.

Accrued Interest – the carrying amounts of accrued interest approximate fair value.

Other Financial Instruments – the fair value of other financial instruments, including loan commitments, unfunded lines of credit and unfunded standby letters of credit, based on discounted cash flow analyses, is not material.

The carrying and fair values of the Company's assets and liabilities as of December 31, 2013 and 2012 respectively are as follows:

	2013		2012	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Cash and due from banks	$ 980,256	$ 980,256	$ 1,274,534	$ 1,274,534
Federal funds sold	8,213,143	8,213,143	10,385,116	10,385,116
Investment securities	9,816,006	9,816,006	9,249,903	9,249,903
Loans – net	70,759,513	72,217,920	57,348,935	58,119,287
Accrued interest receivable	273,502	273,502	231,998	231,998
Noninterest bearing deposits	15,322,270	15,322,270	12,022,846	12,022,846
Interest bearing deposits	27,599,783	27,599,783	26,368,673	26,368,673
Time deposits	36,010,625	36,526,952	31,482,076	31,812,864
FHLB Advances	1,900,000	1,941,135	-	-
Accrued interest payable	114,437	114,437	108,116	108,116

NOTE 14 – EMPLOYEE BENEFIT PLAN

On January 1, 2009, the Bank adopted a 401(k) Plan (the "Plan") for the benefit of substantially all of its employees. Under the Plan, employees may elect to defer, up to the maximum allowed by IRS regulations, pre-tax income through contributions to the Plan. In order to maintain "safe harbor" status, the Bank may contribute 3.0% of eligible employees' compensation into the Plan. The contributions to the Plan were $35,120 and $29,792 for 2013 and 2012, respectively. Participant contributions and employer safe harbor contributions are fully vested immediately. The Plan also has discretionary profit-sharing and matching provisions. The Bank made no contributions under either of these provisions in 2013 or 2012. Contributions made under the discretionary provisions become fully vested after six years.

NOTE 15 – FAIR VALUE MEASUREMENTS

Accounting standards require that certain assets and liabilities be reported at fair value in the financial statements and provide a framework for establishing that fair value. The framework for determining fair value is based on a hierarchy that prioritizes the inputs and valuation techniques used to measure fair value.

The following tables present information about the Company's assets measured at fair value on a recurring basis on December 31, 2013 and 2012 and the valuation techniques used by the Company to determine those values.

Level 1 – In general, fair values determined by Level 1 inputs use quoted prices in active markets for identical assets that the Company has the ability to access.

Level 2 – Fair values determined by Level 2 inputs use other inputs that are observable, either directly or indirectly. These Level 2 inputs include quoted prices for similar assets in active markets, and other inputs such as interest rates and yield curves that are observable at commonly quoted intervals.

Level 3 – Level 3 inputs are unobservable inputs, including inputs that are available in situations where there is little, if any, market activity for the related asset. These Level 3 fair value measurements are based primarily on management's own estimates using pricing models, discounted cash flow methodologies, or similar techniques taking into account the characteristics of the asset.
In instances where inputs used to measure fair value fall into different levels in the above fair value hierarchy, fair value measurements in their entirety are categorized based on the lowest level input that is significant to the valuation. The Company's assessment of the significance of particular inputs to these fair value measurements requires judgment and considers factors specific to each asset.

Assets Measured at Fair Value on a Recurring Basis at December 31, 2013

	Quoted Prices in Active Markets For Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance at December 31, 2013
U.S. government and federal agency	$ 3,391,660	$ -	$ -	$ 3,391,660
Corporate	676,726	-	-	676,726
Municipal	-	5,747,620	-	5,747,620
Total	$ 4,068,386	$ 5,747,620	$ -	$ 9,816,006

Assets Measured at Fair Value on a Recurring Basis at December 31, 2012

	Quoted Prices in Active Markets For Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance at December 31, 2012
U.S. government and federal agency	$ 2,548,034	$ -	$ -	$ 2,548,034
Corporate	614,497	-	-	614,497
Municipal	-	6,087,372	-	6,087,372
Total	$ 3,162,531	$ 6,087,372	$ -	$ 9,249,903

The Company also has assets that under certain conditions are subject to measurement at fair value on a nonrecurring basis. These assets include impaired loans. The fair value of these loans was $1,391,312 and $1,663,815 as of December 31, 2013 and 2012, respectively. The Company has estimated the fair values of these assets primarily on Level 3 inputs. Impaired loans are generally valued using the fair value of collateral provided by third party appraisals. These valuations include assumptions related to cash flow projections, discount rates, and recent comparable sales. The numerical ranges of unobservable inputs for these valuation assumptions are not meaningful.

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