UNITED STATES
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**
For the fiscal year ended December 31, 2020
or

☐ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the transition period from to

Commission file number: 001-33037

SOUTHERN NATIONAL BANCORP OF VIRGINIA, INC.
(Exact name of registrant as specified in its charter)

Virginia **(State or other jurisdiction of incorporation or organization)**	**20-1417448** **(I.R.S. Employer Identification No.)**

6830 Old Dominion Drive
McLean, Virginia 22101
(Address of principal executive offices) (Zip code)

(703) 893-7400
(Registrant's telephone number including area code)

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

Title of each class	Trading symbol	Name of each exchange on which registered
Common Stock, $0.01 par value	SONA	Nasdaq Global Market

Securities registered pursuant to Section 12(g) of the Act: None

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

Indicate by check mark if 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 whether the registrant has submitted electronically, every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes ☒ No ☐

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

Large accelerated filer ☐ Accelerated filer ☒ Smaller reporting company ☐ Emerging growth company ☐

Non-accelerated filer ☐

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐

Indicate by check mark whether the registrant has filed a report on and attestation to its management's assessment of the effectiveness of internal control over financial reporting under Section 404(b) of the Sarbanes-Oxley Act (15 U.S.C. 7262(b)) by the registered public accounting firm that prepared or issues its audit report. ☒ Yes ☐ No

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

The aggregate market value of voting stock held by non-affiliates of the registrant as of June 30, 2020 was approximately $230.8 million based on the closing price of the common stock on such date.

The number of shares of common stock outstanding as of March 5, 2021 was 24,438,545.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's definitive proxy statement pursuant to Regulation 14A of the Securities Exchange Act of 1934 in conjunction with the registrant's 2021 Annual Meeting of Shareholders are incorporated by reference into Part III, Items 10-14 of this Annual Report on Form 10-K.

SOUTHERN NATIONAL BANCORP OF VIRGINIA, INC.
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CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Annual Report on Form 10-K contains statements about future expectations, activities and events that constitute forward-looking statements within the meaning of, and subject to the protection of, Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Exchange Act and are intended to be covered by the safe harbor provided by the same. Forward-looking statements are not historical facts and are based on current expectations, estimates and projections about our industry, management's beliefs and certain assumptions made by management, many of which, by their nature, are inherently uncertain and beyond our control, particularly with regard to developments related to the novel coronavirus ("COVID-19"). Accordingly, we caution you that any such forward-looking statements are not guarantees of future performance and are subject to risks, assumptions and uncertainties that are difficult to predict. Although we believe that the expectations reflected in these forward-looking statements are reasonable as of the date made, actual results may prove to be materially different from the results expressed or implied by the forward-looking statements. The words "believe," "may," "forecast," "should," "anticipate," "estimate," "expect," "intend," "continue," "would," "could," "hope," "might," "assume," "objective," "seek," "plan," "strive" or similar words, or the negatives of these words, identify forward-looking statements.

Forward-looking statements involve risks and uncertainties that may cause our actual results to differ materially from the expectations of future results we express or imply in any forward-looking statements. In addition to the other factors discussed in the "Risk Factors" section of this Annual Report on Form 10-K, factors that could contribute to those differences include, but are not limited to:

- the effects of future economic, business and market conditions and disruptions in the credit and financial markets, domestic and foreign;
- the impact of COVID-19 on our business, including the impact of the actions taken by governmental authorities to contain the virus or address the impact of the virus on the United States economy (including, without limitation, the Coronavirus Aid, Relief and Economic Security ("CARES" Act)), and the resulting effect of all of such items on our operations, liquidity and capital position, and on the financial condition of our borrowers and other customers;
- adverse results from current or future litigation, regulatory examinations or other legal and/or regulatory actions, including as a result of our participation in and execution of government programs related to the COVID-19 pandemic;
- changes in the local economies in our market areas which adversely affect our customers and their ability to transact profitable business with us, including the ability of our borrowers to repay their loans according to their terms or a change in the value of the related collateral;
- changes in the availability of funds resulting in increased costs or reduced liquidity, as well as the adequacy of our cash flow from operations and borrowings to meet our short-term liquidity needs;
- a deterioration or downgrade in the credit quality and credit agency ratings of the investment securities in our investment securities portfolio;
- impairment concerns and risks related to our investment securities portfolio of collateralized mortgage obligations, agency mortgage-backed securities, obligations of states and political subdivisions and pooled trust preferred securities;
- the incurrence and possible impairment of goodwill associated with current or future acquisitions and possible adverse short-term effects on our results of operations;
- increased credit risk in our assets and increased operating risk caused by a material change in commercial, consumer and/or real estate loans as a percentage of our total loan portfolio, including as a result of the financial impact of COVID-19;
- the concentration of our loan portfolio in loans collateralized by real estate;
- our level of construction and land development and commercial real estate loans;
- failure to prevent a breach to our Internet-based system and online commerce security, including as a result of increased remote working by our employees;
- changes in the levels of loan prepayments and the resulting effects on the value of our loan portfolio;
- the failure of assumptions and estimates underlying the establishment of and provisions made to the allowance for credit losses;

- our ability to expand and grow our business and operations, including the establishment of additional branches and acquisition of additional branches and banks, and our ability to realize the cost savings and revenue enhancements we expect from such activities;
- government intervention in the U.S. financial system, including the effects of legislative, tax, accounting and regulatory actions and reforms, including the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act"), the Jumpstart Our Business Startups Act, the Consumer Financial Protection Bureau, the capital ratios of Basel III as adopted by the federal banking authorities, and the Tax Cuts and Jobs Act of 2017 and the CARES Act;
- uncertainty related to the transition away from or new methods of calculating the London Inter-bank Offered Rate ("LIBOR");
- increased competition for deposits and loans adversely affecting rates and terms;
- the continued service of key management personnel;
- the potential payment of interest on demand deposit accounts to effectively compete for customers;
- potential environmental liability risk associated with properties that we assume upon foreclosure;
- increased asset levels and changes in the composition of assets and the resulting impact on our capital levels and regulatory capital ratios;
- risks of current or future mergers and acquisitions, including the related time and cost of implementing transactions and the potential failure to achieve expected gains, revenue growth or expense savings;
- increases in regulatory capital requirements for banking organizations generally, which may adversely affect our ability to expand our business or could cause us to shrink our business;
- acts of God or of war or other conflicts, acts of terrorism, pandemics or other catastrophic events that may affect general economic conditions;
- changes in accounting policies, rules and practices and applications or determinations made thereunder, including the impact of the adoption of the current expected credit losses ("CECL") methodology;
- fraudulent and negligent acts by loan applicants, mortgage brokers and our employees;
- failure to maintain effective internal controls and procedures;
- the risk that our deferred tax assets could be reduced if future taxable income is less than currently estimated, if corporate tax rates in the future are less than current rates, or if sales of our capital stock trigger limitations on the amount of net operating loss carryforwards that we may utilize for income tax purposes;
- our ability to attract and retain qualified employees; and
- other factors and risks described under "Risk Factors" herein and in any of our subsequent reports that we file with the Securities and Exchange Commission (the "Commission" or "SEC") under the Exchange Act.

Forward-looking statements are not guarantees of performance or results and should not be relied upon as representing management's views as of any subsequent date. A forward-looking statement may include a statement of the assumptions or bases underlying the forward-looking statement. We believe we have chosen these assumptions or bases in good faith and that they are reasonable. We caution you, however, that assumptions or bases almost always vary from actual results, and the differences between assumptions or bases and actual results can be material. When considering forward-looking statements, you should refer to the risk factors and other cautionary statements in this Annual Report on Form 10-K and in our periodic and current reports filed with the SEC for specific factors that could cause our actual results to be different from those expressed or implied by our forward-looking statements. These statements speak only as of the date of this Annual Report on Form 10-K (or an earlier date to the extent applicable). Except as required by applicable law, we undertake no obligation to update publicly these statements in light of new information or future events.

PART I

Item 1. Business

Overview

Southern National Bancorp of Virginia, Inc. ("Southern National", "SNBV", "we" or "our") is the bank holding company for Sonabank ("Sonabank" or the "Bank"), a Virginia state-chartered bank. Sonabank provides a range of financial services to individuals and small and medium sized businesses. As of December 31, 2020, Southern National had $2.44 billion in total loans, $3.09 billion in total assets, $2.43 billion in total deposits and $390.6 million in total stockholders' equity. At December 31, 2020, Sonabank had forty-two full-service branches in Virginia and Maryland and also provides services to customers through certain internet and mobile applications. Thirty-seven full-service retail branches are in Virginia (Ashland, Burgess, Callao, Central Garage, Charlottesville, Chester, Clifton Forge, Colonial Heights, Courtland, Deltaville, Fairfax, Front Royal, Gloucester, Gloucester Point, Hampton, Hartfield, Heathsville, Kilmarnock, Leesburg, McLean, Mechanicsville (2), Middleburg, Midlothian, New Market, Newport News, Quinton, Reston, Richmond, South Riding, Surry, Tappahannock (2), Urbanna, Warrenton, Waverly, and Williamsburg) and five full-service retail branches are in Maryland (Bethesda, Brandywine, Owings, Rockville, and Upper Marlboro). We have administrative offices in Warrenton and Glen Allen, Virginia. Our South Riding branch will be closing effective April 15, 2021.

As part of the Company's rebranding initiatives, on January 28, 2021, Southern National announced that it is changing its name to Primis Financial Corp. and the Bank is changing its name to Primis Bank effective March 31, 2021.

While we offer a wide range of commercial banking services, we focus on making loans secured primarily by commercial real estate and other types of secured and unsecured commercial loans to small and medium-sized businesses in a number of industries, as well as loans to individuals for a variety of purposes, including 1-4 family residential loans. We are a leading Small Business Administration ("SBA") lender among Virginia community banks. We also invest in real estate-related securities, including collateralized mortgage obligations and agency mortgage backed securities. Our principal sources of funds for loans and investing in securities are deposits and, to a lesser extent, borrowings. We offer a broad range of deposit products, including checking, NOW, savings, and money market accounts and certificates of deposit. We actively pursue business relationships by utilizing the business contacts of our senior management, other bank officers and our directors, thereby capitalizing on our knowledge of our local market areas.

The Bank owns 48.9% of Southern Trust Mortgage, LLC ("STM"), a regional mortgage banking company headquartered in Virginia Beach, Virginia. As of December 31, 2020, our equity investment in STM totaled $12.7 million and our preferred stock investment in STM totaled $3.3 million. STM has mortgage banking originators in Delaware, Virginia, Maryland, North Carolina and South Carolina. STM only originates retail mortgages.

On August 25, 2020, Southern National completed the sale of $60.0 million of its fixed-to-floating rate Subordinated Notes due 2030 (the "SNBV Subordinated Notes"). The SNBV Subordinated Notes will bear interest at an initial rate of 5.40% per annum, payable semi-annually in arrears on March 1 and September 1 of each year, commencing on March 1, 2021. From and including September 1, 2025 to, but excluding the maturity date or the date of earlier redemption (the "floating rate period"), the interest rate will reset quarterly to an annual interest rate equal to the Benchmark Rate, which is expected to be three-month Term SOFR, plus 531 basis points for each quarterly interest period during the floating rate period and payable quarterly in arrears on March 1, June 1, September 1, and December 1 of each year, commencing on December 1, 2025. Notwithstanding the foregoing, in the event that the Benchmark Rate is less than zero, the Benchmark Rate shall be deemed to be zero.

On November 1, 2020, the Company launched the Panacea Financial division, which will focus on national lending, deposit gathering, wealth, and insurance needs with unique products and services for the medical community.

We primarily market our products and services to small and medium-sized businesses and to retail consumers. Our strategy is to provide superior service through our employees, who are relationship-oriented and committed to their

respective customers. Through this strategy, we intend to grow our business, expand our customer base and improve our profitability. The key elements of our strategy are to:

- *Utilize the Strength of our Management Team*. The experience and market knowledge of our management team is one of our greatest strengths and competitive advantages. The Company's board of directors appointed Mr. Dennis J. Zember, Jr. as the new president and chief executive officer, effective February 19, 2020. Mr. Zember, currently our chief executive officer, has more than 24 years of financial experience in the banking industry.
- *Rebranding Initiative and Proposed Name Change*: As part of the Company's rebranding initiatives, on January 28, 2021, the Board of Directors of the Company approved changing the Company's name to Primis Financial Corp., to be effective as of March 31, 2021. The Company's wholly-owned banking subsidiary, Sonabank, will also change its name to Primis Bank, effective March 31, 2021. Over the last year, the Company has focused on building the foundation for a Company with higher expectations around innovation and technology. We want to deliver a better return for our shareholders and a better experience for our customers. We are committed to train harder, develop more expertise in all areas and build relationships that will last. Changing our name and our brand, and committing to an image that mirrors this attitude is critical. Effective March 31, 2021, our ticker symbol will also change from SONA to FRST and our website will become *www.primisbank.com*.
- *Leverage Our Existing Foundation for Additional Growth.* Based on our management's depth of experience and certain infrastructure investments, we believe that we will be able to take advantage of certain economies of scale typically enjoyed by larger organizations to expand our operations both organically and through strategic cost-effective branch or bank acquisitions. We believe that the investments we have made in our data processing, risk management infrastructure, staff and branch network will be able to support a much larger asset base. We are committed, however, to control any additional growth in a manner designed to minimize risk and to maintain strong capital ratios.
- *Continue to Pursue Selective Acquisition Opportunities*. Historically, acquisitions have been a key part of our growth. We believe that we have demonstrated the skill sets and experience necessary to acquire and integrate successfully both bank and branch acquisitions, and that with our strong capital position, we are well-positioned to take advantage of acquisition opportunities as they may arise. We intend to focus on targets in our market areas or other attractive areas with significant core deposits and/or a potential customer base compatible with our growth strategy.
- *Focus on the Business Owner*. It is our goal to be the bank that business owners in our markets turn to first for commercial banking needs as a result of our superior personal service and the tailored products and services that we provide. To help achieve this goal, we:
    - have a standing credit committee that meets as often as necessary on a "when needed" basis to review completed loan applications, making extensive use of technology to facilitate our internal communications and thereby enabling us to respond to our customers promptly;
    - are an SBA approved "Preferred" lender, which permits us to make SBA loan decisions at Sonabank rather than waiting for SBA processing. We offer a number of different types of SBA loans designed for the small and medium-sized business owner and many of our SBA loan customers also have other relationships with Sonabank. This product group is complex and "paper intensive" and not well utilized by some of our competitors;
    - provide Internet business banking at *www.sonabank.com* which allows our business customers 24-hour web-based access to their accounts so they can confirm or transfer balances, pay bills, download statements and use our "Web Lockbox" or "Sona Cash Manager;"
    - provide our business customers with "Sona In-House," a service that utilizes Check 21 technology to allow customers to make remote deposits from their business locations and gives them access to those funds within 24 to 48 hours; and
    - provide our business customers with access to SABL, our state-of-the-art asset-based lending system. Unlike most asset-based lending systems, which are based on manual processes or software that certifies a company's borrowing base periodically, SABL provides a real time capability to analyze and adjust borrowing availability based on actual collateral levels. SABL is predicated on a link between any kind of accounting software used by the customer and Sonabank's server.
- *Maintain Local Decision-Making and Accountability*. We believe that we have a competitive advantage over larger national and regional financial institutions by providing superior customer service with experienced,

knowledgeable management, localized decision-making capabilities and prompt credit decisions. We believe that our customers want to deal directly with the people who make the credit decisions.

- *Focus on Asset Quality and Strong Underwriting*. We consider asset quality to be of primary importance and have taken measures in an effort to ensure that, despite the growth in our loan portfolio, we maintain strong asset quality through strong underwriting standards.
- *Build a Stable Core Deposit Base*. We intend to continue to grow a stable core deposit base of business and retail customers. To the extent that our asset growth outpaces this local deposit funding source, we plan to continue to borrow and raise deposits in the national market using deposit intermediaries. We intend to continue our practice of developing a deposit relationship with each of our loan customers.

General

Our principal business is the acquisition of deposits from the general public through our branch offices and deposit intermediaries and the use of these deposits to fund our loan and investment security portfolios. We seek to be a full service community bank that provides a wide variety of financial services to our middle market corporate clients as well as to our retail clients. We are an active commercial lender, have been designated as a “Preferred SBA Lender” and participate in the Virginia Small Business Financing Authority lending program. In addition, we are an active commercial real estate lender. We also invest funds in mortgage-backed securities, collateralized mortgage obligations, securities issued by agencies of the federal government, obligations of states and political subdivisions and pooled trust preferred securities.

The principal sources of funds for our lending and investment activities are deposits, repayment of loans, prepayments from mortgage-backed securities, repayments of maturing investment securities, Federal Home Loan Bank (“FHLB”) advances and other borrowed money.

Principal sources of revenue are interest and fees on loans and investment securities, equity earnings from STM, as well as fee income derived from the maintenance of deposit accounts and income from bank-owned life insurance policies. Our principal expenses include interest paid on deposits, advances from the FHLB of Atlanta, junior subordinated debt, senior subordinated notes and other borrowings, and operating expenses.

Available Information

Southern National files annual, quarterly, periodic and other reports under the Securities Exchange Act of 1934, as amended, with the SEC. These reports are posted and are available at no cost on our website, *www.sonabank.com*, through the Investor Relations link, as soon as reasonably practicable after we file such documents with the SEC. Our filings are also available through the SEC’s website at *www.sec.gov*.

Lending Activities

Our primary strategic objective is to serve small to medium-sized businesses in our market with a variety of unique and useful services, including a full array of commercial mortgage and non-mortgage loans. These loans include commercial real estate loans, construction and permanent loans, development and builder loans, accounts receivable financing, lines of credit, equipment and vehicle loans, leasing, and commercial overdraft protection. We strive to do business in the areas served by our branches, which is also where our marketing is focused, and the vast majority of our loan customers are located in existing market areas. Substantially all of our loans are with borrowers in Virginia, Maryland, West Virginia, and Washington, D.C. The SBA may from time to time come to us because of our reputation and expertise as an SBA lender and ask us to review a loan outside of our core counties but within our market area. Prior to making a loan, we obtain loan applications to determine a borrower’s ability to repay, and the more significant items on these applications are verified through the use of credit reports, financial statements and confirmations.

The following is a discussion of each of the major types of lending in which we engage. For more information on our lending activities, see “Item 7. Management’s Discussion and Analysis of Financial Condition.”

Commercial Real Estate Lending

Permanent. Commercial real estate lending includes loans for permanent financing. Commercial real estate lending typically involves higher loan principal amounts and the repayment of loans is dependent, in large part, on sufficient income from the properties securing the loans to cover operating expenses and debt service. As a general practice, we require our commercial real estate loans to be secured by well-managed income producing properties with adequate margins and to be guaranteed by responsible parties. We look for opportunities where cash flow from the collateral properties provides adequate debt service coverage and the guarantor's net worth is strong. At December 31, 2020, our commercial real estate loans for permanent financing, including multi-family residential loans and loans secured by farmland, totaled $1.15 billion, or 47.2% of our loan portfolio. Owner occupied commercial real estate loans totaled $435.0 million.

Our underwriting guidelines for commercial real estate loans reflect all relevant credit factors, including, among other things, the income generated from the underlying property to adequately service the debt, the availability of secondary sources of repayment and the overall creditworthiness of the borrower. In addition, we look to the value of the collateral, while maintaining the level of equity invested by the borrower.

All valuations on property which will secure loans over $250 thousand are performed by independent outside appraisers who are reviewed by our executive vice president of credit risk management and/or our appraisal reviewer. We retain a valid lien on real estate and obtain a title insurance policy (on first trust loans only) that insures the property is free of encumbrances. In addition, we do title searches on all loans secured by real estate.

Construction. We recognize that construction loans for commercial, multifamily and other non-residential properties can involve risk due to the length of time it may take to bring a finished real estate product to market. As a result, we will only make these types of loans when pre-leasing or pre-sales or other credit factors suggest that the borrower can carry the debt if the anticipated market and property cash flow projections change during the construction phase.

Income producing property loans are supported by evidence of the borrower's capacity to service the debt. All of our commercial construction loans are guaranteed by the principals or general partners. At December 31, 2020, we had $103.3 million of construction and land development loans outstanding.

Construction loan borrowers are generally pre-qualified for the permanent loan by us or a third party. We obtain a copy of the contract with the general contractor who must be acceptable to us. All plans, specifications and surveys must include proposed improvements. We review feasibility studies and risk analyses showing sensitivity of the project to variables such as interest rates, vacancy rates, lease rates and operating expenses.

Commercial Business Lending

These loans consist of lines of credit, revolving credit facilities, demand loans, term loans, equipment loans, SBA loans, stand-by letters of credit and unsecured loans. Commercial business loans are generally secured by accounts receivable, equipment, inventory and other collateral, such as readily marketable stocks and bonds with adequate margins, cash value in life insurance policies and savings and time deposits at Sonabank. At December 31, 2020, our commercial business loans totaled $187.1 million.

In general, commercial business loans involve more credit risk than residential mortgage loans and real estate-backed commercial loans and, therefore, usually yield a higher return to us. The increased risk for commercial business loans is due to the type of collateral securing these loans. The increased risk also derives from the expectation that commercial loans will be serviced principally from the operations of the business, which may not be successful. Historical trends have shown that these types of loans have higher delinquencies than mortgage loans. Because of this, we often utilize the SBA 7(a) program (which generally guarantees the repayment of up to 75% of the principal and accrued interest to us) to reduce the inherent risk associated with commercial business lending.

Another way that we reduce risk in the commercial loan portfolio is by taking accounts receivable as collateral using our SABL system. Our accounts receivable financing facilities, which provide a relatively high yield with considerable

collateral control, are lines of credit under which a company can borrow up to the amount of a borrowing base which covers a certain percentage of the company's receivables. From our customer's point of view, accounts receivable financing is an efficient way to finance expanding operations because borrowing capacity expands as sales increase. Customers can borrow from 75% to 90% of qualified receivables. In most cases, the borrower's customers pay us directly. For borrowers with a good track record for earnings and quality receivables, we will consider pricing based on an increment above the prime rate for transactions in which we lend up to a percentage of qualified outstanding receivables based on reported aging of the receivables portfolio.

We also actively pursue for our customers equipment lease financing opportunities. We provide financing and use a third party to service the leases. Payment is derived from the cash flow of the borrower, so credit quality may not be any lower than it would be in the case of an unsecured loan for a similar amount and term.

SBA Lending

We have developed an expertise in the federally guaranteed SBA program. The SBA program is an economic development program which finances the expansion of small businesses. We are a Preferred Lender in the Washington, D.C. and Richmond, Virginia Districts of the SBA. As an SBA Preferred Lender, our pre-approved status allows us to quickly respond to customers' needs. Under the SBA program, we generally originate and fund SBA 7(a) loans which qualify for guarantees up to 75% of principal and accrued interest (up to 90% in select instances). We also originate 504 chapter loans in which we generally provide 50% of the financing, taking a first lien on the real property as collateral.

We provide SBA loans to potential borrowers who are proposing a business venture, often with existing cash flow and a reasonable chance of success. We do not treat the SBA guarantee as a substitute for a borrower meeting our credit standards, and, except for minimum capital levels or maximum loan terms, the borrower must meet our other credit standards as applicable to loans outside the SBA process.

Residential Mortgage Lending

Permanent. Our business model generally does not include originating permanent residential mortgage loans. We originate such loans solely on a case-by-case basis. In the case of conventional loans, we typically lend up to 80% of the appraised value of single-family residences and require mortgage insurance for loans exceeding that amount. We have no sub-prime loans.

Sonabank has established with STM underwriting guidelines under which it will purchase residential construction only, construction loans that convert to permanent, and permanent loans primarily in its Virginia and Maryland footprint from STM. These are largely loans that do not conform to FNMA or FHLMC standards because of size or acreage. We purchased loans in an aggregate amount of $80.6 million from STM during 2020.

We retain a valid lien on real estate and obtain a title insurance policy that ensures that the property is free of encumbrances. We also require hazard insurance and flood insurance for all loans secured by real property if the real property is in a flood plain as designated by the Department of Housing and Urban Development. We also require most borrowers to advance funds on a monthly basis from which we make disbursements for items such as real estate taxes, private mortgage insurance and hazard insurance.

Home Equity Lines of Credit ("HELOC"). At December 31, 2020, we had outstanding HELOC balances totaling $91.6 million.

Consumer Lending

We offer various types of secured and unsecured consumer loans. We make consumer loans primarily for personal, family or household purposes as a convenience to our customer base since these loans are not the focus of our lending activities. As a general guideline, a consumer's debt service should not exceed 40% of gross income or 45% of net income. For purposes of this calculation, debt includes house payment or rent, fixed installment payments, the estimated

payment for the loan being requested and the minimum required payment on any revolving debt. At December 31, 2020, we had $22.3 million of consumer loans outstanding.

Credit Approval and Collection Policies

Because future loan losses are so closely intertwined with our underwriting policy, we have instituted what management believes is a stringent loan underwriting policy. Our underwriting guidelines are tailored for particular credit types, including lines of credit, revolving credit facilities, demand loans, term loans, equipment loans, real estate loans, SBA loans, stand-by letters of credit and unsecured loans. We will make extensions of credit based, among other factors, on the potential borrower's creditworthiness, likelihood of repayment and proximity to market areas served.

For loans less than $1.5 million, we have a standing Credit Committee comprised of certain officers, each of whom has a defined lending authority in combination with other officers. These individual lending authorities are determined by our Executive Chairman and Chief Risk Officer and are based on the individual's technical ability and experience. These lending authorities are approved by our board of directors. Our Credit Committee is comprised of three levels of members, based on experience: regular, senior, and executive. The executive members of our Credit Committee include two senior members – our Chief Credit Officer and our President and CEO and two junior members – our Chief SBA Lending Officer and our Head of Commercial Banking. Our Chief Credit Risk Officer, must approve risk ratings for loans over $1.5 million, as well as exceptions to the Credit Policy. Our Commercial Credit Team Lead must approve exceptions to Credit Policy for loans less than $1.5 million. Generally, group credits over $20 million must be approved by the Credit Committee and full Board of Directors or the Credit Committee plus two outside directors. Under our loan approval process, the sponsoring loan officer's approval is required on all credit submissions. This approval must be included in or added to the individual and joining authorities outlined below. The sponsoring loan officer is primarily responsible for the customer's relationship with us, including, among other things, obtaining and maintaining adequate credit file information. We require each loan officer to maintain loan files in an order and detail that would enable a disinterested third party to review the file and determine the current status and quality of the credit.

In addition to the approval of the sponsoring loan officer, we require approvals from one or more members of the Credit Committee on all loans. The approvals required differ based on the size of the borrowing relationship. At least one regular and one senior or executive member must approve loans up to $500 thousand. One regular, one senior and one executive member of the committee must approve all loans between $500 thousand and $1.0 million. One regular, one senior and two executive members must approve loans between $1.0 million and $1.5 million. Loans in the amount of $1.5 million to legal lending limit are approved by the Executive Credit Committee which meets every Thursday. Members of this committee include our President and CEO, Chief Credit Officer, Chief Credit Risk Officer, Chief SBA Lending Officer, Head of Commercial Banking (nonvoting), Director of Small Business and Consumer Lending and Commercial Credit Risk Officer. The Executive Credit Committee also approves risk ratings, and exceptions to credit policy. As of December 31, 2020, our legal lending limit was approximately $54.2 million.

The following collection actions are the minimal procedures which management believes are necessary to properly monitor past due loans and leases. When a borrower fails to make a payment, we contact the borrower in person, in writing or on the telephone. At a minimum, all borrowers are notified by mail when payments of principal and/or interest are 10 days past due. Real estate and commercial loan borrowers are assessed a late charge when payments are 10-15 days past due. Customers are contacted by a loan officer before the loan becomes 60 days delinquent. After 90 days, if the loan has not been brought current or an acceptable arrangement is not worked out with the borrower, we will institute measures to remedy the default, including commencing foreclosure action with respect to mortgage loans and repossessions of collateral in the case of consumer loans.

If foreclosure is effected, the property is sold at a public auction in which we may participate as a bidder. If we are the successful bidder, we include the acquired real estate property in our other real estate owned ("OREO") account until it is sold. These assets are initially recorded at fair value net of estimated selling costs. To the extent there is a subsequent decline in fair value, that amount is charged to operating expense. At December 31, 2020, we had OREO totaling $3.1 million.

Special Products and Services

To complement our array of loans, we also provide the following special products and services to our commercial customers:

Cash Management Services

Cash Management services are offered that enable the Bank's business customers to maximize the efficiency of their cash management. Specific products offered in our Cash Management services program include the following:

- Investment/sweep accounts
- Wire Transfer services
- Employer Services/Payroll processing services
- Zero balance accounts
- Night depository services
- Lockbox services
- Depository transfers
- Merchant services (third party)
- ACH originations
- Business debit cards
- Controlled disbursement accounts
- SONA 24/7 (Check 21 processing)
- Sonabank asset based lending (SABL)
- Mobiliti, a mobile banking application for personal and business accounts

Some of the products listed above are described in-depth below.

- **SONA 24/7/Check 21:** SONA 24/7 is ideal for landlords, property managers, medical professionals, and any other businesses that accept checks. SONA 24/7 allows customers of Sonabank to have total control over how, when, and where their checks will be deposited. SONA 24/7 uses the Check Truncation technology outlined by the "Check Clearing for the 21st Century Act", passed in October 2004 ("Check 21"). With Check Truncation, paper checks can be converted to electronic images and processed between participating banks, vastly speeding up the check clearing process. SONA In-House passes on the benefits of Check Truncation directly to Sonabank's business customers.

- **Lockbox Services:** Sonabank will open a lockbox, retrieve and scan incoming checks, and deposit them directly into the customer's account. The images of the checks will then be available to view online. This makes bookkeeping for the customer fast and easy, and because Sonabank is checking the lockbox daily, funds will often be available sooner. Big businesses have been using lockboxes for decades as a cash management tool. Sonabank makes this service cost effective for all small and medium sized businesses as well.

- **Employer Services:** Sonabank will provide its business clients with software that allows them to generate ACH payroll transactions to their employees' accounts.

- **SABL:** Asset Based Lending is a form of "collateral-based" lending. It is a combination of secured lending and short-term business lending. It is a specialized form of financing that allows a bank's commercial customers to pledge their working assets, typically accounts receivable and, to a lesser extent, inventory, as collateral to secure financing. Asset Based Lending borrowers are typically in the service, manufacturing or distribution fields.

  SABL is an Asset Based Lending software system built by Sonabank that allows the Bank to monitor the collateral of its commercial borrowers who have pledged their working assets (accounts receivables and other qualifying assets such as inventory) as collateral. SABL has the ability to track other offsets (liabilities, e.g.

other loans the customer has with the Bank) to the line of credit. SABL serves to provide the more stringent controls and supervision that this type of lending requires.

One control that is typical of Asset Based Lending is that the commercial borrower is required to have its customers remit invoice payments to a bank controlled lockbox. The bank retrieves these payments and the bank applies them directly to any outstanding balance on the line. SABL allows for this and can combine that service with remote capture (Check 21) if warranted.

Most Asset Based Lending systems are manual processes or software that certifies the borrowing base periodically. These certifications are usually provided in the form of manually created borrowing bases backed up with field exams. SABL provides a real time capability to analyze and adjust borrowing availability based on the levels of collateral at the moment.

SABL also offers an automated collateral upload, taking receivable information directly from the clients accounting system. SABL also offers discretionary borrowings and pay offs, allowing clients to borrow on or pay down their line at their discretion, as long as they are compliant with the SABL system. Lastly, SABL offers superior reporting, offering reports to bank officers that provide certain information they need to monitor risk. Customized reports can also be built for clients.

- **Mobiliti:** Sona Mobile is perfect for customers on the go, as it is available on a large variety of devices and networks. Sona Mobile offers easy access to account balances, transactions and internal transfers. Mobile Deposit allows customers to save time by eliminating the need to visit a branch. The customer can deposit a check through Sona Mobile by using their certified device (up to $5,000).

  Sona Business Mobile can help business customers manage their finances faster than ever. Customers have access to their information via a wide range of devices and networks. The shared user credentials and security settings between online and mobile banking make access more efficient for the business customer. Sona Business Mobile offers standard online banking features, along with enhanced features such as ACH & Wire transfer processing, including granting approvals to users to complete those processes. Mobile deposit is a time saving tool that allows business customers to deposit checks through Sona Business Mobile from their certified device (up to $10,000).

- **Other Consumer/Retail Products and Services.** Other products and services that are offered by the Bank are primarily directed toward the individual customer and include the following:

  - Debit cards
  - ATM services
  - Travelers Checks
  - Notary service in some branches
  - Wire transfers
  - Online banking with bill payment services
  - Credit Cards
  - Kasasa - rewards program

Competition

The banking business is highly competitive, and our profitability depends principally on our ability to compete in the market areas in which our banking operations are located. We experience substantial competition in attracting and retaining savings deposits and in lending funds. The primary factors we encounter in competing for savings deposits are convenient office locations and rates offered. Direct competition for savings deposits comes from other commercial bank and thrift institutions, money market mutual funds and corporate and government securities which may offer more attractive rates than insured depository institutions are willing to pay. The primary factors we encounter in competing for loans include, among others, interest rate and loan origination fees and the range of services offered. Competition for

origination of loans normally comes from other commercial banks, thrift institutions, mortgage bankers, mortgage brokers, insurance companies and fintech or digital lending companies. We have been able to compete effectively with other financial institutions by:

- emphasizing customer service and technology;
- establishing long-term customer relationships and building customer loyalty; and
- providing products and services designed to address the specific needs of our customers.

Human Capital

Our goal is to attract, develop, retain and plan for the succession of key talent and executives to achieve our strategic objectives. We are continually investing in our workforce to further emphasize diversity and inclusion and to foster our employees' growth and career development. At December 31, 2020, we had 382 employees, nearly all of whom are fulltime and of which approximately 75% were female and 25% were minorities. Fostering an inclusive environment requires that all employees are heard. Our Intranet houses the “Employee Voice” which is a vehicle for employees to make suggestions, asks questions or voice an opinion regarding the Company’s practices. We are launching “Work Place” on March 31, 2021, which is a social media platform that will allow our employees to interact with each other and share thoughts on what is important to them as an individual employee and as a community member.

While the majority of our employees reside in Virginia, our recruitment efforts are both local and nationwide. We utilize a wide range of recruitment vehicles ranging from college recruitment sites such as “Handshake” to posting on popular job boards and conducting nationwide profile searches to find qualified candidates. We realize that great people know other great people so we also offer a referral bonus to our employees. We offer a comprehensive benefits program to our employees that is designed to give employees the ability to select between a wide variety of benefits that meet their individual needs. We offer four different medical plans, two of which allow for the employee to make contributions and receive an employer match on a Health Savings Account. In addition to dental insurance, pet insurance, supplemental insurance and a 401k we offer employer paid short-term and long-term disability and life insurance. Our employees also enjoy a cash incentive for participating in our Wellness Program. All new employees attend “Systems Training” where they learn how to utilize key Company systems. New employees are also required to complete multiple learning modules that cover important compliance and regulatory requirements in the banking industry. We encourage all employees to obtain job related training by covering the cost of the classes and/or learning materials and tests.

We have maintained a commitment to the prosperity of each community the Company serves. In addition to providing financial products built for the needs of our customers, the Company uses associate volunteerism and corporate philanthropy to build strong community partnerships. Starting in 2021, each employee will be given 8 paid hours to volunteer in their community or charity of choice.

COVID-19 brought new challenges to the workplace this past year and we responded with personal protection equipment and guidance on how to mitigate the threat of COVID. Our branches were equipped with plexi-glass barriers and all employees were provided with masks and gloves. The 2020-2021 COVID Guide with corresponding Incident Report Form was implemented in 2020.

SUPERVISION AND REGULATION

Bank holding companies and banks are extensively regulated under federal and state law. This discussion is a summary and is qualified in its entirety by reference to the particular statutory and regulatory provisions described below, and is not intended to be an exhaustive description of the statutes or regulations applicable to Southern National or the Bank. The business of Southern National and the Bank is subject to extensive regulation and supervision under federal and state law, including oversight by the Board of Governors of the Federal Reserve System ("Federal Reserve") and the Virginia Bureau of Financial Institutions ("VBFI"), a regulatory division of the Virginia State Corporation Commission.

Changes in laws and regulations may alter the structure, regulation and competitive relationships of financial institutions. In addition, bank regulatory agencies may issue enforcement actions, policy statements, interpretive letters and similar written guidance applicable to us or the Bank. It cannot be predicted whether and in what form new laws and regulations, or interpretations thereof, may be adopted or the extent to which the business of Southern National and the Bank may be affected thereby, but they may have a material adverse effect on our business, operations, and earnings.

Violations of laws and regulations, or other unsafe and unsound practices, may result in regulatory agencies imposing fines or penalties, cease and desist orders, or taking other enforcement actions. Under certain circumstances, these agencies may enforce these remedies directly against officers, directors, employees and other parties participating in the affairs of a bank or bank holding company. Under federal and state laws and regulations pertaining to the safety and soundness of insured depository institutions, federal and state banking regulators have the authority to compel or restrict certain actions on our part if they determine that we have insufficient capital or other resources, or are otherwise operating in a manner that may be deemed to be inconsistent with safe and sound banking practices. Under this authority, our bank regulators can require us or our subsidiaries to enter into informal or formal supervisory agreements, including board resolutions, memoranda of understanding, written agreements and consent or cease and desist orders, pursuant to which we would be required to take identified corrective actions to address cited concerns and to refrain from taking certain actions.

If we become subject to and are unable to comply with the terms of any future regulatory actions or directives, supervisory agreements, or orders, then we could become subject to additional, heightened supervisory actions and orders, possibly including consent orders, prompt corrective action restrictions and/or other regulatory actions, including prohibitions on the payment of dividends on our common stock and preferred stock. If our regulators were to take such additional supervisory actions, then we could, among other things, become subject to significant restrictions on our ability to develop any new business, as well as restrictions on our existing business, and we could be required to raise additional capital, dispose of certain assets and liabilities within a prescribed period of time, or both. The terms of any such supervisory action could have a material negative effect on our business, reputation, operating flexibility, financial condition, and the value of our common stock and preferred stock.

Supervision, regulation, and examination of Southern National, the Bank, and our respective subsidiaries by the appropriate regulatory agencies, as described herein, are intended primarily for the protection of consumers, bank depositors and the Deposit Insurance Fund ("DIF") of The Federal Deposit Insurance Corporation ("FDIC") and the U.S. banking and financial system, rather than holders of our capital stock.

Bank Holding Company Regulation

Southern National is subject to extensive supervision and regulation by the Federal Reserve System pursuant to the Bank Holding Company Act of 1956, as amended (the "Bank Holding Company Act"). We are required to file with the Federal Reserve periodic reports and such other information as the Federal Reserve may request. Ongoing supervision is provided through regular examinations by the Federal Reserve and other means that allow the regulators to gauge management's ability to identify, assess and control risk in all areas of operations in a safe and sound manner and to ensure compliance with laws and regulations. In addition to regulation by the Federal Reserve as a bank holding company, Southern National is subject to supervision and regulation by the VBFI under the banking and general business corporation laws of the Commonwealth of Virginia.

Activity Limitations. Southern National is registered with the Federal Reserve as a bank holding company. Bank holding companies generally are limited to the business of banking, managing or controlling banks, and other activities that the Federal Reserve determines to be closely related to banking, or managing or controlling banks as to be a proper incident thereto. Bank holding companies are prohibited from acquiring or obtaining control of more than five percent (5%) of the outstanding voting interests of any company that engages in activities other than those activities permissible for bank holding companies. Examples of activities that the Federal Reserve has determined to be permissible are making, acquiring, brokering, or servicing loans; leasing personal property; providing certain investment or financial advice; performing certain data processing services; acting as agent or broker in selling credit life insurance and other insurance products in certain locations; and performing certain insurance underwriting activities. The Bank Holding Company Act does not place geographic limits on permissible non-banking activities of bank holding companies. Even with respect to permissible activities, however, the Federal Reserve has the power to order a holding company or its subsidiaries to terminate any activity or its control of any subsidiary when the Federal Reserve has reasonable cause to believe that continuation of such activity or control of such subsidiary would pose a serious risk to the financial safety, soundness or stability of any bank subsidiary of that holding company.

Source of Strength Obligations. A bank holding company is required to act as a source of financial and managerial strength to its subsidiary bank. The term “source of financial strength” means the ability of a company, such as us, that directly or indirectly owns or controls an insured depository institution, such as the Bank, to provide financial assistance to such insured depository institution in the event of financial distress. The appropriate federal banking agency for the depository institution (in the case of the Bank, this agency is the Federal Reserve) may require reports from us to assess our ability to serve as a source of strength and to enforce compliance with the source of strength requirements by requiring us to provide financial assistance to the Bank in the event of financial distress. If we were to enter bankruptcy or become subject to the orderly liquidation process established by the Dodd-Frank Act, any commitment by us to a federal bank regulatory agency to maintain the capital of the Bank would be assumed by the bankruptcy trustee or the FDIC, as appropriate, and entitled to a priority of payment. In addition, the FDIC provides that any insured depository institution generally will be liable for any loss incurred by the FDIC in connection with the default of, or any assistance provided by the FDIC to, a commonly controlled insured depository institution. The Bank is an FDIC-insured depository institution and thus subject to these requirements.

Acquisitions. The Bank Holding Company Act requires every bank holding company to obtain the prior approval of the Federal Reserve or waiver of such prior approval before it (1) acquires ownership or control of any voting shares of any bank if, after such acquisition, such bank holding company will own or control more than five percent (5%) of the voting shares of such bank, (2) acquires all of the assets of a bank, or (3) merges with any other bank holding company. In reviewing a proposed covered acquisition, among other factors, the Federal Reserve considers (1) the financial and managerial resources of the companies involved, including pro forma capital ratios; (2) the risk to the stability of the United States banking or financial system; (3) the convenience and needs of the communities to be served, including performance under the CRA; and (4) the effectiveness of the companies in combatting money laundering. The Federal Reserve also reviews any indebtedness to be incurred by a bank holding company in connection with a proposed acquisition to ensure that the bank holding company can service such indebtedness without adversely affecting its ability to serve as a source of strength to its bank subsidiaries. Well capitalized and well managed bank holding companies are permitted to acquire control of banks in any state, subject to federal regulatory approval, without regard to whether such a transaction is prohibited by the laws of any state. However, a bank holding company may not, following an interstate acquisition, control more than 10% of nationwide insured deposits or 30% of deposits within any state in which the acquiring bank operates.

Change in Control. Federal law restricts the amount of voting stock of a bank holding company or a bank that a person (including an entity) may acquire without the prior approval of banking regulators. Under the federal Change in Bank Control Act and the regulations thereunder, a person or group must give advance notice to and obtain approval from the Federal Reserve before acquiring control of any bank holding company, such as Southern National. The Change in Bank Control Act creates a rebuttable presumption of control if a person or group acquires the power to vote 10% or more of our outstanding common stock. The overall effect of such laws is to make it more difficult to acquire a bank holding company and a bank by tender offer or similar means than it might be to acquire control of another type of corporation. Consequently, shareholders of the Company may be less likely to benefit from the rapid increases in stock

prices that may result from tender offers or similar efforts to acquire control of other companies. Investors should be aware of these requirements when acquiring shares of our stock.

Virginia Law. Certain state corporation laws may have an anti-takeover affect. Virginia law restricts transactions between a Virginia corporation and its affiliates and potential acquirers. The following discussion summarizes the two Virginia statutes that may discourage an attempt to acquire control of Southern National.

Virginia Code Sections 13.1-725 – 727.1 govern “Affiliated Transactions.” These provisions, with several exceptions discussed below, require approval by the holders of at least two-thirds of the remaining voting shares of material acquisition transactions between a Virginia corporation and any holder of more than 10% of any class of its outstanding voting shares. Affiliated Transactions include mergers, share exchanges, material dispositions of corporate assets not in the ordinary course of business, any dissolution of the corporation proposed by or on behalf of an interested shareholder, or any reclassification, including a reverse stock split, recapitalization, or merger of the corporation with its subsidiaries which increases the percentage of voting shares owned beneficially by any 10% shareholder by more than 5%.

These provisions were designed to deter certain takeovers of Virginia corporations. In addition, the statute provides that, by affirmative vote of a majority of the voting shares other than shares owned by any 10% shareholder, a corporation can adopt an amendment to its articles of incorporation or bylaws providing that the Affiliated Transactions provisions shall not apply to the corporation. Southern National “opted out” of the Affiliated Transactions provisions when it incorporated.

Virginia law also provides that shares acquired in a transaction that would cause the acquiring person’s voting strength to meet or exceed any of the three thresholds (20%, 33.33% or 50%) have no voting rights for those shares exceeding that threshold, unless granted by a majority vote of shares not owned by the acquiring person. This provision empowers an acquiring person to require the Virginia corporation to hold a special meeting of shareholders to consider the matter within 50 days of the request. Southern National also “opted out” of this provision at the time of its incorporation.

Governance and Financial Reporting Obligations. We are required to comply with various corporate governance and financial reporting requirements under the Sarbanes-Oxley Act of 2002, as well as rules and regulations adopted by the SEC, the Public Company Accounting Oversight Board, and NASDAQ. In particular, we are required to include management and independent registered public accounting firm reports on internal controls as part of our Annual Report on Form 10-K in order to comply with Section 404 of the Sarbanes-Oxley Act. We have evaluated our controls, including compliance with the SEC rules on internal controls, and have and expect to continue to spend significant amounts of time and money on compliance with these rules. Our failure to comply with these internal control rules may materially adversely affect our reputation, ability to obtain the necessary certifications to financial statements, and the values of our securities.

Corporate Governance. The Dodd-Frank Act addressed many investor protections, corporate governance, and executive compensation matters that will affect most U.S. publicly traded companies. The Dodd-Frank Act (1) granted shareholders of U.S. publicly traded companies an advisory vote on executive compensation; (2) enhanced independence requirements for Compensation Committee members; and (3) required companies listed on national securities exchanges to adopt incentive-based compensation claw-back policies for executive officers.

Incentive Compensation. The Dodd-Frank Act required the banking agencies and the SEC to establish joint rules or guidelines for financial institutions with more than $1.0 billion in assets, such as Southern National and the Bank, which prohibit incentive compensation arrangements that the agencies determine to encourage inappropriate risks by the institution. The federal banking agencies issued proposed rules in 2011 and previously issued guidance on sound incentive compensation policies. In 2016, the federal banking agencies also proposed rules that would, depending upon the assets of the institution, directly regulate incentive compensation arrangements and would require enhanced oversight and recordkeeping. As of December 31, 2020, these rules have not been implemented. We and Sonabank have undertaken efforts to ensure that our incentive compensation plans do not encourage inappropriate risks, consistent with three key principles—that incentive compensation arrangements should appropriately balance risk and financial rewards, be compatible with effective controls and risk management, and be supported by strong corporate governance.

Shareholder Say-On-Pay Votes. The Dodd-Frank Act requires public companies to take shareholders' votes on proposals addressing compensation (known as say-on-pay), the frequency of a say-on-pay vote, and the golden parachutes available to executives in connection with change-in-control transactions. Public companies must give shareholders the opportunity to vote on the compensation at least every three years and the opportunity to vote on frequency at least every six years, indicating whether the say-on-pay vote should be held annually, biennially, or triennially.

Anti-tying rules. A bank holding company and its subsidiaries are prohibited from engaging in certain tying arrangements in connection with extensions of credit, leases or sales of property, or furnishing of services.

Capital Requirements

Southern National and the Bank are each required under federal law to maintain certain minimum capital levels based on ratios of capital to total assets and capital to risk-weighted assets. The required capital ratios are minimums, and the federal banking agencies may determine that a banking organization, based on its size, complexity or risk profile, must maintain a higher level of capital in order to operate in a safe and sound manner. Risks such as concentration of credit risks and the risk arising from non-traditional activities, as well as the institution's exposure to a decline in the economic value of its capital due to changes in interest rates, and an institution's ability to manage those risks are important factors that are to be taken into account in assessing an institution's overall capital adequacy. The following is a brief description of the relevant provisions of these capital rules and their potential impact on our capital levels.

Southern National and the Bank are each subject to the following risk-based capital ratios: a common equity Tier 1 ("CET1") risk-based capital ratio, a Tier 1 risk-based capital ratio, which includes CET1 and additional Tier 1 capital, and a total risk-based capital ratio, which includes Tier 1 and Tier 2 capital. CET1 is primarily comprised of the sum of common stock instruments and related surplus net of treasury stock, plus retained earnings and certain qualifying minority interests, less certain adjustments and deductions, including with respect to goodwill, intangible assets, mortgage servicing assets and deferred tax assets subject to temporary timing differences. Additional Tier 1 capital is primarily comprised of noncumulative perpetual preferred stock, tier 1 minority interests and grandfathered trust preferred securities. Tier 2 capital consists of instruments disqualified from Tier 1 capital, including qualifying subordinated debt, other preferred stock and certain hybrid capital instruments, and a limited amount of loan loss reserves up to a maximum of 1.25% of risk-weighted assets, subject to certain eligibility criteria. The capital rules also define the risk-weights assigned to assets and off-balance sheet items to determine the risk-weighted asset components of the risk-based capital rules, including, for example, certain "high volatility" commercial real estate, past due assets, structured securities and equity holdings.

The leverage capital ratio, which serves as a minimum capital standard, is the ratio of Tier 1 capital to quarterly average total consolidated assets net of goodwill, certain other intangible assets, and certain required deduction items. The required minimum leverage ratio for all banks is 4%.

In addition, effective January 1, 2019, the capital rules require a capital conservation buffer of CET1 of 2.5% above each of the minimum capital ratio requirements (CET1, Tier 1, and total risk-based capital), which is designed to absorb losses during periods of economic stress. These buffer requirements must be met for a bank or bank holding company to be able to pay dividends, engage in share buybacks or make discretionary bonus payments to executive management without restriction.

The Federal Deposit Insurance Corporation Improvement Act of 1991 ("FDICIA"), among other things, requires the federal bank regulatory agencies to take "prompt corrective action" regarding depository institutions that do not meet minimum capital requirements. FDICIA establishes five regulatory capital tiers: "well capitalized", "adequately capitalized", "undercapitalized", "significantly undercapitalized", and "critically undercapitalized". A depository institution's capital tier will depend upon how its capital levels compare to various relevant capital measures and certain other factors, as established by regulation. FDICIA generally prohibits a depository institution from making any capital distribution (including payment of a dividend) or paying any management fee to its holding company if the depository

institution would thereafter be undercapitalized. The FDICIA imposes progressively more restrictive restraints on operations, management and capital distributions, depending on the category in which an institution is classified.

To be well-capitalized, the Bank must maintain at least the following capital ratios:

- 6.5% CET1 to risk-weighted assets;
- 8.0% Tier 1 capital to risk-weighted assets;
- 10.0% Total capital to risk-weighted assets; and
- 5.0% leverage ratio.

The Federal Reserve has not yet revised the well-capitalized standard for bank holding companies to reflect the higher capital requirements imposed under the current capital rules. For purposes of the Federal Reserve's Regulation Y, bank holding companies, such as Southern National, must maintain a Tier 1 risk-based capital ratio of 6.0% or greater and a total risk-based capital ratio of 10.0% or greater to be well-capitalized. If the Federal Reserve were to apply the same or a similar well-capitalized standard to bank holding companies as that applicable to the Bank, Southern National's capital ratios as of December 31, 2020 would exceed such revised well-capitalized standard. Also, the Federal Reserve may require bank holding companies, including Southern National, to maintain capital ratios substantially in excess of mandated minimum levels, depending upon general economic conditions and a bank holding company's particular condition, risk profile and growth plans.

Failure to be well-capitalized or to meet minimum capital requirements could result in certain mandatory and possible additional discretionary actions by regulators that, if undertaken, could have an adverse material effect on our operations or financial condition. Failure to meet minimum capital requirements could also result in restrictions on Southern National's or the Bank's ability to pay dividends or otherwise distribute capital or to receive regulatory approval of applications or other restrictions on its growth.

Both Southern National and the Bank's regulatory capital ratios were above the applicable well-capitalized standards and met the capital conservation buffer as of December 31, 2020. Based on current estimates, we believe that Southern National and the Bank will continue to exceed all applicable well-capitalized regulatory capital requirements and the capital conservation buffer in 2021.

On October 29, 2019, the federal banking agencies jointly issued a final rule to simplify the regulatory capital requirements for eligible banks and holding companies with less than $10 billion in consolidated assets that opt into the Community Bank Leverage Ratio ("CBLR") framework. A qualifying community banking organization with total consolidated assets of less than $10 billion that exceeds the CBLR threshold would be exempt from the agencies' current capital framework, including the risk-based capital requirements and capital conservation buffer described above, and would be deemed well-capitalized under the agencies' prompt corrective action regulations. Under the final rule, if a qualifying community banking organization elects to use the CBLR framework, it will be considered "well-capitalized" so long as its CBLR is greater than 9%. Southern National does not use the CBLR framework.

In June 2016, the FASB issued ASU 2016-13, which introduced CECL as the methodology to replace the current "incurred loss" methodology for financial assets measured at amortized cost, and changed the approaches for recognizing and recording credit losses on available-for-sale debt securities and purchased credit impaired financial assets. Under the incurred loss methodology, credit losses are recognized only when the losses are probable or have been incurred; under CECL, companies are required to recognize the full amount of expected credit losses for the lifetime of the financial assets, based on historical experience, current conditions and reasonable and supportable forecasts. This change results in earlier recognition of credit losses that the Company deems expected but not yet probable. For SEC reporting companies that do not meet the definition of a smaller reporting company and with December 31 calendar year ends, such as the Company, CECL became effective January 1, 2020. The CARES Act allowed us to delay implementation until December 31, 2020.

Payment of Dividends

Southern National is a legal entity separate and distinct from the Bank and other subsidiaries. Its primary source of cash, other than securities offerings, is dividends from the Bank. Under the Federal Deposit Insurance Act, no dividends may be paid by an insured bank if the bank is in arrears in the payment of any insurance assessment due to the FDIC. The payment of dividends by the Bank may also be affected by other regulatory requirements and policies, such as the maintenance of adequate capital. If, in the opinion of the applicable regulatory authority, a bank under its jurisdiction is engaged in, or is about to engage in, an unsafe or unsound practice (which, depending on the financial condition of the bank, could include the payment of dividends), such authority may require, after notice and hearing, that such bank cease and desist from such practice. The Federal Reserve has formal and informal policies which provide that insured banks should generally pay dividends only out of current operating earnings.

Under a Federal Reserve policy adopted in 2009, the board of directors of a bank holding company must consider certain factors to ensure that its dividend level is prudent relative to maintaining a strong financial position, and is not based on overly optimistic earnings scenarios, such as potential events that could affect its ability to pay, while still maintaining a strong financial position. As a general matter, the Federal Reserve has indicated that the board of directors of a bank holding company should consult with the Federal Reserve and eliminate, defer or significantly reduce the bank holding company's dividends if:

- its net income available to shareholders for the past four quarters, net of dividends previously paid during that period, is not sufficient to fully fund the dividends;
- its prospective rate of earnings retention is not consistent with its capital needs and overall current and prospective financial condition; or
- it will not meet, or is in danger of not meeting, its minimum regulatory capital adequacy ratios.

Bank Regulation

The operation of the Bank is subject to state and federal statutes applicable to state banks and the regulations of the Federal Reserve, the FDIC and the Consumer Financial Protection Bureau ("CFPB"). The operations of the Bank may also be subject to applicable Office of the Comptroller of the Currency ("OCC") regulation to the extent state banks are granted parity with national banks. Such statutes and regulations relate to, among other things, required reserves, investments, loans, mergers and consolidations, issuances of securities, payments of dividends, establishment of branches, consumer protection and other aspects of the Bank's operations. Violations of laws and regulations, or other unsafe and unsound practices, may result in these agencies imposing fines or penalties, cease and desist orders, or taking other enforcement actions. Under certain circumstances, these agencies may enforce these remedies directly against officers, directors, employees and other parties participating in the affairs of a bank or bank holding company.

Safety and Soundness. The Federal Deposit Insurance Act requires the federal prudential bank regulatory agencies, such as the Federal Reserve, to prescribe, by regulation or guideline, operational and managerial standards for all insured depository institutions relating to: (1) internal controls; (2) information systems and audit systems; (3) loan documentation; (4) credit underwriting; (5) interest rate risk exposure; and (6) asset quality. The agencies also must prescribe standards for asset quality, earnings, and stock valuation, as well as standards for compensation, fees and benefits. The federal banking agencies have adopted regulations and Interagency Guidelines Establishing Standards for Safety and Soundness to implement these required standards. These guidelines set forth the safety and soundness standards used to identify and address problems at insured depository institutions before capital becomes impaired. Under the regulations, if a regulator determines that a bank fails to meet any standards prescribed by the guidelines, the regulator may require the bank to submit an acceptable plan to achieve compliance, consistent with deadlines for the submission and review of such safety and soundness compliance plans.

Examinations. The Bank is subject to regulation, reporting, and periodic examinations by the Federal Reserve and the VBFI. These regulatory authorities routinely examine the Bank's reserves, loan and investment quality, consumer compliance, management policies, procedures and practices and other aspects of operations. The Federal Reserve has adopted the Federal Financial Institutions Examination Council's ("FFIEC") rating system and assigns each financial institution a confidential composite rating based on an evaluation and rating of six essential components of an

institution's financial condition and operations, including Capital Adequacy, Asset Quality, Management, Earnings, Liquidity and Sensitivity to Market Risk, as well as the quality of risk management practices.

Consumer Protection. The Dodd-Frank Act established the CFPB, an independent regulatory authority housed within the Federal Reserve having centralized authority, including examination and enforcement authority, for consumer protection in the banking industry. The CFPB has rule writing, examination, and enforcement authority with regard to the Bank's (and Southern National's) compliance with a wide array of consumer financial protection laws, including the Truth in Lending Act, the Real Estate Settlement Procedures Act, the Truth in Savings Act, the Electronic Funds Transfer Act, the Equal Credit Opportunity Act, the Home Mortgage Disclosure Act, the S.A.F.E. Mortgage Licensing Act, the Fair Credit Reporting Act (except Sections 615(e) and 628), the Fair Debt Collection Practices Act, and the Gramm-Leach-Bliley Act (sections 502 through 509 relating to privacy), among others. The CFPB has broad authority to enforce a prohibition on unfair, deceptive, or abusive acts and practices. Authority to supervise and examine Southern National and the Bank for compliance with federal consumer laws remains largely with the Federal Reserve. However, the CFPB may participate in examinations on a "sampling basis" and may refer potential enforcement actions against such institutions to their primary regulators. In addition, the Dodd-Frank Act permits states to adopt consumer protection laws and regulations that are stricter than those regulations promulgated by the CFPB, and state attorneys general are permitted to enforce consumer protection rules adopted by the CFPB against certain institutions.

Deposit Insurance Assessments. The Deposit Insurance Fund ("DIF") of the FDIC insures the deposits of the Bank generally up to a maximum of $250,000 per depositor, per insured bank, for each account ownership category. The FDIC charges insured depository institutions quarterly premiums to maintain the DIF. Deposit insurance assessments are based on average total consolidated assets minus its average tangible equity, and take into account certain risk-based financial ratios and other factors. The assessment rate schedule can change from time to time, at the discretion of the FDIC, subject to certain limits.

Insurance of deposits may be terminated by the FDIC upon a finding that an institution has engaged in unsafe or unsound practices, is in an unsafe or unsound condition to continue operations or has violated any applicable law, regulation, rule, order or condition imposed by a bank's federal regulatory agency. In addition, the Federal Deposit Insurance Act provides that, in the event of the liquidation or other resolution of an insured depository institution, the claims of depositors of the institution, including the claims of the FDIC as subrogee of insured depositors, and certain claims for administrative expenses of the FDIC as a receiver, will have priority over other general unsecured claims against the institution, including those of the parent bank holding company.

Insider Transactions. The Federal Reserve has adopted regulations that restrict preferential loans and loan amounts to "affiliates" and "insiders" of banks, require banks to keep information on loans to major shareholders and executive officers and bar certain director and officer interlocks between financial institutions.

Reserves. The Bank is subject to Federal Reserve regulations that require the Bank to maintain reserves against transaction accounts (primarily checking accounts). These reserve requirements are subject to annual adjustment by the Federal Reserve. Effective March 26, 2020, reserve requirement ratios were reduced to zero percent.

Anti-Money Laundering. A continued focus of governmental policy relating to financial institutions in recent years has been combating money laundering and terrorist financing. The USA PATRIOT Act broadened the application of anti-money laundering regulations to apply to additional types of financial institutions such as broker-dealers, investment advisors and insurance companies, and strengthened the ability of the U.S. Government to help prevent, detect and prosecute international money laundering and the financing of terrorism. The principal provisions of Title III of the USA PATRIOT Act require that regulated financial institutions, including state member banks: (i) establish an anti-money laundering program that includes training and audit components; (ii) comply with regulations regarding the verification of the identity of any person seeking to open an account; (iii) take additional required precautions with non-U.S. owned accounts; and (iv) perform certain verification and certification of money laundering risk for their foreign correspondent banking relationships. Failure of a financial institution to comply with the USA PATRIOT Act's requirements could have serious legal and reputational consequences for the institution. Sonabank has augmented its systems and procedures to meet the requirements of these regulations and will continue to revise and update its policies, procedures and controls to reflect changes required by law.

FinCEN has adopted rules that require financial institutions to obtain beneficial ownership information with respect to legal entities with which such institutions conduct business, subject to certain exclusions and exemptions. Bank regulators are focusing their examinations on anti-money laundering compliance, and we continue to monitor and augment, where necessary, our anti-money laundering compliance programs.

Bank regulators routinely examine institutions for compliance with these anti-money laundering obligations and have been active in imposing "cease and desist" and other regulatory orders and money penalty sanctions against institutions found to be in violation of these requirements. On January 1, 2021, Congress passed federal legislation that made sweeping changes to federal anti-money laundering laws, including changes that will be implemented in 2021 and subsequent years.

Economic Sanctions. The Office of Foreign Assets Control ("OFAC") is responsible for helping to ensure that U.S. entities do not engage in transactions with certain prohibited parties, as defined by various Executive Orders and acts of Congress. OFAC publishes, and routinely updates, lists of names of persons and organizations suspected of aiding, harboring or engaging in terrorist acts, including the Specially Designated Nationals and Blocked Persons List. If we find a name on any transaction, account or wire transfer that is on an OFAC list, we must undertake certain specified activities, which could include blocking or freezing the account or transaction requested, and we must notify the appropriate authorities.

Concentrations in Lending. During 2006, the federal bank regulatory agencies released guidance on "Concentrations in Commercial Real Estate Lending" (the "Guidance") and advised financial institutions of the risks posed by CRE lending concentrations. The Guidance requires that appropriate processes be in place to identify, monitor and control risks associated with real estate lending concentrations. Higher allowances for credit losses and capital levels may also be required. The Guidance is triggered when CRE loan concentrations exceed either:

- Total reported loans for construction, land development, and other land of 100% or more of a bank's total risk based capital; or
- Total reported loans secured by multifamily and nonfarm nonresidential properties and loans for construction, land development, and other land of 300% or more of a bank's total risk based capital.

The Guidance also applies when a bank has a sharp increase in CRE loans or has significant concentrations of CRE secured by a particular property type. The Guidance also applies when a bank has a sharp increase in CRE loans or has significant concentrations of CRE secured by a particular property type.

Community Reinvestment Act. The Bank is subject to the provisions of the CRA, which imposes a continuing and affirmative obligation, consistent with their safe and sound operation, to help meet the credit needs of entire communities where the bank accepts deposits, including low- and moderate-income neighborhoods. The Federal Reserve's assessment of the Bank's CRA record is made available to the public. Further, a less than satisfactory CRA rating will slow, if not preclude, expansion of banking activities and prevent a company from becoming or remaining a financial holding company. Federal CRA regulations require, among other things, that evidence of discrimination against applicants on a prohibited basis, and illegal or abusive lending practices be considered in the CRA evaluation. The Bank has a rating of "Satisfactory" in its most recent CRA evaluation.

Consumer Regulation. Activities of the Bank are subject to a variety of statutes and regulations designed to protect consumers. These laws and regulations include, among numerous other things, provisions that:

- limit the interest and other charges collected or contracted for by the Bank, including rules respecting the terms of credit cards and of debit card overdrafts;
- govern the Bank's disclosures of credit terms to consumer borrowers;
- require the Bank to provide information to enable the public and public officials to determine whether it is fulfilling its obligation to help meet the housing needs of the community it serves;
- prohibit the Bank from discriminating on the basis of race, creed or other prohibited factors when it makes decisions to extend credit;

- govern the manner in which the Bank may collect consumer debts; and
- prohibit unfair, deceptive or abusive acts or practices in the provision of consumer financial products and services.

Mortgage Rules. Pursuant to rules adopted by the CFPB, banks that make residential mortgage loans are required to make a good faith determination that a borrower has the ability to repay a mortgage loan prior to extending such credit, require that certain mortgage loans contain escrow payments, obtain new appraisals under certain circumstances, comply with integrated mortgage disclosure rules, and follow specific rules regarding the compensation of loan originators and the servicing of residential mortgage loans.

Transactions with affiliates. There are various restrictions that limit the ability of the Bank to finance, pay dividends or otherwise supply funds to Southern National or other affiliates. In addition, banks are subject to certain restrictions under Section 23A and B of the Federal Reserve Act on certain transactions, including any extension of credit to its bank holding company or any of its other affiliates, on investments in the securities thereof, and on the taking of such securities as collateral for loans to any borrower.

Privacy and Cybersecurity. The Bank is subject to federal and state banking regulations that limit its ability to disclose non-public information about consumers to non-affiliated third parties. These limitations require us to periodically disclose our privacy policies to consumers and allow consumers to prevent disclosure of certain personal information to a non-affiliated third party under certain circumstances. Consumers also have the option to direct banks and other financial institutions not to share information about transactions and experiences with affiliated companies for the purpose of marketing products or services. Banking institutions are required to implement a comprehensive information security program that includes administrative, technical, and physical safeguards to ensure the security and confidentiality of customer records and information. These security and privacy policies and procedures for the protection of confidential and personal information are in effect across our lines of business. Furthermore, the federal banking regulators regularly issue guidance regarding cybersecurity intended to enhance cyber risk management. A financial institution is expected to implement multiple lines of defense against cyber-attacks and ensure that their risk management procedures address the risk posed by potential cyber threats. A financial institution is further expected to maintain procedures to effectively respond to a cyber-attack and resume operations following any such attack. Southern National has adopted and implemented policies and procedures to comply with these privacy, information security, and cybersecurity requirements. On December 18, 2020, the federal banking agencies proposed a new rule that would require banks to notify their regulators within 36 hours of a “computer-security incident” that rises to the level of a “notification incident.”

Audit Reports. Insured institutions with total assets of $500 million or more must submit annual audit reports prepared by independent auditors to federal and state regulators. In some instances, the audit report of the institution’s holding company can be used to satisfy this requirement. Independent auditors must receive examination reports, supervisory agreements and reports of enforcement actions. For insured institutions with total assets of $1.0 billion or more, financial statements prepared in accordance with U.S. GAAP, management’s certifications concerning responsibility for the financial statements, internal controls and compliance with legal requirements designated by the FDIC, and an attestation by the independent auditor regarding the statements of management relating to the internal controls must be submitted. For insured institutions with total assets of more than $3.0 billion, independent auditors may be required to review quarterly financial statements. The FDICIA requires that institutions with total assets of $1.0 billion or more have independent audit committees, consisting of outside directors only. The committees of insured institutions with total assets of $3.0 billion or more must include members with experience in banking or financial management, must have access to outside counsel, and must not include representatives of large customers.

The foregoing is only a brief summary of certain statutes, rules, and regulations that may affect Southern National and the Bank. Numerous other statutes and regulations also will have an impact on the operations of Southern National and the Bank. Supervision, regulation and examination of banks by the regulatory agencies are intended primarily for the protection of depositors, not shareholders.

Item 1A. Risk Factors

An investment in our common stock involves risks. The following is a description of the material risks and uncertainties that Southern National believes affect its business and should be considered before making an investment in our common stock. 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 the risks described in this Annual Report on Form 10-K were to actually occur, our financial condition, results of operations and cash flows could be materially and adversely affected. If this were to happen, the value of our common stock could decline significantly and you could lose part or all of your investment. This Form 10-K also contains forward-looking statements that may not be realized as a result of certain factors, including, but not limited to, the risks described herein and in our other public filings with the SEC. Please refer to the section in this Form 10-K entitled "Special Cautionary Notice Regarding Forward-Looking Statements" for additional information regarding forward-looking statements.

Strategic Risks

Our business strategy includes strategic growth, and our financial condition and results of operations could be negatively affected if we fail to grow or fail to manage our growth effectively.

We intend to continue pursuing a growth strategy for our business. Our prospects must be considered in light of the risks, expenses and difficulties frequently encountered by growing companies such as the continuing need for infrastructure and personnel, the time and costs inherent in integrating a series of different operations and the ongoing expense of acquiring and staffing new banks or branches. We may not be able to expand our presence in our existing markets or successfully enter new markets and any expansion could adversely affect our results of operations. Failure to manage our growth effectively could have a material adverse effect on our business, future prospects, financial condition or results of operations, and could adversely affect our ability to successfully implement our business strategy. Our ability to grow successfully will depend on a variety of factors, including the continued availability of desirable business opportunities, the competitive responses from other financial institutions in our market areas and our ability to manage our growth.

Although there can be no assurance of success or the availability of branch or bank acquisitions in the future we may seek to supplement our internal growth through attractive acquisitions. We cannot predict the number, size or timing of acquisitions, or whether any such acquisition will occur at all. Our acquisition efforts have traditionally focused on targeted banking entities in markets in which we currently operate and markets in which we believe we can compete effectively. However, as consolidation of the financial services industry continues, the competition for suitable acquisition candidates may increase and, as the number of appropriate targets decreases, the prices for potential acquisitions could increase which could reduce our potential returns, and reduce the attractiveness of these opportunities to us. We may compete with other financial services companies for acquisition opportunities, and many of these competitors have greater financial resources than we do and may be able to pay more for an acquisition than we are able or willing to pay.

We must respond to rapid technological changes and these changes may be more difficult or expensive than anticipated.

If competitors introduce new products and services embodying new technologies, or if new industry standards and practices emerge, our existing product and service offerings, technology and systems may become obsolete. Further, if we fail to adopt or develop new technologies or to adapt our products and services to emerging industry standards, we may lose current and future customers, which could have a material adverse effect on our business, financial condition and results of operations. The financial services industry is changing rapidly and in order to remain competitive, we must continue to enhance and improve the functionality and features of our products, services and technologies. These changes may be more difficult or expensive than we anticipate.

The implementation of other new lines of business or new products and services may subject us to additional risk.

We continuously evaluate our service offerings and may implement new lines of business or offer new products and services within existing lines of business in the future. There are substantial risks and uncertainties associated with these efforts. In developing and marketing new lines of business and/or new products and services, we undergo a new product process to assess the risks of the initiative, and invest significant time and resources to build internal controls, policies and procedures to mitigate those risks, including hiring experienced management to oversee the implementation of the initiative. Initial timetables for the introduction and development of new lines of business and/or new products or services may not be achieved and price and profitability targets may not prove feasible. External factors, such as compliance with regulations, competitive alternatives, and shifting market preferences, may also impact the successful implementation of a new line of business and/or a new product or service. Furthermore, any new line of business and/or new product or service could require the establishment of new key and other controls and have a significant impact on our existing system of internal controls. In addition, the financial services market, including banking services, is undergoing rapid changes with frequent introductions of new technology-driven products and services. Our future success may depend, in part, on our ability to use technology competitively to offer products and services that provide convenience to customers and create additional efficiencies in our operations. The widespread adoption of new technologies has and will continue to require us to make substantial capital expenditures to modify or adapt our systems to remain competitive and offer new products and services. Our ability to effectively implement new technologies to improve our operations and systems will impact our competitive position in the financial services industry. Furthermore, we may not be successful in introducing new products and services in response to industry trends or developments in technology, or those new products may not be accepted by customers. Failure to successfully manage these risks in the development and implementation of new lines of business and/or new products or services could have a material adverse effect on our business and, in turn, our financial condition and results of operations.

We may not be able to successfully integrate our acquisitions or to realize the anticipated benefits of them.

A successful integration of each acquired bank with ours will depend substantially on our ability to successfully consolidate operations, corporate cultures, systems and procedures and to eliminate redundancies and costs. While we have substantial experience in successfully integrating institutions we have acquired, we may encounter difficulties during integration, such as:

- the loss of key employees;
- the disruption of operations and businesses;
- loan and deposit attrition, customer loss and revenue loss;
- possible inconsistencies in standards, control procedures and policies;
- unexpected issues with expected branch closures; and/or
- unexpected issues with costs, operations, personnel, technology and credit;

all of which could divert resources from regular banking operations. Additionally, general market and economic conditions or governmental actions affecting the financial industry generally may inhibit our successful merger integrations.

Further, we acquire banks with the expectation that these mergers will result in various benefits including, among other things, benefits relating to enhanced revenues, a strengthened market position for the combined company, cross selling opportunities, technology, cost savings and operating efficiencies. Achieving the anticipated benefits of these mergers is subject to a number of uncertainties, including whether we integrate these institutions in an efficient and effective manner, and general competitive factors in the marketplace. Failure to achieve these anticipated benefits could result in a reduction in the price of our shares as well as in increased costs, decreases in the amount of expected revenues and diversion of management's time and energy and could materially and adversely affect our business, financial condition and operating results.

Operational Risks

Outbreak of the novel coronavirus disease 2019 (“COVID-19”) has had and will likely continue to have an adverse impact on the markets in which we operate and on our business, operations and financial condition.

The outbreak of COVID-19 has adversely impacted a broad range of industries in which the Company’s customers operate and has impaired and could continue to impair their ability to fulfill their financial obligations to the Company. In March 2020, the World Health Organization declared COVID-19 to be a global pandemic. The spread of COVID-19 has caused significant uncertainty, volatility and disruption in the U.S. and global economy and has disrupted banking and other financial activity in the areas in which the Company operates. Given the ongoing and dynamic nature COVID-19, it is not possible to accurately predict the extent, severity or duration of these conditions or when normal economic and operating conditions will resume. For this reason, the extent to which the COVID-19 pandemic affects our business, operations and financial condition, as well as our regulatory capital and liquidity ratios and credit ratings, is highly uncertain and unpredictable and depends on, among other things, new information that may emerge concerning the scope, duration and severity of the COVID-19 pandemic and actions taken by governmental authorities and other parties in response to the pandemic. If the pandemic is prolonged, the adverse impact on the markets in which we operate and on our business, operations and financial condition could deepen.

Congress, the President, and the Federal Reserve have taken several actions designed to minimize the economic impact of COVID-19. The Coronavirus Aid, Relief and Economic Security (“CARES”) Act was signed into law at the end of March 2020 as a $2 trillion legislative package. The goal of the CARES Act is to prevent a severe economic downturn through various measures, including direct financial aid to American families and economic stimulus to significantly impacted industry sectors. The package also includes extensive emergency funding for hospitals and healthcare providers. In addition to the general impact of COVID-19, certain provisions of the CARES Act as well as other recent legislative and regulatory relief efforts have had and are expected to continue to have a material impact on the Company’s operations. The CARES Act includes provisions that temporarily delay the required implementation date of Financial Accounting Standards Board (“FASB”) Accounting Standards Codification (“ASC”) Topic 326, *Financial Instruments—Credit Losses*, and suspend the requirements related to accounting for a troubled debt restructuring (“TDR”), for certain entities.

The Company’s business is dependent upon the willingness and ability of its employees and customers to conduct banking and other financial transactions. If the global response to contain COVID-19 escalates further or is unsuccessful, the Company could experience a material adverse effect on its business, financial condition, results of operations and cash flows. While it is not possible to know the full universe or extent that the impact of COVID-19, and resulting measures to curtail its spread, will have on the Company’s operations, the Company is disclosing potentially material items of which it is aware.

Capital and liquidity

While the Company believes that it has sufficient capital to withstand an extended economic recession brought about by COVID-19, its reported and regulatory capital ratios could be adversely impacted by further credit losses. The Company relies on cash on hand as well as dividends from its subsidiary bank to service its debt. If the Company’s capital deteriorates such that its subsidiary bank is unable to pay dividends to it for an extended period of time, the Company may not be able to service its debt.

The Company maintains access to multiple sources of liquidity. Wholesale funding markets have remained open to us, but rates for short term funding have recently been volatile. If funding costs are elevated for an extended period of time, it could have an adverse effect on the Company’s net interest margin. If an extended recession causes a large number of the Company’s deposit customers to withdraw their funds, the Company might become more reliant on volatile or more expensive sources of funding.

COVID-19 could cause a further and sustained decline in the Company’s stock price or the occurrence of what management would deem to be an event that could, under certain circumstances, cause us to perform another goodwill impairment test and result in an impairment charge being recorded for that period. In the event that the Company

concludes that all or a portion of its goodwill is impaired, a non-cash charge for the amount of such impairment would be recorded to earnings. Such a charge would have no impact on tangible capital or regulatory capital.

Lending operations and accommodations to borrowers

As a result of COVID-19, businesses in the Company's markets have experienced significant operational disruptions. In accordance with regulatory guidelines to work with borrowers during this unstable economic environment, the Company provided certain modifications, including interest only or principal and interest deferments. As of December 31, 2020, total modified loans or loans with requests for modifications were $122.0 million and the Company anticipates minimal additional deferrals in 2021.

With the passage of the Paycheck Protection Program ("PPP"), administered by the Small Business Administration ("SBA"), the Company is actively assisting its customers with loan applications through the program. PPP loans have a two or five year term and earn interest at 1%. The Company believes that the majority of these loans will ultimately be forgiven by the SBA in accordance with the terms of the program. As of December 31, 2020, the Company had originated 4,269 PPP loans representing $319.4 million to its customers. Loans funded through the PPP program are guaranteed by the SBA and loans that meet certain regulatory criteria are subject to forgiveness. In the event that the PPP loans are not fully guaranteed by the SBA, the Company could be required to establish additional allowance for credit loss through additional credit loss expense charged to earnings. We started seeing forgiveness of the PPP loans in the fourth quarter of 2020 and continue to expect additional forgiveness in 2021.

Credit

The Company is working with customers directly affected by COVID-19 and is offering short-term assistance in accordance with regulatory guidelines. As a result of the economic environment caused by the COVID-19 virus, the Company is engaging in more frequent communication with borrowers to better understand their financial situation and the challenges they face, allowing it to respond proactively as needs and issues arise. It is possible that the Company's asset quality measures could worsen at future measurement periods if the effects of COVID-19 are prolonged.

We rely on third-party vendors to provide key components of our business infrastructure.

Third-party vendors provide key components of our business operations such as data processing, recording and monitoring transactions, online banking interfaces and services, Internet connections and network access. We have selected these third-party vendors carefully and have conducted the due diligence consistent with regulatory guidance and best practices. While we have ongoing programs to review third-party vendors and assess risk, we do not control their actions. Any problems caused by these third parties, including those resulting from disruptions in communication services provided by a vendor, failure of a vendor to handle current or higher volumes, cyber-attacks and security breaches at a vendor, failure of a vendor to provide services for any reason or poor performance of services, could adversely affect our ability to deliver products and services to our customers and otherwise conduct our business. Financial or operational difficulties of a third-party vendor could also hurt our operations if those difficulties interfere with the vendor's ability to serve us. Furthermore, our vendors could also be sources of operational and information security risk to us, including from breakdowns or failures of their own systems or capacity constraints. Replacing these third-party vendors could also create significant delay and expense. Accordingly, use of such third parties creates an unavoidable inherent risk to our business operations.

We face significant cyber and data security risk that could result in the disclosure of confidential information, adversely affect our business or reputation and expose us to significant liabilities.

As a financial institution, we are under threat of loss due to hacking and cyber-attacks. This risk has increased in recent years, and continues to increase, as we continue to expand customer capabilities to utilize internet and other remote channels to transact business. Two of the most significant cyber-attack risks that we face are e-fraud and loss of sensitive customer data. Loss from e-fraud occurs when cybercriminals breach and extract funds directly from customer or our accounts. The attempts to breach sensitive customer data, such as account numbers and social security numbers, are less frequent but would present significant reputational, legal and/or regulatory costs to us if successful. Our risk and

exposure to these matters remains heightened because of the evolving nature and complexity of these threats from cybercriminals and hackers, our plans to continue to provide internet banking and mobile banking channels, and our plans to develop additional remote connectivity solutions to serve our customers. While we have not experienced any material losses relating to cyber-attacks or other information security breaches since 2017, we have been subject of hacking and cyber-attack and there can be no assurance that we will not suffer additional losses in the future.

In response to the COVID-19 pandemic, we have modified our business practices with a portion of our employees working remotely from their homes to have our operations uninterrupted as much as possible. Further, technology in employees' homes may not be as robust as in our offices and could cause the networks, information systems, applications, and other tools available to employees to be more limited or less reliable than in our offices. The continuation of these work-from-home measures also introduces additional operational risk, including increased cybersecurity risk. These cyber risks include greater phishing, malware, and other cybersecurity attacks, vulnerability to disruptions of our information technology infrastructure and telecommunications systems for remote operations, increased risk of unauthorized dissemination of confidential information, limited ability to restore the systems in the event of a systems failure or interruption, greater risk of a security breach resulting in destruction or misuse of valuable information, and potential impairment of our ability to perform critical functions, including wiring funds, all of which could expose us to risks of data or financial loss, litigation and liability and could seriously disrupt our operations and the operations of any impacted customers.

The occurrence of any cyber-attack or information security breach could result in material adverse consequences to us including damage to our reputation and the loss of customers. We also could face litigation or additional regulatory scrutiny. Litigation or regulatory actions in turn could lead to significant liability or other sanctions, including fines and penalties or reimbursement of customers adversely affected by security breach. Even if we do not suffer any material adverse consequences as a result of other future events, successful attacks or systems failures at the Bank or at other financial institutions could lead to a general loss of customer confidence in financial institutions including the Bank.

Our ability to mitigate the adverse consequences of occurrences is in part dependent on the quality of our information security procedures and contracts and our ability to anticipate the timing and nature of any such event that occurs. In recent years, we have incurred significant expense towards improving the reliability of our systems and their security from attack. Nonetheless, there remains the risk that we may be materially harmed by cyber-attack and information security breach or others in the future. Methods used to attack information systems change frequently (with generally increasing sophistication), often are not recognized until launched against a target, may be supported by foreign governments or other well-financed entities, and may originate from less regulated and remote areas around the world. As a result, we may be unable to address these methods in advance of attacks, including by implementing adequate preventive measures. If such an attack or breach does occur, we might not be able to fix it timely or adequately. To the extent that such an attack or breach relates to products or services provided by others, we seek to engage in due diligence and monitoring to limit the risk. In addition, as the regulatory environment related to information security, data collection and use, and privacy becomes increasingly rigorous, with new and constantly changing requirements applicable to our business, compliance with those requirements could also result in additional costs.

We are dependent on key personnel and the loss of one or more of those key personnel could impair our relationship with our customers and adversely affect our business.

Many community banks attract customers based on the personal relationships that the banks' officers and customers establish with each other and the confidence that the customers have in the officers. We significantly depend on the continued service and performance of our key management personnel. We also believe our management team's depth and breadth of experience in the banking industry is integral to executing our business plan. The loss of the services of members of our senior management team or other key employees or the inability to attract additional qualified personnel as needed could have a material adverse effect on our business.

Credit Risks

We are subject to risks related to our concentration of construction and land development and commercial real estate loans.

As of December 31, 2020, we had $103.3 million of construction and land development loans. Construction and land development loans are subject to risks during the construction phase that are not present in standard residential real estate and commercial real estate loans. These risks include:

- the viability of the contractor;
- the contractor's ability to successfully complete the project, to meet deadlines and time schedules and to stay within cost estimates; and
- concentrations of such loans with a single contractor and its affiliates.

Real estate construction and land development loans may involve the disbursement of substantial funds with repayment dependent, in part, on the success of the ultimate project rather than the ability of a borrower or guarantor to repay the loan and also present risks of default in the event of declines in property values or volatility in the real estate market during the construction phase. Our practice, in the majority of instances, is to secure the personal guaranty of individuals in support of our real estate construction and land development loans which provides us with an additional source of repayment. As of December 31, 2020, we did not have any nonperforming construction and land development loans and had $1.2 million of assets that have been foreclosed. If one or more of our larger borrowers were to default on their construction and land development loans, and we did not have alternative sources of repayment through personal guarantees or other sources, or if any of the aforementioned risks were to occur, we could incur significant losses.

As of December 31, 2020, we had $1.15 billion of commercial real estate loans, including multi-family residential loans and loans secured by farmland. Commercial real estate lending typically involves higher loan principal amounts and the repayment is dependent, in large part, on sufficient income from the properties securing the loan to cover operating expenses and debt service.

A significant amount of our loans are secured by real estate and any declines in real estate values in our primary markets could be detrimental to our financial condition and results of operations.

Real estate lending (including commercial, construction, land development, and residential loans) is a large portion of our loan portfolio, constituting $1.91 billion, or approximately 78.0% of our total loan portfolio, as of December 31, 2020. Although residential and commercial real estate values are strong in our market area, such values may not remain elevated. If loans that are collateralized by real estate become troubled during a time when market conditions are declining or have declined, then we may not be able to realize the full value of the collateral that we anticipated at the time of originating the loan, which could require us to increase our provision for credit losses and adversely affect our financial condition and results of operations.

As of December 31, 2020, $648.9 million, or approximately 26.5% of our total loans, were secured by single-family residential real estate. This includes $557.3 million in residential 1-4 family loans and $91.6 million in home equity lines of credit. If housing prices in our market areas do not remain strong or deteriorate, we may experience an increase in nonperforming loans, provision for credit losses and charge-offs.

If the value of real estate in our market areas were to decline materially, a significant portion of our loan portfolio could become under-collateralized, which could have a material adverse effect on our asset quality, capital structure and profitability.

As of December 31, 2020, 47.2% of our loan portfolio was comprised of loans secured by commercial real estate, including multi-family residential loans and loans secured by farmland. In the majority of these loans, real estate was the primary collateral component. In some cases we take real estate as security for a loan even when it is not the primary component of collateral. The real estate collateral that provides the primary or an alternate source of repayment in the event of default may deteriorate in value during the term of the loan as a result of changes in economic conditions,

fluctuations in interest rates and the availability of loans to potential purchasers, changes in tax and other laws and acts of nature. If we are required to liquidate the collateral securing a loan to satisfy the debt during a period of reduced real estate values, our earnings and capital could be adversely affected. We are subject to increased lending risks in the form of loan defaults as a result of the high concentration of real estate lending in our loan portfolio. A weak real estate market in our primary market areas could have an adverse effect on the demand for new loans, the ability of borrowers to repay outstanding loans, the value of real estate and other collateral securing the loans and the value of real estate owned by us. If real estate values decline, it is also more likely that we would be required to increase our allowance for credit losses, which could adversely affect our financial condition and results of operations.

If our nonperforming assets increase, our earnings will suffer.

At December 31, 2020, our nonperforming assets (which consist of nonaccrual loans, loans past due 90 days and accruing and OREO) totaled $17.5 million, or 0.72% of total loans and OREO, which is an increase of $2.4 million, or 16.0%, compared with non-covered nonperforming assets (which consist of non-covered nonaccrual loans, loans past due 90 days and accruing and OREO), which totaled $15.1 million, or 0.69% of total non-covered loans and OREO at December 31, 2019. At December 31, 2018, our non-covered nonperforming assets were $11.8 million, or 0.54% of total non-covered loans and OREO.

Economic and market conditions are unstable, and our nonperforming assets as a percentage of total loans and OREO has improved, we may incur losses if there is a continued increase in nonperforming assets in the future. Our nonperforming assets adversely affect our net income in various ways. We do not record interest income on nonaccrual loans or OREO, thereby adversely affecting our net interest income, and increasing loan administration costs. When we take collateral in foreclosures and similar proceedings, we are required to mark the related loan to the then fair value of the collateral, which may ultimately result in a loss. We must reserve for probable losses, which is established through a current period charge to the provision for credit losses as well as from time to time, as appropriate, a write down of the value of properties in our OREO portfolio to reflect changing market values. Additionally, there are legal fees associated with the resolution of problem assets as well as carrying costs such as taxes, insurance and maintenance related to our OREO. Further, the resolution of nonperforming assets requires the active involvement of management, which can distract them from more profitable activity. Finally, an increase in the level of nonperforming assets increases our regulatory risk profile. There can be no assurance that we will not experience future increases in nonperforming assets.

If our allowance for credit losses is not adequate to cover actual loan losses, our earnings will decrease.

As a lender, we are exposed to the risk that our borrowers may not repay their loans according to the terms of these loans, and the collateral securing the payment of these loans may be insufficient to ensure repayment. We make various assumptions and judgments about the collectability of our loan portfolio, including the creditworthiness of the borrowers and the value of the real estate and other assets serving as collateral for the repayment of many of our loans. The amount of the allowance represents management's best estimate of current expected credit losses on loans considering available information, from internal and external sources, relevant to assessing collectability over the loans' contractual terms, adjusted for expected prepayments when appropriate. If our assumptions prove to be incorrect or if we experience significant loan losses, our current allowance may not be sufficient to cover actual loan losses and adjustments may be necessary to allow for different economic conditions or adverse developments in our loan portfolio. A material addition to the allowance for credit losses could cause our earnings to decrease. Due to the relatively unseasoned nature of our loan portfolio, we may experience an increase in delinquencies and losses as these loans continue to mature.

In addition, federal regulators periodically review our allowance for credit losses and may require us to increase our provision for credit losses or recognize further charge-offs, based on judgments different than those of our management. Any significant increase in our allowance for credit losses or charge-offs required by these regulatory agencies could have a material adverse effect on our results of operations and financial condition.

The small to medium-sized businesses we lend to may have fewer resources to weather a downturn in the economy, which may impair a borrower's ability to repay a loan to us that could materially harm our operating results.

We make loans to professional firms and privately owned businesses that are considered to be small to medium-sized businesses. Small to medium-sized businesses frequently have smaller market shares than their competition, may be more vulnerable to economic downturns, often need substantial additional capital to expand or compete and may experience substantial volatility in operating results, any of which may impair a borrower's ability to repay a loan. In addition, the success of a small and medium-sized business often depends on the management talents and efforts of one or two persons or a small group of persons, and the death, disability or resignation of one or more of these persons could have a material adverse impact on the business and its ability to repay our loan. Economic downturns in our target markets could cause us to incur substantial loan losses that could materially harm our operating results.

We are subject to credit quality risks and our credit policies may not be sufficient to avoid losses.

We are subject to the risk of losses resulting from the failure of borrowers, guarantors and related parties to pay interest and principal amounts on their loans. Although we maintain credit policies and credit underwriting, monitoring and collection procedures, these policies and procedures may not prevent losses, particularly during periods in which the local, regional or national economy suffers a general decline. If borrowers fail to repay their loans, our financial condition and results of operations would be adversely affected.

Market Risks

Our profitability depends significantly on local economic conditions in the areas where our operations and loans are concentrated, and our geographic concentration makes us vulnerable to local weather catastrophes, public health issues, and other external events, which could adversely affect our results of operations and financial condition.

We operate in a mixed market environment with influences from both rural and urban areas. Our profitability depends on the general economic conditions in our market areas of Northern Virginia, Maryland, Washington, D.C., Charlottesville and Clifton Forge (Alleghany County), Front Royal, New Market, Northern Neck, Middle Peninsula, Richmond, Hampton Roads and the surrounding areas. Unlike larger banks that are more geographically diversified, we provide banking and financial services to clients primarily in these market areas. As of December 31, 2020, substantially all of our commercial real estate, real estate construction and residential real estate loans were made to borrowers in our market area. The local economic conditions in this area have a significant impact on our commercial, real estate and construction and consumer loans, the ability of the borrowers to repay these loans and the value of the collateral securing these loans. In addition, if the population or income growth in these market areas slows, stops or declines, income levels, deposits and housing starts could be adversely affected and could result in the curtailment of our expansion, growth and profitability.

Additionally, political conditions could impact our earnings. For example, political debate over the budget, taxes and the potential for reduced government spending may adversely impact the economy, and more specifically local economic conditions given the concentration of Federal workers and government contractors in our market. Further, the occurrence of events such as hurricanes, tropical storms, tornados, winter storms, freezes, flooding and other large-scale weather catastrophes in and along the Atlantic coast, and further public health issues, such as pandemics or other widespread health emergencies, could adversely affect our financial condition or results of operations. Such areas could be adversely impacted by such events in those regions, the nature and severity of which are difficult to predict. Furthermore, climate change could increase the frequency and severity of these risks. These and other unpredictable external events could have an adverse effect on us in that such events could materially disrupt our operations or the ability or willingness of its customers to access the financial services offered by the Company. These events could reduce our earnings and cause volatility in our financial results for any fiscal quarter or year and have a material adverse effect on our financial condition and/or results of operations.

Our business is subject to interest rate risk and variations in interest rates may negatively affect our financial performance.

The majority of our assets and liabilities are monetary in nature and subject us to significant risk from changes in interest rates. Fluctuations in interest rates are not predictable or controllable. Like most financial institutions, changes in interest rates can impact our net interest income as well as the valuation of our assets and liabilities, which is the difference between interest earned from interest-earning assets, such as loans and investment securities, and interest paid on interest-bearing liabilities, such as deposits and borrowings. We expect that we will periodically experience "gaps" in the interest rate sensitivities of our assets and liabilities, meaning that either our interest-bearing liabilities will be more sensitive to changes in market interest rates than our interest-earning assets, or vice versa. In either event, if market interest rates should move contrary to our position, this "gap" will negatively impact our earnings. Many factors impact interest rates, including governmental monetary policies, inflation, recession, changes in unemployment, the money supply, and international disorder and instability in domestic and foreign financial markets.

Based on our analysis of the interest rate sensitivity of our assets, an increase in the general level of interest rates may negatively affect the market value of the portfolio equity, but will positively affect our net interest income since most of our assets have floating rates of interest that adjust fairly quickly to changes in market rates of interest. Additionally, an increase in interest rates may, among other things, reduce the demand for loans and our ability to originate loans. A decrease in the general level of interest rates may affect us through, among other things, increased prepayments on our loan and mortgage-backed securities portfolios and increased competition for deposits. Accordingly, changes in the level of market interest rates affect our net yield on interest-earning assets, loan origination volume, loan and mortgage-backed securities portfolios, and our overall results. Although our asset liability management strategy is designed to control our risk from changes in market interest rates, it may not be able to prevent changes in interest rates from having a material adverse effect on our results of operations and financial condition.

Declines in asset values may result in impairment charges and adversely affect the value of our investment securities, financial performance and capital.

We maintain an investment securities portfolio that includes, but is not limited to, collateralized mortgage obligations, agency mortgage-backed securities and pooled trust preferred securities. The market value of investment securities may be affected by factors other than the underlying performance of the issuer or composition of the bonds themselves, such as ratings downgrades, adverse changes in the business climate and a lack of liquidity for resales of certain investment securities. At each reporting period, we evaluate investment securities and other assets for impairment indicators. We may be required to record additional impairment charges if our investment securities suffer a decline in value that is considered other-than-temporary. During the years ended December 31, 2020, 2019 and 2018, we incurred no other-than-temporary impairment charges related to credit losses or sales of securities. If in future periods we determine that a significant impairment has occurred, we would be required to charge against earnings the credit-related portion of the other-than-temporary impairment, which could have a material adverse effect on our results of operations in the periods in which the write-offs occur.

Our stock price can be volatile.

Stock price volatility may make it more difficult for you to resell your common stock when you want and at prices you find attractive. Our stock price can fluctuate significantly in response to a variety of factors including, among other things:

- actual or anticipated variations in quarterly results of operations;
- recommendations by securities analysts;
- operating and stock price performance of other companies that investors deem comparable to us;
- news reports relating to trends, concerns and other issues in the financial services industry;
- perceptions in the marketplace regarding us and/or our competitors;
- new technology used, or services offered, by competitors;
- significant acquisitions or business combinations, strategic partnerships, joint ventures or capital commitments by or involving us or our competitors;

- failure to integrate acquisitions or realize anticipated benefits from acquisitions;
- changes in valuations of Goodwill and other Intangible Assets;
- changes in government regulations; and
- geopolitical conditions such as acts or threats of terrorism, military conflicts or pandemics.

General market fluctuations, industry factors and general economic and political conditions and events, such as economic slowdowns or recessions, interest rate changes or credit loss trends, could also cause our stock price to decrease regardless of operating results.

The trading volume in our common stock is less than that of other larger financial services companies.

Although our common stock is listed for trading on the NASDAQ Global Market, the trading volume is low, and you are not assured liquidity with respect to transactions in our common stock. A public trading market having the desired characteristics of depth, liquidity and orderliness depends on the presence in the marketplace of willing buyers and sellers of our common stock at any given time. This presence depends on the individual decisions of investors and general economic and market conditions over which we have no control. Given the lower trading volume of our common stock, significant sales of our common stock, or the expectation of these sales, could cause our stock price to fall.

Liquidity Risks

Liquidity risk could impair our ability to fund operations and jeopardize our financial condition, results of operations and cash flows.

Liquidity is essential to our business. Our ability to implement our business strategy will depend on our ability to obtain funding for loan originations, working capital, possible acquisitions and other general corporate purposes. An inability to raise funds through deposits, borrowings, securities sold under agreements to repurchase, the sale of loans and other sources could have a substantial negative effect on our liquidity. We do not anticipate that our retail and commercial deposits will be sufficient to meet our funding needs in the foreseeable future. We therefore rely on deposits obtained through intermediaries, FHLB advances, and other wholesale funding sources to obtain the funds necessary to implement our growth strategy.

Our access to funding sources in amounts adequate to finance our activities or on terms which are acceptable to us could be impaired by factors that affect us specifically or the financial services industry or economy in general, including a decrease in the level of our business activity as a result of a downturn in the markets in which our loans are concentrated or adverse regulatory action against us. Our ability to borrow could also be impaired by factors that are not specific to us, such as a disruption in the financial markets or negative views and expectations about the prospects for the financial services industry. To the extent we are not successful in obtaining such funding, we will be unable to implement our strategy as planned which could have a material adverse effect on our financial condition, results of operations and cash flows.

Capital Adequacy Risks

Future growth or operating results may require us to raise additional capital, but that capital may not be available, be available on unfavorable terms or may be dilutive.

Sonabank is required by the FRB to maintain adequate levels of capital to support our operations. In the event that our future operating results erode capital, if the Bank is required to maintain capital in excess of well-capitalized standards, or if we elect to expand through loan growth or acquisitions, we may be required to raise additional capital. Our ability to raise capital will depend on conditions in the capital markets, which are outside our control, and on our

financial performance. Accordingly, we cannot be assured of our ability to raise capital on favorable terms when needed, or at all. If we cannot raise additional capital when needed, we will be subject to increased regulatory supervision and the imposition of restrictions on our growth and business. These outcomes could negatively impact our ability to operate or further expand our operations through acquisitions or the establishment of additional branches and may result in increases in operating expenses and reductions in revenues that could have a material adverse effect on our financial condition and results of operations. In addition, in order to raise additional capital, we may need to issue shares of our common stock that would dilute the book value of our common stock and reduce our current shareholders' percentage ownership interest to the extent they do not participate in future offerings.

We may issue a new series of preferred stock or debt securities, which would be senior to our common stock and may cause the market price of our common stock to decline.

We have issued $27.0 million in aggregate principal amount of 5.875% Fixed-to-Floating Rate Subordinated Notes due January 31, 2027 and $60.0 million of fixed-to-floating rate Subordinated Notes due 2030. In the future, we may increase our capital resources by making additional offerings of debt or equity securities, which may include senior or additional subordinated notes, classes of preferred shares and/or common shares. Holders of our common stock are not entitled to preemptive rights or other protections against dilution. Preferred shares and debt, if issued, have a preference on liquidating distributions or a preference on dividend or interest payments that could limit our ability to make a distribution to the holders of our common stock. Future issuances and sales of parity preferred stock, or the perception that such issuances and sales could occur, may also cause prevailing market price for our common stock to decline and may adversely affect our ability to raise additional capital in the financial markets at times and prices favorable to us. Further issuances of our common stock could be dilutive to holders of our common stock.

We currently intend to pay dividends on our common stock; however, our future ability to pay dividends is subject to restrictions.

We declared the first cash dividend on our common stock in February 2012, and each quarter thereafter through 2019. There are a number of restrictions on our ability to pay dividends. It is the policy of the FRB that bank holding companies should pay cash dividends on common stock only out of income available over the past year and only if prospective earnings retention is consistent with the organization's expected future needs and financial condition. The policy provides that bank holding companies should not maintain a level of cash dividends that undermines the bank holding company's ability to serve as a source of strength to its banking subsidiaries.

Our principal source of funds to pay dividends on our common stock is cash dividends that we receive from the Bank. The payment of dividends by the Bank to us is subject to certain restrictions imposed by federal banking laws, regulations and authorities. The federal banking statutes prohibit federally insured banks from making any capital distributions (including a dividend payment) if, after making the distribution, the institution would be "under capitalized" as defined by statute. In addition, the relevant federal regulatory agencies have authority to prohibit an insured bank from engaging in an unsafe or unsound practice, as determined by the agency, in conducting an activity. The payment of dividends could be deemed to constitute such an unsafe or unsound practice, depending on the financial condition of the Bank. Regulatory authorities could impose administratively stricter limitations on the ability of the Bank to pay dividends to us if such limits were deemed appropriate to preserve certain capital adequacy requirements.

Regulatory Risks

We are heavily regulated by federal and state agencies; changes in laws and regulations or failures to comply with such laws and regulations may adversely affect our operations and our financial results.

We and the Bank are subject to extensive regulation, supervision and examination by federal and state banking authorities. Any change in applicable regulations or federal or state legislation could have a substantial impact on us and the Bank, and our respective operations. Additional legislation and regulations may be enacted or adopted in the future

that could significantly affect our powers, authority and operations or the powers, authority and operations of the Bank, which could have a material adverse effect on our financial condition and results of operations.

Further, bank regulatory authorities have the authority to bring enforcement actions against banks and their holding companies for unsafe or unsound practices in the conduct of their businesses or for violations of any law, rule or regulation, any condition imposed in writing by the appropriate bank regulatory agency or any written agreement with the agency. Possible enforcement actions against us could include the issuance of a cease-and-desist order that could be judicially enforced, the imposition of civil monetary penalties, the issuance of directives to increase capital or enter into a strategic transaction, whether by merger or otherwise, with a third party, the appointment of a conservator or receiver, the termination of insurance on deposits, the issuance of removal and prohibition orders against institution-affiliated parties, and the enforcement of such actions through injunctions or restraining orders. The exercise of this regulatory discretion and power may have a negative impact on us.

As a regulated entity, Sonabank must maintain certain required levels of regulatory capital that may limit our operations and potential growth.

As further described above under Supervision and Regulation—Capital Requirements, Southern National and the Bank each are subject to various regulatory capital requirements administered by the FRB.

Failure to meet minimum capital requirements can initiate certain mandatory, and possibly additional, discretionary actions by regulators that, if undertaken, could have a direct material effect on the Bank's and our consolidated financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of the Bank's assets, liabilities and certain off-balance sheet commitments as calculated under these regulations.

As of December 31, 2020, Southern National and the Bank exceeded the amounts required to be well capitalized with respect to all four required capital ratios. As of December 31, 2020, Southern National's leverage, CET1 risk-based capital, Tier 1 risk-based capital and Total risk-based capital ratios were 9.69%, 13.05%, 13.52% and 19.58%, respectively. As of December 31, 2020, the Bank's leverage, CET1 risk-based capital, Tier 1 risk-based capital and Total risk-based capital ratios were 11.25%, 15.83%, 15.83% and 17.09%, respectively.

Many factors affect the calculation of Southern National and the Bank's risk-based assets and its ability to maintain the level of capital required to achieve acceptable capital ratios. For example, changes in risk weightings of assets relative to capital and other factors may combine to increase the amount of risk-weighted assets in the Tier 1 risk-based capital ratio and the Total risk-based capital ratio. Any increases in its risk-weighted assets will require a corresponding increase in its capital to maintain the applicable ratios. In addition, recognized loan losses in excess of amounts reserved for such losses, loan impairments, impairment losses on investment securities and other factors will decrease the Bank's capital, thereby reducing the level of the applicable ratios.

Southern National and the Bank's failure to remain well capitalized for bank regulatory purposes could affect customer confidence, our ability to grow, our costs of funds and FDIC insurance costs, our ability to pay dividends on our capital stock, our ability to make acquisitions, and on our business, results of operations and financial condition. Under FRB rules, if the Bank ceases to be a well-capitalized institution for bank regulatory purposes, the interest rates that it pays on deposits and its ability to accept, renew or rollover brokered deposits may be restricted. As of December 31, 2020, we had $270 thousand of brokered deposits, which represented 0.01% of our total deposits.

Financial Reporting Risks

Failure to maintain an effective system of disclosure controls and procedures could have a material adverse effect on our business, results of operations and financial condition and could impact the price of our common stock.

Failure to maintain an effective internal control environment could result in us not being able to accurately report our financial results, prevent or detect fraud, or provide timely and reliable financial information pursuant to our reporting obligations, which could have a material adverse effect on our business, financial condition, and results of operations. Further, it could cause our investors to lose confidence in the financial information we report, which could affect the trading price of our common stock.

Management regularly reviews and updates our disclosure controls and procedures, including our internal control over financial reporting. Any system of controls, however well designed and operated, is based in part on certain assumptions and can provide only reasonable, not absolute, assurances that the objectives of the system are met. Any failure or circumvention of our controls and procedures or failure to comply with regulations related to controls and procedures could have a material adverse effect on our business, results of operations and financial condition.

Item 1B. Unresolved Staff Comments

Southern National does not have any unresolved staff comments from the SEC to report for the year ended December 31, 2020.

Item 2. Properties

Southern National's principal office is located at 6830 Old Dominion Drive, McLean, Virginia. Southern National and Sonabank also have executive offices located at 1002 Wisconsin Avenue, N.W., Washington, DC and 10900 Nuckols Road, Suite 325, Glen Allen, Virginia. Including these main locations, our bank owns 32 properties and leases 25 properties, all of which are used as branch locations or for housing operational units in Maryland and Virginia. At December 31, 2020, Sonabank had forty-two full-service branches in Virginia and Maryland and also provides services to customers through certain internet and mobile applications. Thirty-seven full-service retail branches are in Virginia (Ashland, Burgess, Callao, Central Garage, Charlottesville, Chester, Clifton Forge, Colonial Heights, Courtland, Deltaville, Fairfax, Front Royal, Gloucester, Gloucester Point, Hampton, Hartfield, Heathsville, Kilmarnock, Leesburg, McLean, Mechanicsville (2), Middleburg, Midlothian, New Market, Newport News, Quinton, Reston, Richmond, South Riding, Surry, Tappahannock (2), Urbanna, Warrenton, Waverly, and Williamsburg) and five full-service retail branches are in Maryland (Bethesda, Brandywine, Owings, Rockville, and Upper Marlboro). We have administrative offices in Warrenton and Glen Allen, Virginia. Our South Riding branch will be closing effective April 15, 2021.

Southern National believes its facilities are in good operating condition, are suitable and adequate for its operational needs and are adequately insured.

Item 3. Legal Proceedings

Southern National and Sonabank are from time to time a party, as both plaintiff and defendant, to various claims and proceedings arising in the ordinary course of the Bank's business, including administrative and/or legal proceedings that may include employment-related claims, as well as claims of lender liability, breach of contract, and other similar lending-related claims. While the ultimate resolution of these matters cannot be determined at this time, the Bank's management presently believes that such matters, individually and in the aggregate, will not have a material adverse effect on the Bank's financial condition or results of operations.

Item 4. Mine Safety Disclosures.

Not applicable.

PART II

Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

Common Stock Market Prices

Southern National's common stock is traded on the Nasdaq Global Market under the symbol "SONA". There were 24,438,545 shares of our common stock outstanding at the close of business on March 5, 2021, which were held by 1,347 shareholders of record. As of that date, the closing price of our common stock on the NASDAQ Global Market was $15.75.

Recent Sales of Unregistered Securities

None.

Securities Authorized for Issuance under Equity Compensation Plans

As of December 31, 2020, Southern National had outstanding stock options granted under the 2010 Stock Awards and Incentive Plan (the "2010 Plan") and the 2017 Equity Compensation Plan (the "2017 Plan"), which were approved by its shareholders. The following table provides information as of December 31, 2020 regarding Southern National's equity compensation plans under which our equity securities are authorized for issuance:

Plan category	Number of securities to be issued upon exercise of outstanding options A	Weighted average exercise price of outstanding options 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	450,800	$ 10.50	552,800
Equity compensation plans not approved by security holders	—	—	—
Total	450,800	$ 10.50	552,800

Issuer Purchases of Equity Securities

None.

Dividends

We declared the first cash dividend on our common stock in February 2012, and each quarter thereafter through 2020. There are a number of restrictions on our ability to pay dividends. It is the policy of the FRB that bank holding companies should pay cash dividends on common stock only out of income available over the past year and only if prospective earnings retention is consistent with the organization's expected future needs and financial condition. The policy provides that bank holding companies should not maintain a level of cash dividends that undermines the bank holding company's ability to serve as a source of strength to its banking subsidiaries. Banking regulations require maintaining certain capital levels and may limit the dividends paid by the Bank to Southern National or by Southern National to shareholders. The Company's ability to pay dividends to stockholders is largely dependent upon the dividends it receives from the Bank, and the Bank is subject to regulatory limitations on the amount of cash dividends it may pay.

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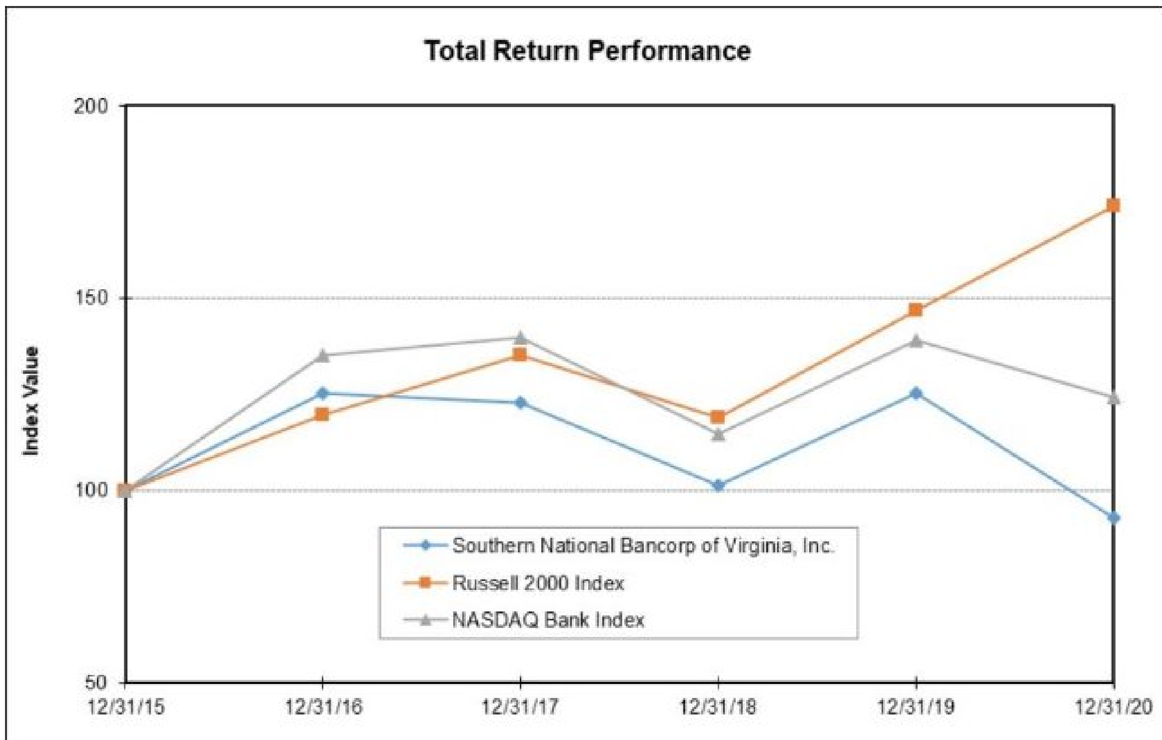
Performance Graph

The following chart compares the cumulative total shareholder return on Southern National common stock during the five years ended December 31, 2020, with the cumulative total return of the Russell 2000 Index and the NASDAQ Bank Index for the same period. Dividend reinvestment has been assumed. This comparison assumes $100 invested on December 31, 2015 in Southern National common stock, the Russell 2000 Index and the NASDAQ Bank Index. The historical stock price performance for Southern National common stock shown on the graph below is not necessarily indicative of future stock performance.



	2015	2016	2017	2018	2019	2020
Southern National Bancorp of Virginia, Inc.	100.00	125.11	122.74	101.23	125.19	92.73
Russell 2000 Index	100.00	119.48	135.18	118.72	146.89	173.86
NASDAQ Bank Index	100.00	135.02	139.77	114.74	139.10	124.31

Item 6. Selected Financial Data

The following table sets forth selected financial data for Southern National as of and for the years ended December 31, 2020, 2019, 2018, 2017, and 2016:

	2020	2019	2018	2017	2016
		(in thousands, except per share amounts)			
Results of Operations:					
Interest income	$ 117,779	$ 120,524	$ 118,907	$ 83,570	$ 48,947
Interest expense	26,139	36,924	27,841	15,653	8,633
Net interest income	91,640	83,600	91,066	67,917	40,314
Provision for credit losses	19,450	350	4,200	8,625	4,912
Net interest income after provision for credit losses	72,190	83,250	86,866	59,292	35,402
Noninterest income	25,451	12,586	10,199	5,429	2,820
Noninterest expenses	67,740	56,592	53,760	49,149	22,815
Income before income taxes	29,901	39,244	43,305	15,572	15,407
Income tax expense	6,614	6,077	9,614	13,147	5,095
Net income	$ 23,287	$ 33,167	$ 33,691	$ 2,425	$ 10,312
Per Share Data:					
Earnings per share - Basic	$ 0.96	$ 1.38	$ 1.40	$ 0.13	$ 0.84
Earnings per share - Diluted	$ 0.96	$ 1.36	$ 1.39	$ 0.13	$ 0.83
Cash dividends paid per share	$ 0.40	$ 0.36	$ 0.32	$ 0.32	$ 0.32
Book value per share	$ 16.03	$ 15.60	$ 14.48	$ 13.48	$ 10.30
Dividend payout ratio	41.64 %	26.09 %	22.86 %	246.15 %	38.10 %
Weighted average shares outstanding - Basic	24,239,481	24,050,037	24,012,437	18,390,810	12,251,804
Weighted average shares outstanding - Diluted	24,362,665	24,325,182	24,272,617	18,671,392	12,426,783
Shares issued and outstanding at end of period	24,368,612	24,181,534	24,052,253	23,936,453	12,263,643
Selected Performance Ratios and Other Data:					
Return on average assets	0.78 %	1.22 %	1.25 %	0.13 %	0.95 %
Return on average equity	6.04 %	9.13 %	9.99 %	1.02 %	8.37 %
Yield on earning assets	4.31 %	4.88 %	4.86 %	4.76 %	4.84 %
Cost of funds	1.01 %	1.58 %	1.19 %	0.94 %	0.91 %
Net interest margin	3.35 %	3.39 %	3.72 %	3.87 %	3.99 %
Net charge-offs to average loans	0.07 %	0.11 %	0.06 %	0.51 %	0.53 %
Allowance for credit losses to total loans [(1)]	1.49 %	0.47 %	0.57 %	0.46 %	0.95 %
Stockholders' equity to total assets	12.64 %	13.86 %	12.89 %	12.35 %	11.06 %
Financial Condition:					
Total assets	$ 3,088,673	$ 2,722,170	$ 2,701,295	$ 2,614,252	$ 1,142,443
Total loans	2,440,496	2,186,047	2,178,824	2,062,328	930,415
Total deposits	2,432,606	2,124,718	2,097,600	1,865,156	912,982
Stockholders' equity	390,554	377,241	348,290	322,772	126,344

(1) Included non-covered loans for the years ended December 31, 2019, 2018, 2017, and 2016.

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

Item 7 of our Annual Report on Form 10-K generally discusses year-to-year comparisons between the years ended December 31, 2020 and 2019. Discussions of comparisons between 2019 and 2018 are not included in this Form10-K but can be found in "Item 7—Management's Discussion and Analysis of Financial Condition and Results of Operations" in our Annual Report on Form10-K for the year ended December 31, 2019.

Management's discussion and analysis is presented to aid the reader in understanding and evaluating the financial condition and results of operations of Southern National. This discussion and analysis should be read with the consolidated financial statements, the footnotes thereto, and the other financial data included in this report.

COVID-19 PANDEMIC

In March 2020, the World Health Organization declared COVID-19 as a global pandemic. This public health crisis has resulted in unprecedented uncertainty, volatility and disruption in financial markets and in governmental, commercial and consumer activity in the United States and globally, including the markets that we serve. In response to the crisis, the Board of Governors of the Federal Reserve reduced benchmark federal fund interest rates to near zero. In addition, in March 2020, the CARES Act was enacted. The CARES Act contains substantial tax and spending provisions intended to address the financial impact of the COVID-19 pandemic.

The COVID-19 pandemic has resulted in significant health, economic and other major consequences throughout the communities the Company serves, as well as nationally and globally. The Company has implemented a number of procedures in response to the pandemic to support the safety and well-being of our employees, customers and shareholders that continue through the date of this report:

- We have addressed the safety of our branches and while the branches generally remain open to customers, we have taken steps, and continue to evaluate ways, to encourage transactions through our drive-thru facilities;
- At the onset of the pandemic, we pro-actively conducted outreach to commercial loan customers to understand the potential impact that COVID-19 could have on their business. We implemented deferral arrangements in accordance with the CARES Act and bank regulatory guidance. To help mitigate the effects of COVID-19, loan customers could apply for a deferral of payments, or portions thereof, for up to 90 days. After 90 days, customers could apply for an additional deferral, and a small proportion of our customers requested such an additional deferral. The majority of our deferrals have resumed payment. At December 31, 2020, there were 44 loans in COVID-19 related deferment with an aggregate outstanding balance of $122.0 million; and
- We have chosen to participate in the CARES Act Paycheck Protection Program that will provide government guaranteed and forgivable loans to our customers. As of December 31, 2020, the Company had funded approximately $319.4 million of SBA approved PPP loans to over 4,269 customers.

The Company continues to closely monitor the pandemic and expects to make future changes to respond to the pandemic as it evolves.

CRITICAL ACCOUNTING POLICIES

Our accounting policies are in accordance with U.S. GAAP and with general practices within the banking industry. Management makes a number of estimates and assumptions relating to reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during periods presented. Different assumptions in the application of these methods or policies could result in material changes in our financial statements. As such, the following policies are considered "critical accounting policies" for us.

Allowance for Credit Losses ("ACL")

The allowance for credit losses on loans is a contra-asset valuation account, calculated in accordance with ASC 326 that is deducted from the amortized cost basis of loans to present the net amount expected to be collected. The amount of the allowance represents management's best estimate of current expected credit losses on loans considering available information, from internal and external sources, relevant to assessing collectability over the loans' contractual terms, adjusted for expected prepayments when appropriate. The contractual term excludes expected extensions, renewals and modifications unless (i) management has a reasonable expectation that a trouble debt restructuring will be executed with an individual borrower or (ii) such extension or renewal options are not unconditionally cancellable by us and, in such cases, the borrower is likely to meet applicable conditions and likely to request extension or renewal. Relevant available information includes historical credit loss experience, current conditions and reasonable and supportable forecasts. While historical credit loss experience provides the basis for the estimation of expected credit losses, adjustments to historical loss information may be made for differences in current portfolio-specific risk characteristics, environmental conditions or other relevant factors. The allowance for credit losses is measured on a collective basis for portfolios of loans when similar risk characteristics exist. Loans that do not share risk characteristics are evaluated for expected credit losses on an individual basis and excluded from the collective evaluation. Expected credit losses for collateral dependent loans, including loans where the borrower is experiencing financial difficulty but foreclosure is not probable, are based on the fair value of the collateral at the reporting date, adjusted for selling costs as appropriate.

Credit loss expense related to loans reflects the totality of actions taken on all loans for a particular period including any necessary increases or decreases in the allowance related to changes in credit loss expectations associated with specific loans or pools of loans. Portions of the allowance may be allocated for specific credits; however, the entire allowance is available for any credit that, in management's judgment, should be charged off. While management utilizes its best judgment and information available, the ultimate appropriateness of the allowance is dependent upon a variety of factors beyond our control, including the performance of our loan portfolio, the economy, changes in interest rates and the view of the regulatory authorities toward loan classifications.

In calculating the allowance for credit losses, most loans are segmented into pools based upon similar characteristics and risk profiles. Common characteristics and risk profiles include the type/purpose of loan, underlying collateral, geographical similarity and historical/expected credit loss patterns. In developing these loan pools for the purposes of modeling expected credit losses, we also analyzed the degree of correlation in how loans within each portfolio respond when subjected to varying economic conditions and scenarios as well as other portfolio stress factors. For allowance modeling purposes, our loan pools include (i) commercial real estate - owner occupied, (ii) commercial real estate - non-owner occupied, (iii) construction and land development, (iv) commercial, (v) agricultural loans, (vi) residential 1-4 family and (vii) consumer loans. We periodically reassess each pool to ensure the loans within the pool continue to share similar characteristics and risk profiles and to determine whether further segmentation is necessary.

For each loan pool, we measure expected credit losses over the life of each loan utilizing a combination of inputs: (i) probability of default ("PD"), which is the likelihood that loan will stop performing/default, (ii) probability of attrition ("PA"), which is the likelihood that a loan will pay-off prior to maturity, (iii) loss given default ("LGD"), which is the expected loss rate for loans in default and (iv) exposure at default ("EAD"), which is the estimated outstanding principal balance of the loans upon default, including the expected funding of unfunded commitments outstanding as of the measurement date. Inputs are pool-specific, though not necessarily solely reliant on internally-sourced data. Internal data is supplemented by, but not replaced by, peer data when required, primarily to determine the PD input. The various pool-specific inputs may be adjusted for current macroeconomic assumptions, as further discussed below, and other factors such as differences in underwriting standards, portfolio mix, or when historical asset terms do not reflect the contractual terms of the financial assets being evaluated as of the measurement date. Each time we measure expected credit losses, we assess the relevancy of historical information and consider any necessary adjustments to address any differences in current asset-specific characteristics.

Significant macroeconomic variables utilized in our allowance models include, among other things, (i) VA Gross Domestic Product, (ii) VA House Price Index, and (iii) VA unemployment rates. The macroeconomic variables utilized as inputs in forecast modeling were subjected to a variety of analysis procedures and were selected primarily based on

statistical relevancy and correlation to historical credit losses, where historical credit losses may be fully internally-sourced or supplemented with peer data.

PDs were estimated by analyzing the relationship between the historical performance of each loan pool and historical economic trends over a complete economic cycle. Again, historical performance data is either fully internally-sourced or supplemented with peer data where necessary. PDs are adjusted to reflect the current impact of certain macroeconomic variables as well as their expected changes over a reasonable and supportable forecast period. We have determined that we are reasonably able to forecast the macroeconomic variables used in our forecast modeling processes with an acceptable degree of confidence for a total of four quarters. This forecast period is followed by an additional eight quarter reversion process whereby the forecasted macroeconomic variables are reverted to their historical mean on a straight-line basis. By reverting these economic inputs to their historical mean and considering loan/borrower specific attributes, our allowance models are intended to yield a measurement of expected credit losses that reflects average historical loss rates (which may be supplemented by peer data) for periods subsequent to the initial twelve-quarters consisting of the forecast and reversion periods. The LGD is linked to PD based on benchmark historical loss averages for each loan pool. That is, LGD is dynamic with PD; as PD increases, so will LGD, and vice versa. In this context, “benchmark” refers to the use of third-party data, and “historical loss averages” refers to the fraction of defaulted balance that tends to be lost. By nature of its connection to PD, LGD is by extension adjusted to reflect the current impact of certain macroeconomic variables as well as their expected changes over the four-quarter forecast period and eight-quarter reversion process, which management considers to be both reasonable and supportable. This same forecast/reversion period is used for all macroeconomic variables used in all of our economic forecast models. PA and EAD are estimated using either a Discounted Cash Flow or Remaining Life model, both of which use various timing inputs to estimate the loan balance that remains at various future points in time, and thus also at the time of a default event.

Management qualitatively adjusts allowance model results for risk factors that are not considered within our quantitative modeling processes but are nonetheless relevant in assessing the expected credit losses within our loan pools. These qualitative factor (“Q-Factor”) adjustments may increase or decrease management's estimate of expected credit losses by a calculated percentage or amount based upon the estimated level of risk. The various risks that may be considered in making Q-Factor adjustments include, among other things, the impact of (i) changes in lending policies and procedures, including changes in underwriting standards and practices for collections, write-offs, and recoveries, (ii) actual and expected changes in international, national, regional, and local economic and business conditions and developments that affect the collectability of the loan pools, (iii) changes in the nature and volume of the loan pools and in the terms of the underlying loans, (iv) changes in the experience, ability, and depth of our lending management and staff, (v) changes in volume and severity of past due financial assets, the volume of non-accrual assets, and the volume and severity of adversely classified or graded assets, (vi) changes in the quality of our credit review function, (vii) changes in the value of the underlying collateral for loans that are non-collateral dependent, (viii) the existence, growth, and effect of any concentrations of credit and (ix) other factors such as the regulatory, legal and technological environments; competition; and events such as natural disasters or health pandemics.

In some cases, management may determine that an individual loan exhibits unique risk characteristics which differentiate the loan from other loans within our loan pools. In such cases, the loans are evaluated for expected credit losses on an individual basis and excluded from the collective evaluation. Specific allocations of the allowance for credit losses are determined by analyzing the borrower’s ability to repay amounts owed, collateral deficiencies, the relative risk grade of the loan and economic conditions affecting the borrower’s industry, among other things. A loan is considered to be collateral dependent when, based upon management's assessment, the borrower is experiencing financial difficulty and repayment is expected to be provided substantially through the operation or sale of the collateral. In such cases, expected credit losses are based on the fair value of the collateral at the measurement date, adjusted for estimated selling costs if satisfaction of the loan depends on the sale of the collateral. We reevaluate the fair value of collateral supporting collateral dependent loans on a quarterly basis. The fair value of real estate collateral supporting collateral dependent loans is evaluated by our internal appraisal services using a methodology that is consistent with the Uniform Standards of Professional Appraisal Practice. The fair value of collateral supporting collateral dependent construction loans is based on an “as is” valuation.

Accounting for Acquired Loans

Southern National has purchased, primarily through acquisitions, individual loans and groups of loans, some of which have shown evidence of credit deterioration since origination. These purchased loans are recorded at fair value such that there is no carryover of the seller's allowance for credit losses. We adopted ASU 2016-13, Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments, on January 1, 2020 which now requires us to record purchased financial assets with credit deterioration (PCD assets), defined as a more-than-insignificant deterioration in credit quality since origination or issuance, at the purchase price plus the allowance for credit losses expected at the time of acquisition. Under this method, there is no credit loss expense affecting net income on acquisition of PCD assets. Changes in estimates of expected credit losses after acquisition are recognized as credit loss expense (or reversal of credit loss expense) in subsequent periods as they arise. Any non-credit discount or premium resulting from acquiring a pool of purchased financial assets with credit deterioration shall be allocated to each individual asset. At the acquisition date, the initial allowance for credit losses determined on a collective basis shall be allocated to individual assets to appropriately allocate any non-credit discount or premium. The non-credit discount or premium, after the adjustment for the allowance for credit losses, shall be accreted to interest income using the interest method based on the effective interest rate determined after the adjustment for credit losses at the adoption date.

A purchased financial asset that does not qualify as a PCD asset is accounted for similar to an originated financial asset. Generally, this means that an entity recognizes the allowance for credit losses for non-PCD assets through net income at the time of acquisition. In addition, both the credit discount and non-credit discount or premium resulting from acquiring a pool of purchased financial assets that do not qualify as PCD assets shall be allocated to each individual asset. This combined discount or premium shall be accreted to interest income using the effective yield method.

Goodwill

Under FASB ASC 350, *Intangibles – Goodwill and Other*, goodwill is not amortized, but rather tested annually for impairment. Southern National evaluates goodwill for impairment on an annual basis or more frequently if events or circumstances warrant. Our annual assessment occurs during the third calendar quarter. Goodwill totaled $101.9 million at December 31, 2020. There was no impairment recorded for the years ended December 31, 2020, 2019 and 2018.

Valuation of Deferred Tax Asset

The provision for income taxes reflects the tax effects of the transactions reported in the consolidated financial statements, including taxes currently due as well as changes in deferred taxes. Deferred tax assets and liabilities represent estimates of the future tax return consequences of temporary differences between carrying amounts and tax bases of assets and liabilities. Deferred tax assets and liabilities are computed by using currently enacted income tax rates and applying those rates to the periods in which the deferred tax assets or liabilities are expected to be realized or settled. As changes in tax laws or rates are enacted, deferred tax assets and liabilities are adjusted through the provision for income taxes. As of December 31, 2020 and 2019, management concluded that it is more likely than not that Southern National will generate sufficient taxable income to fully utilize our deferred tax assets.

OVERVIEW

Southern National is a corporation that was formed on July 28, 2004 under the laws of the Commonwealth of Virginia and is the holding company for Sonabank, a Virginia state-chartered bank which commenced operations on April 14, 2005. Sonabank provides a range of financial services to individuals and small and medium sized businesses.

At December 31, 2020, Sonabank had forty-two full-service branches in Virginia and Maryland and also provides services to customers through certain internet and mobile applications. Thirty-seven full-service retail branches are in Virginia (Ashland, Burgess, Callao, Central Garage, Charlottesville, Chester, Clifton Forge, Colonial Heights, Courtland, Deltaville, Fairfax, Front Royal, Gloucester, Gloucester Point, Hampton, Hartfield, Heathsville, Kilmarnock, Leesburg, McLean, Mechanicsville (2), Middleburg, Midlothian, New Market, Newport News, Quinton, Reston, Richmond, South Riding, Surry, Tappahannock (2), Urbanna, Warrenton, Waverly, and Williamsburg) and five full-service retail branches are in Maryland (Bethesda, Brandywine, Owings, Rockville, and Upper Marlboro). We have

administrative offices in Warrenton and Glen Allen, Virginia. Our South Riding branch will be closing effective April 15, 2021.

While we offer a wide range of commercial banking services, we focus on making loans secured primarily by commercial real estate and other types of secured and unsecured commercial loans to small and medium-sized businesses in a number of industries, as well as loans to individuals for a variety of purposes. We are a leading SBA lender among Virginia community banks. We also invest in real estate-related investment securities, including collateralized mortgage obligations and agency mortgage backed securities. Our principal sources of funds for loans and investing in securities are deposits and, to a lesser extent, borrowings. We offer a broad range of deposit products, including checking, NOW, savings, and money market accounts and certificates of deposit. We actively pursue business relationships by utilizing the business contacts of our senior management, other bank officers and our directors, thereby capitalizing on our knowledge of our local market areas.

FINANCIAL HIGHLIGHTS

- Total assets as of December 31, 2020 were $3.09 billion.
- Loans on deferral as of December 31, 2020 were $122.0 million or 5.75% of total loans, excluding PPP balances, in-line with our expectations. Approximately 59% of total deferrals were from the hotel portfolio while restaurant deferrals declined to approximately $0.5 million.
- Total deposits increased $307.9 million from the prior year.
- Demand deposits (noninterest-bearing, NOW, money market) increased to 72.3% of total deposits as of December 31, 2020, compared to 56.3% as of December 31, 2019.
- Cost of deposits declined to 0.92% for the year ended December 31, 2020 compared to 1.43% for the year ended December 31, 2019.
- The Company booked its first Panacea loan customers in the fourth quarter of 2020.
- Allowance for credit losses to gross loans (excluding PPP balances) was 1.71% as of December 31, 2020.

RESULTS OF OPERATIONS

Net Income

Net income for the year ended December 31, 2020 was $23.3 million, compared to $33.2 million for the year ended December 31, 2019. The 29.8% decrease in the net income during the year ended December 31, 2020 compared to the year ended December 31, 2019 was primarily driven by higher provision for credit losses in 2020. The decline in net income was also driven by a charge of $4.4 million, net of taxes of salary and benefits expense related to the restructuring of executive management in 2020 and increased staffing in the commercial lending and Panacea Financial divisions along with the modified incentive and bonus plans and increased costs associated with recruitment in 2020. These decreases were partially offset by an increase in equity gain from the Company's mortgage affiliate driven by higher margins on closed loans and materially higher volumes from refinance activity as well as production from new hires and teams that were on-boarded in 2019. The decline in net income was also offset by a decline in cost of deposits and an increase in recoveries related to acquired charged-off loans and investment securities in the current year.

Net Interest Income

Our operating results depend primarily on our net interest income, which is the difference between interest and dividend income on interest-earning assets such as loans and investments, and interest expense on interest-bearing liabilities such as deposits and borrowings.

Net interest income was $91.6 million for the year ended December 31, 2020, compared to $83.6 million for the year ended December 31, 2019. The increase in net interest income was due to higher levels of average earning assets and as a result of lower costs of funds including deposits and borrowings in 2020. Southern National's net interest margin for the year ended December 31, 2020 was 3.35%, compared to 3.39% for the year ended December 31, 2019. Net interest margin was impacted heavily by the origination of PPP loans in 2020. Total income on interest-earning assets was

$117.8 million and $120.5 million for the year ended December 31, 2020 and 2019, respectively. The yield on average interest-earning assets was 4.31% and 4.88% for the year ended December 31, 2020 and 2019, respectively. The decrease was primarily driven by market conditions. Interest and fees on loans totaled $111.6 million and $112.1 million for the year ended December 31, 2020 and 2019, respectively. The accretion of the discount on loans acquired in the acquisitions contributed $4.3 million to net interest income during the year ended December 31, 2020, compared to $3.9 million during the year ended December 31, 2019. The increase in accretion was due to increased acquired loan paydowns and payoffs. Average loans during the year ended December 31, 2020 were $2.40 billion compared to $2.16 billion during the year ended December 31, 2019.

The following table details average balances of interest-earning assets and interest-bearing liabilities, the amount of interest earned/paid on such assets and liabilities, and the yield/rate for the periods indicated:

Average Balance Sheets and Net Interest Analysis For the Year Ended

	December 31, 2020			December 31, 2019			December 31, 2018		
	Average Balance	Interest Income/ Expense	Yield/ Rate	Average Balance	Interest Income/ Expense	Yield/ Rate	Average Balance	Interest Income/ Expense	Yield/ Rate
	(Dollar amounts in thousands)								
Assets									
Interest-earning assets:									
Loans, net of deferred fees [(1)] [(2)]	$ 2,400,896	$ 111,647	4.65 %	$ 2,159,681	$ 112,181	5.19 %	$ 2,138,845	$ 110,213	5.15 %
Investment securities	217,932	4,730	2.17 %	241,800	6,224	2.57 %	247,182	6,386	2.58 %
Other earning assets	114,275	1,402	1.23 %	66,582	2,119	3.18 %	59,594	2,308	3.87 %
Total earning assets	2,733,103	117,779	4.31 %	2,468,063	120,524	4.88 %	2,445,621	118,907	4.86 %
Allowance for credit losses	(20,638)			(11,852)			(11,292)		
Total non-earning assets	273,673			264,265			260,348		
Total assets	$ 2,986,138			$ 2,720,475			$ 2,694,677		
Liabilities and stockholders' equity									
Interest-bearing liabilities:									
NOW and other demand accounts	$ 481,470	$ 3,505	0.73 %	$ 360,254	$ 2,989	0.83 %	$ 324,797	$ 1,478	0.46 %
Money market accounts	508,260	4,188	0.82 %	439,097	7,745	1.76 %	328,142	3,060	0.93 %
Savings accounts	167,567	490	0.29 %	145,855	461	0.32 %	159,865	512	0.32 %
Time deposits	645,123	12,149	1.88 %	868,420	19,407	2.23 %	808,718	13,185	1.63 %
Total interest-bearing deposits	1,802,420	20,332	1.13 %	1,813,626	30,602	1.69 %	1,621,521	18,235	1.12 %
Borrowings	358,087	5,807	1.62 %	188,647	6,322	3.35 %	380,822	9,606	2.52 %
Total interest-bearing liabilities	2,160,507	26,139	1.21 %	2,002,273	36,924	1.84 %	2,002,343	27,841	1.39 %
Noninterest-bearing liabilities:									
Demand deposits	416,249			332,924			336,380		
Other liabilities	24,693			22,115			18,646		
Total liabilities	2,601,449			2,357,312			2,357,370		
Stockholders' equity	384,689			363,163			337,307		
Total liabilities and stockholders' equity	$ 2,986,138			$ 2,720,475			$ 2,694,677		
Net interest income		$ 91,640			$ 83,600			$ 91,066	
Interest rate spread			3.10 %			3.04 %			3.47 %
Net interest margin			3.35 %			3.39 %			3.72 %

(1) Includes loan fees in both interest income and the calculation of the yield on loans.

(2) Calculations include non-accruing loans in average loan amounts outstanding.

The following table summarizes changes in net interest income attributable to changes in the volume of interest-earning assets and interest-bearing liabilities compared to changes in interest rates. The change in interest, due to both rate and volume, has been proportionately allocated between rate and volume.

	Year Ended December 31, 2020 vs. 2019			Year Ended December 31, 2019 vs. 2018		
	Increase (Decrease) Due to Change in:			Increase (Decrease) Due to Change in:		
	Volume	Rate	Net Change	Volume	Rate	Net Change
	(in thousands)					
Interest-earning assets:						
Loans, net of deferred fees	$ (6,602)	$ 6,068	$ (534)	$ 1,172	$ 796	$ 1,968
Investment securities	(468)	(1,026)	(1,494)	(129)	(33)	(162)
Other earning assets	(4,950)	4,233	(717)	365	(553)	(188)
Total interest-earning assets	(12,020)	9,275	(2,745)	1,408	210	1,618
Interest-bearing liabilities:						
NOW and other demand accounts	808	(293)	515	176	1,335	1,511
Money market accounts	1,493	(5,049)	(3,556)	1,304	3,380	4,684
Savings accounts	62	(33)	29	(50)	—	(50)
Time deposits	(4,515)	(2,743)	(7,258)	1,074	5,148	6,222
Total interest-bearing deposits	(2,152)	(8,118)	(10,270)	2,504	9,863	12,367
Borrowings	(1,217)	702	(515)	(9,391)	6,108	(3,283)
Total interest-bearing liabilities	(3,369)	(7,416)	(10,785)	(6,887)	15,971	9,084
Change in net interest income	$ (8,651)	$ 16,691	$ 8,040	$ 8,295	$ (15,761)	$ (7,466)

Provision for Credit Losses

The provision for credit losses is a current charge to earnings made in order to adjust the allowance for credit losses to an appropriate level for inherent probable losses in the loan portfolio based on an evaluation of the loan portfolio, current economic conditions, changes in the nature and volume of lending, historical loan experience and other known internal and external factors affecting loan collectability. Our allowance for credit losses is calculated by segmenting the loan portfolio by loan type and applying risk factors to each segment. The risk factors are determined by considering historical loss data, peer data, as well as applying management's judgment.

The Company elected to defer adoption of CECL until the earlier of the termination date of the current national emergency, declared on March 31, 2020, under the National Emergencies Act in connection with the COVID-19 outbreak, or December 31, 2020. The Company adopted ASU 2016-13 effective January 1, 2020 and implemented as of December 31, 2020, resulting in a gross cumulative effect adjustment of $8.3 million. The provision for credit losses for the years ended December 31, 2020, 2019 and 2018 was $19.5 million, $350 thousand and $4.2 million, respectively. We had charge-offs totaling $2.3 million during 2020, $3.3 million during 2019 and $3.1 million during 2018. There were recoveries totaling $685 thousand during 2020, $906 thousand during 2019 and $1.8 million during 2018.

The Financial Condition Section of Management's Discussion and Analysis provides information on our loan portfolio, past due loans, nonperforming assets and the allowance for credit losses.

Noninterest Income

The following tables present the major categories of noninterest income for the years ended December 31, 2020, 2019 and 2018 (in thousands):

	For the Year Ended December 31,		
(dollars in thousands)	**2020**	**2019**	**Change**
Account maintenance and deposit service fees	$ 6,520	$ 7,159	$ (639)
Income from bank-owned life insurance	1,559	1,699	(140)
Equity gain from mortgage affiliate	10,789	1,191	9,598
Recoveries related to acquired charged-off loans and investment securities	6,500	1,537	4,963
Other	703	1,000	(297)
Total noninterest income	$ 25,451	$ 12,586	$ 12,865

(dollars in thousands)	**2019**	**2018**	**Change**
Account maintenance and deposit service fees	$ 7,159	$ 5,959	$ 1,200
Income from bank-owned life insurance	1,699	1,983	(284)
Equity loss from mortgage affiliate	1,191	(894)	2,085
Gain on sales of investment securities	—	—	—
Recoveries related to acquired charged-off loans and investment securities	1,537	2,610	(1,073)
Other	1,000	541	459
Total noninterest income	$ 12,586	$ 10,199	$ 2,387

Noninterest income increased 102% to $25.5 million for the year ended December 31, 2020, compared to $12.6 million for the year ended December 31, 2019. The $12.9 million increase was primarily driven by a $9.6 million increase in equity gain from the Company’s mortgage affiliate and $5.0 million increase in recoveries related to acquired charged-off loans and investment securities. Equity gain from the Company’s mortgage affiliate increased $9.6 million driven by higher margins on closed loans and materially higher volumes from refinance activity as well as production from new hires and teams that were on-boarded in 2019. The increase was also attributable to a recovery related to a previously charged-off acquired loan of approximately $2.0 million during 2020. These increases were partially offset by a decrease of $639 thousand in account maintenance and deposit service fees primarily in account service charges and non-sufficient funds fee. Income from bank-owned life insurance decreased $140 thousand due to death benefits paid in 2019.

Noninterest Expense

The following tables present the major categories of noninterest expense for the years ended December 31, 2020, 2019 and 2018 (in thousands):

	For the Year Ended December 31,		
(dollars in thousands)	**2020**	**2019**	**Change**
Salaries and benefits	$ 36,675	$ 26,261	$ 10,414
Occupancy expenses	6,142	6,204	(62)
Furniture and equipment expenses	2,725	2,719	6
Amortization of core deposit intangible	1,364	1,418	(54)
Virginia franchise tax expense	2,457	2,251	206
Data processing expense	3,178	2,381	797
Telephone and communication expense	1,497	1,615	(118)
Net (gain) loss on other real estate owned	960	(38)	998
Professional fees	4,726	3,612	1,114
Other operating expenses	8,016	10,169	(2,153)
Total noninterest expenses	$ 67,740	$ 56,592	$ 11,148

(dollars in thousands)	**2019**	**2018**	**Change**
Salaries and benefits	$ 26,261	$ 27,706	$ (1,445)
Occupancy expenses	6,204	6,628	(424)
Furniture and equipment expenses	2,719	2,795	(76)
Amortization of core deposit intangible	1,418	1,445	(27)
Virginia franchise tax expense	2,251	1,839	412
FDIC assessment	—	—	—
Data processing expense	2,381	1,885	496
Telephone and communication expense	1,615	2,035	(420)
Amortization of FDIC indemnification asset			—
Net (gain) loss on other real estate owned	(38)	360	(398)
Professional fees	3,612	1,644	1,968
Other operating expenses	10,169	7,423	2,746
Total noninterest expenses	$ 56,592	$ 53,760	$ 2,832

Noninterest expenses were $67.7 million during the year ended December 31, 2020, compared to $56.6 million during the year ended December 31, 2019. The 19.7% increase in noninterest expenses was primarily due to an increase in employee compensation and benefits expense, higher legal and professional fees and higher data processing expense, partially offset by lower other operating expenses. Employee compensation and benefits expense totaled $36.7 million and $26.3 million for the year ended December 31, 2020 and 2019, respectively. The increase was associated with a pre-tax management restructuring expense of $5.6 million in 2020 and increased staffing in the commercial lending and Panacea Financial divisions along with the modified incentive and bonus plans and increased costs associated with recruitment in 2020. The increase in noninterest expense during the year ended December 31, 2020 was also attributable to a $1.1 million increase in professional fees driven by higher consulting and legal services and a $797 thousand increase in data processing expense. We also recorded net loss of $960 thousand on other real estate owned for the year ended December 31, 2020 compared to a net gain of $38 thousand for the year ended December 31, 2019. The decrease in other operating expenses was driven by a pre-tax nonrecurring loss of $3.2 million with related legal expense of $502 thousand during 2019 that did not recur, partially offset by increased expenses associated with our pending name change and rebranding efforts.

FINANCIAL CONDITION

Balance Sheet Overview

Total assets were $3.09 billion as of December 31, 2020 and $2.72 billion as of December 31, 2019. Total loans increased 11.6%, from $2.19 billion at December 31, 2019 to $2.44 billion at December 31, 2020, with loan growth in

2020 primarily due to PPP loan originations. Excluding PPP loans, loans outstanding decreased $65.0 million, or 3.0%, since December 31, 2019. Total deposits were $2.43 billion at December 31, 2020 compared to $2.12 billion at December 31, 2019 and total equity was $390.6 million and $377.2 million at December 31, 2020 and December 31, 2019, respectively.

Loans

Total loans, net of deferred fees were $2.44 billion and $2.19 billion at December 31, 2020 and 2019, respectively. Loan growth in 2020 was primarily due to PPP loan originations, which totaled $319.4 million at December 31, 2020. Excluding PPP loans, loans outstanding decreased $65.0 million, or 3.0%, since December 31, 2019. As of December 31, 2020, we had $122.0 million of loans on deferral, or 5.75% of total loans excluding PPP loans. Hotel loans account for 58.9% of all deferrals with 27.1% of the hotel portfolio deferred at December 31, 2020.

As of December 31, 2020 and 2019, substantially all of our loans were to customers located in Virginia and Maryland. We are not dependent on any single customer or group of customers whose insolvency would have a material adverse effect on operations.

The following table summarizes the composition of our loans, net of unearned income, at December 31 for the years indicated (in thousands):

	2020		2019		2018		2017		2016	
	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percent
Loans secured by real estate:										
Commercial real estate - owner occupied	$ 435,078	17.8 %	$ 414,479	19.0 %	$ 407,031	18.7 %	$ 401,847	19.5 %	$ 154,807	16.6 %
Commercial real estate - non-owner occupied	600,706	24.6 %	559,195	25.6 %	540,698	24.8 %	440,700	21.4 %	279,634	29.9 %
Secured by farmland	11,662	0.5 %	17,622	0.8 %	20,966	1.0 %	23,038	1.1 %	541	0.1 %
Construction and land development	103,264	4.2 %	150,750	6.9 %	146,654	6.7 %	197,972	9.6 %	91,067	9.8 %
Residential 1-4 family	557,257	22.8 %	604,777	27.7 %	565,083	25.9 %	483,006	23.4 %	230,810	24.8 %
Multi- family residential	107,267	4.4 %	82,055	3.8 %	82,516	3.8 %	70,892	3.4 %	30,021	3.2 %
Home equity lines of credit	91,606	3.7 %	109,006	5.0 %	128,225	5.9 %	152,829	7.4 %	29,203	3.1 %
Total real estate loans	1,906,840	78.0 %	1,937,884	88.7 %	1,891,173	86.8 %	1,770,284	85.8 %	816,083	87.5 %
Commercial loans	187,060	7.7 %	221,447	10.1 %	255,441	11.7 %	253,258	12.3 %	115,365	12.4 %
Paycheck protection program loans	319,428	13.1 %	—	— %	—	— %	—	— %	—	— %
Consumer loans	22,290	0.9 %	26,304	1.2 %	32,347	1.5 %	39,374	1.9 %	856	0.1 %
Total Non-PCD loans	2,435,618	99.6 %	2,185,635	100 %	2,178,961	100 %	2,062,916	100 %	932,304	100 %
PCD loans	8,908	0.4 %								
Total loans	2,444,526	100.0 %								
Plus (less) deferred costs (fees) on loans	(4,030)		412		(137)		(588)		(1,889)	
Loans, net of deferred fees	$ 2,440,496		$ 2,186,047		$ 2,178,824		$ 2,062,328		$ 930,415	

The following table sets forth the contractual maturity ranges of the construction and land development and commercial loan portfolios and the amount of those loans with fixed and floating interest rates in each maturity range as of December 31, 2020 (in thousands):

		After 1 Year Through 5 Years		After 5 Years		
	One Year or Less	Fixed Rate	Floating Rate	Fixed Rate	Floating Rate	Total
Construction and land development	$ 74,442	$ 10,214	$ 7,413	$ 5,048	$ 6,147	$ 103,264
Commercial	100,322	354,880	7,161	8,457	35,668	506,488
Total	$ 174,764	$ 365,094	$ 14,574	$ 13,505	$ 41,815	$ 609,752

Asset Quality; Past Due Loans and Nonperforming Assets

Asset quality remained solid during 2020. The outbreak of COVID-19 and resulting economic instability has had and will likely continue to have an impact on our asset quality, but it is currently unknown to what extent. We will generally place a loan on nonaccrual status when it becomes 90 days past due. Loans will also be placed on nonaccrual status in

cases where we are uncertain whether the borrower can satisfy the contractual terms of the loan agreement. Cash payments received while a loan is categorized as nonaccrual will be recorded as a reduction of principal as long as doubt exists as to future collections. We defer COVID-impacted loans to end of the deferral date and track delinquency from end of that new deferral date. During the third and fourth quarter of 2020, the Company saw a substantial amount of deferred loans return to traditional loan terms.

We maintain appraisals on loans secured by real estate, particularly those categorized as nonperforming loans and potential problem loans. In instances where appraisals reflect reduced collateral values, we make an evaluation of the borrower's overall financial condition to determine the need, if any, for impairment or write-down to their fair values. If foreclosure occurs, we record OREO at the lower of our recorded investment in the loan or fair value less our estimated costs to sell.

Our loss and delinquency experience on our loan portfolio has been limited by a number of factors, including our underwriting standards and the relatively short period of time since the loans were originated. Whether losses and delinquencies in our portfolio will increase significantly depends upon the value of the real estate securing the loans and economic factors, such as the overall economy in our market area, including as a result of the impact of COVID-19.

The following table presents a comparison of nonperforming assets as of December 31, for the years indicated (in thousands):

	December 31, 2020	December 31, 2019 (1)	December 31, 2018 (1)	December 31, 2017 (1)	December 31, 2016 (1)
Nonaccrual loans	$ 14,462	$ 8,900	$ 6709	$ 16,931	$ 3,795
Loans past due 90 days and accruing interest	—	—	—	—	—
Total nonperforming loans	14,462	8,900	6,709	16,931	3,795
Other real estate owned	3,078	6,224	5,077	7,577	8,617
Total nonperforming assets	$ 17,540	$ 15,124	$ 11,786	$ 24,508	$ 12,412
Troubled debt restructurings	$ 987	$ 697	$ 692	$ 672	$ 688
SBA guaranteed amounts included in nonaccrual loans	$ 3,076	$ 4,129	$ 3,391	$ 4,664	$ 2,173
Allowance for credit losses to nonperforming loans	251.32 %	115.30 %	207.63 %	55.50 %	226.88 %
Allowance for credit losses to total loans	1.52 %	0.47 %	0.57 %	0.46 %	0.95 %
Nonperforming assets excluding SBA guaranteed loans to total assets	0.47 %	0.41 %	0.28 %	0.77 %	0.92 %

(2) Included non-covered loans and non-covered assets.

Not included in the table above are $122.0 million of loans that were subject to COVID-related deferrals at December_31, 2020. Some of these loans may become potential problem loans in 2021.

OREO at December 31, 2020 was $3.1 million, compared to $6.2 million at December 31, 2019. The decrease was primarily driven by sale of properties and write-downs on OREO during 2020.

Loans acquired in a transaction covered under an FDIC loss-share agreement expired on December 31, 2019 and therefore any references to "non-covered" loans do not apply to any periods after December 31, 2019. Nonaccrual loans were $14.5 million (excluding $3.1 million of loans fully covered by SBA guarantees) at December 31, 2020, compared to $4.8 million (non-covered and excluding $4.1 million of loans fully covered by SBA guarantees) at December 31, 2019, an increase of 202%. The ratio of non-covered nonperforming assets (excluding the SBA guaranteed loans) to total non-covered assets was 0.41% at December 31, 2019 and the ratio of nonperforming assets (excluding the SBA guaranteed loans) to total assets was 0.47% at December 31, 2020, an increase of 6 basis points.

At December 31, 2020, our total substandard loans totaled $44.6 million. Included in the total substandard loans were SBA guarantees of $2.3 million. Special mention loans totaled $30.0 million at December 31, 2020.

As of December 31, 2020, there were seven TDR loans in the amount of $987 thousand primarily due to the economic impact of COVID-19. There have been no defaults of TDRs modified during the past twelve months.

We identify potential problem loans based on loan portfolio credit quality. We define our potential problem loans as our classified/criticized loans less total nonperforming loans noted above. At December 31, 2020, our potential problem loans totaled $30.2 million.

Allowance for Credit Losses

We are very focused on the asset quality of our loan portfolio, both before and after the loan is made. We have established underwriting standards that we believe are effective in maintaining high credit quality in our loan portfolio. We have experienced loan officers who take personal responsibility for the loans they underwrite, a standing credit committee that reviews each loan application carefully, and a requirement that loans over $1.5 million must be approved by the Executive Credit Committee consisting of the President and CEO, Chief Credit Officer, Chief Credit Risk Officer, Chief SBA Lending Officer, Director of Small Business and Consumer Lending, and the Commercial Credit Risk Officer. Loans in the amount of $20.0 million to legal lending limit are approved by the full Board of Directors or two outside directors. Loans up to $500 thousand must be approved by one regular and one Senior member of our standing Credit Committee, loans in the amount of $500 thousand to $1.5 million must be approved by one regular, one Senior and one executive member (President and CEO or Chief Credit officer) of our standing Credit Committee.

Our allowance for credit losses is established through charges to earnings in the form of a provision for credit losses. Management evaluates the allowance at least quarterly. In addition, on a quarterly basis our board of directors reviews our loan portfolio, evaluates credit quality, reviews the loan loss provision and the allowance for credit losses and makes changes as may be required. In evaluating the allowance, management and the board of directors consider the growth, composition and industry diversification of the loan portfolio, historical loan loss experience, current delinquency levels and all other known factors affecting loan collectability.

The allowance for credit losses is based on the CECL methodology and represents management's estimate of an amount appropriate to provide for expected credit losses in the loan portfolio in the normal course of business. This estimate is based on historical credit loss information adjusted for current conditions and reasonable and supportable forecasts applied to various loan types that compose our portfolio, including the effects of known factors such as the economic environment within our market area will have on net losses. The allowance is also subject to regulatory examinations and determination by the regulatory agencies as to the appropriate level of the allowance.

Our loan review program is administrated by the Chief Credit Risk Officer who reports the results directly to the Audit Committee of the Board of Directors. The Bank's credit policy specifies that "Internal Loan review is responsible for performing a full scope review and written report of loans with a total dollar commitment amount equal to 30% of commercial loans outstanding at the previous year-end including Construction and Development, Nonfarm nonresidential (CRE) and commercial and Industrial. External loan review is responsible for reviewing 50% of the same portfolio at previous year end based on a judgmental sample including loans internally reviewed, and classified and criticized loans. On a combined basis loan reviews on at least 80% of the specified portfolio of loans outstanding at prior year end." In 2020, internal loan review performed loan reviews on loans and commitments totaling 12.8% of this loan portfolio outstanding as of December 31, 2019. An independent third party consultant performed loan reviews on 68.74% of this portfolio. In 2020, internal and external loan reviews were performed on 81.54% of the specified portfolio of loans. In 2020 we plan to have the independent third-party consultant review loans and commitments totaling at least 50% of the loan portfolio outstanding as of December 31, 2020, and another 30% reviewed internally. Loan reviews totaling at least 80% of the specified commercial loan portfolio outstanding at December 31, 2020 will be performed. The purpose of loan review by a third-party is to validate management's assessment of risk of the individual loans in the portfolio and to determine whether the loan was approved, underwritten and is being monitored in accordance with the Bank's credit policy and regulatory guidance. Management's risk assessment of individual loans

takes into consideration among other factors, the estimated value of the underlying collateral, the borrower's ability to repay, the borrower's payment history and current payment status.

The following table sets forth the allowance for credit/loan losses allocated by loan category and the percent of loans in each category to total loans at the dates indicated (in thousands):

	As of December 31,									
	2020		2019		2018		2017		2016	
	Allowance for Credit Losses	Percent of Loans by Category to Total Loans	Allowance for Loan Losses	Percent of Loans by Category to Total Loans	Allowance for Loan Losses	Percent of Loans by Category to Total Loans	Allowance for Loan Losses	Percent of Loans by Category to Total Loans	Allowance for Loan Losses	Percent of Loans by Category to Total Loans
Commercial real estate (1)	$ 19,641	47.2 %	$ 2,530	49.1 %	$ 2,471	48.2 %	$ 2,011	45.4 %	$ 2,389	49.8 %
Construction and land development	1,815	4.2 %	683	6.9 %	821	6.7 %	692	9.6 %	752	9.8 %
Residential 1-4 family (2)	10,480	26.5 %	1,266	32.7 %	1,106	31.8 %	1,586	30.8 %	1,279	27.9 %
Commercial loans	1,498	20.7 %	4,518	10.1 %	6,497	11.7 %	4,496	12.3 %	3,366	12.4 %
Consumer loans	517	0.9 %	190	1.2 %	224	1.5 %	612	1.9 %	78	0.1 %
PCD loans	2,394	0.4 %	—	— %	—	— %	—	— %	—	— %
Total	36,345	100.0 %	9,187	100.0 %	11,119	100.0 %	9,397	100.0 %	7,864	100.0 %
Allowance for acquired loans	—		900		600		—		—	
Total allocated allowance	36,345		10,087		11,719		9,397		7,864	
Unallocated allowance	—		174		564		—		746	
Total	$ 36,345		$ 10,261		$ 12,283		$ 9,397		$ 8,610	

(1) Includes owner and non-owner occupied loans, loans secured by farmland and multi-family residential loans.

(2) Includes home equity lines of credit.

The following table presents an analysis of the allowance for credit losses for the periods indicated (in thousands):

	For the Years Ended December 31,				
	2020	2019	2018	2017	2016
Balance, beginning of period	$ 10,261	$ 12,283	$ 9,397	$ 8,610	$ 8,421
Provision charged to operations:					
Adoption of ASC 326	8,292	—	—	—	—
Total provisions (credits)	19,450	350	4,200	8,625	4,912
Recoveries credited to allowance:					
Real estate - commercial (1)	140	213	15	431	8
Real estate - construction, land and other	—	—	—	1	121
Real estate - residential 1-4 family (2)	418	306	125	17	10
Commercial	94	351	1,626	538	96
Consumer	33	36	18	4	4
Total recoveries	685	906	1,784	991	239
Loans charged off:					
Real estate - commercial (1)	52	1,645	400	100	799
Real estate - construction, land and other	—	—	—	—	449
Real estate - residential 1-4 family (2)	433	742	842	369	22
Commercial	1,734	622	1,566	8,250	3,370
Consumer	124	269	290	110	322
Total loans charged-off	2,343	3,278	3,098	8,829	4,962
Net charge-offs	1,658	1,314	7,838	4,723	2,164
Balance, end of period	$ 36,345	$ 10,261	$ 12,283	$ 9,397	$ 8,610
Net charge-offs to average loans, net of unearned income	0.07 %	0.11 %	0.06 %	0.51 %	0.53 %

(1) Includes owner and non-owner occupied loans, loans secured by farmland and multi-family residential loans.

(2) Includes home equity lines of credit.

In 2020, we had loan charge-offs totaling $2.3 million, compared to $3.3 million in 2019.

We believe that the allowance for credit losses at December 31, 2020 is sufficient to absorb probable incurred credit losses in our loan portfolio based on our assessment of all known factors affecting the collectability of our loan portfolio. Our assessment involves uncertainty and judgment; therefore, the adequacy of the allowance for credit losses cannot be determined with precision and may be subject to change in future periods. In addition, bank regulatory authorities, as part of their periodic examination, may require additional charges to the provision for credit losses in future periods if the results of their reviews warrant additions to the allowance for credit losses.

Investment Securities

Our investment securities portfolio provides us with required liquidity and investment securities to pledge as collateral to secure public deposits, certain other deposits, a line of credit for advances from the FHLB of Atlanta, and repurchase agreements.

Our investment securities portfolio is managed by our executive vice chairman and our treasurer, both of whom have significant experience in this area, with the concurrence of our Asset/Liability Committee. In addition to our executive vice chairman (who is the chairman of the Asset/Liability Committee) and our Controller, this committee is comprised of outside directors and other senior officers of the Bank, including but not limited to our executive chairman, our chief executive officer and our chief financial officer. Investment management is performed in accordance with our investment policy, which is approved annually by the Asset/Liability Committee and the Board of Directors. Our investment policy addresses our investment strategies, approval process, approved securities dealers and authorized investments. Our investment policy authorizes us to invest in:

- Government National Mortgage Association (“GNMA”), Federal National Mortgage Association (“FNMA”) and the Federal Home Loan Mortgage Corporation (“FHLMC”) mortgage-backed securities (“MBS”)
- Collateralized mortgage obligations
- U.S. Treasury securities
- SBA guaranteed loan pools
- Agency securities
- Obligations of states and political subdivisions
- Pooled trust preferred securities comprised of a minimum of 80% bank collateral with an investment grade rating or a minimum of 60% bank collateral with a AAA rating at purchase
- Other corporate debt securities rated Aa3/AA- or better at purchase

MBS are securities that have been developed by pooling a number of real estate mortgages and which are principally issued by agency/government-sponsored entities (“GSEs”) such as the GNMA, FNMA and FHLMC. These securities are deemed to have high credit ratings, and minimum regular monthly cash flows of principal and interest are guaranteed by the issuing agencies.

Unlike U.S. Treasury and U.S. government agency securities, which have a lump sum payment at maturity, MBS provide cash flows from regular principal and interest payments and principal prepayments throughout the lives of the securities. MBS which are purchased at a premium will generally suffer decreasing net yields as interest rates drop because homeowners tend to refinance their mortgages. Thus, the premium paid must be amortized over a shorter period. Conversely, MBS purchased at a discount will obtain higher net yields in a decreasing interest rate environment. As interest rates rise, the opposite will generally be true. During a period of increasing interest rates, fixed rate MBS do not tend to experience heavy prepayments of principal, and consequently the average life of these securities will be lengthened. If interest rates begin to fall, prepayments will generally increase.

Collateralized mortgage obligations (“CMOs”) are bonds that are backed by pools of mortgages. The pools can be GNMA, FNMA or FHLMC pools or they can be private-label pools. The CMOs are designed so that the mortgage collateral will generate a cash flow sufficient to provide for the timely repayment of the bonds. The mortgage collateral

pool can be structured to accommodate various desired bond repayment schedules, provided that the collateral cash flow is adequate to meet scheduled bond payments. This is accomplished by dividing the bonds into classes to which payments on the underlying mortgage pools are allocated. The bond's cash flow, for example, can be dedicated to one class of bondholders at a time, thereby increasing call protection to bondholders. In private-label CMOs, losses on underlying mortgages are directed to the most junior of all classes and then to the classes above in order of increasing seniority, which means that the senior classes have enough credit protection to be given the highest credit rating by the rating agencies.

Obligations of states and political subdivisions (municipal securities) are purchased with consideration of the current tax position of the Bank. In-state (Virginia) municipal bonds will be favored when they present better relative value than comparable out-of-state municipal bonds. Both taxable and tax-exempt municipal bonds may be purchased, but only after careful assessment of the market risk of the security. Appropriate credit evaluation must be performed prior to purchasing municipal bonds.

Southern National's corporate bonds consist of pooled trust preferred securities issued by banks, thrifts and insurance companies as well as senior subordinated notes issued by banks. The collateral pools of these trust preferred securities must be at least 80% banks or thrifts, if the rating at the time of purchase is A3/A- or better. If the rating is Aaa/AAA, the collateral pool must be at least 60% banks or thrifts. These securities generally have a long term (25 years or more), allow early redemption by the issuers, make periodic variable interest payments and mature at face value. Trust preferred securities allow the deferral of interest payments for up to five years.

We classify our investment securities as either held to maturity or available for sale. Debt investment securities that Southern National has the positive intent and ability to hold to maturity are classified as held to maturity and carried at amortized cost. Investment securities classified as available for sale are those debt securities that may be sold in response to changes in interest rates, liquidity needs or other similar factors. Investment securities available for sale are carried at fair value, with unrealized gains or losses net of deferred taxes, included in accumulated other comprehensive income (loss) in stockholders' equity. Investment securities totaling $40.7 million were in the held to maturity portfolio at December 31, 2020, compared to $72.5 million at December 31, 2019. Investment securities totaling $153.2 million were in the available for sale portfolio at December 31, 2020, compared to $164.8 million at December 31, 2019. During 2020 and 2019, $38.9 million and $45.1 million, respectively, of available for sale investment securities and $15.2 million and $15.3 million, respectively, of held to maturity investment securities were purchased. During 2020, $1.9 million and $1.7 million, respectively, of available for sale investment securities and held to maturity investment securities were sold. No investment securities were sold during 2019.

During 2020, we sold all the pooled trust preferred investment securities.

We recognized no credit impairment charges related to credit losses during 2020 or 2019.

Investment securities in our portfolio as of December 31, 2020 were as follows:

- residential government-sponsored collateralized mortgage obligations in the amount of $30.5 million;
- agency residential government-sponsored mortgage-backed securities in the amount of $62.1 million;
- corporate bonds in the amount of $15.1 million;
- commercial mortgage-backed securities in the amount of $30.2 million;
- SBA loan pool securities in the amount of $11.4 million;
- callable agency securities in the amount of $11.1 million;
- municipal bonds in the amount of $33.6 million (fair value of $33.8 million) with a taxable equivalent yield of 3.3% and ratings as follows:

Moody's Rating	Amount (in thousands)	Standard & Poor's Rating	Amount (in thousands)
Aaa	$ 10,855	AAA	$ 12,430
Aa1	6,755	AA+	7,196
Aa2	3,923	AA	5,120
Aa3	695	AA-	1,831
A1	2,326	A+	1,003
A2	1,003	A	822
Baa1	—	BBB+	—
NA	8,260	NA	5,415
Total	$ 33,817	Total	$ 33,817

For additional information regarding investment securities refer to "Item 8. Financial Statements and Supplementary Data, Note 2-Investment Securities."

The following table sets forth a summary of the investment securities portfolio as of the dates indicated. Available for sale investment securities are reported at fair value, and held to maturity investment securities are reported at amortized cost (in thousands).

	December 31,		
	2020	2019	2018
Available for sale securities:			
Residential government-sponsored mortgage-backed securities	$ 37,060	$ 48,979	$ 27,302
Obligations of states and political subdivisions	24,042	17,582	18,055
Corporate securities	15,079	2,012	2,008
Trust preferred securities	—	2,568	2,641
Residential government-sponsored collateralized mortgage obligations	29,416	36,689	43,057
Government-sponsored agency securities	6,075	14,822	3,125
Agency commercial mortgage-backed securities	30,190	27,731	27,304
SBA pool securities	11,371	14,437	19,885
Total	$ 153,233	$ 164,820	$ 143,377
Held to maturity investment securities:			
Residential government-sponsored mortgage-backed securities	$ 25,037	$ 22,925	$ 9,699
Obligations of states and political subdivisions	9,594	15,071	21,496
Trust preferred securities	—	1,938	2,610
Residential government-sponsored collateralized mortgage obligations	1,090	3,128	6,001
Government-sponsored agency securities	5,000	29,386	52,656
Total	$ 40,721	$ 72,448	$ 92,462

The following table sets forth the amortized cost, fair value, and weighted average yield of our investment securities by contractual maturity at December 31, 2020. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties (in thousands).

	Investment Securities Available for Sale		
	Amortized Cost	Fair Value	Weighted Average Yield
Obligations of states and political subdivisions			
Due after one year through five years	$ 2,341	$ 2,486	2.70 %
Due after five years through ten years	8,253	8,631	2.84 %
Due after ten years	12,372	12,925	2.10 %
	22,966	24,042	2.42 %
Corporate securities			
Due after one year through five years	2,000	2,004	5.77 %
Due after five years through ten years	11,000	11,065	4.67 %
Due after ten years	2,000	2,010	4.50 %
	15,000	15,079	4.79 %
Government-sponsored agency securities			
Due after one year through five years	1,500	1,566	2.00 %
Due after ten years	4,485	4,509	2.09 %
	5,985	6,075	2.07 %
Residential government-sponsored mortgage-backed securities			
Due after one year through five years	6,334	6,731	2.46 %
Due after five years through ten years	1,453	1,509	2.06 %
Due after ten years	27,655	28,820	1.99 %
	35,442	37,060	2.08 %
Residential government-sponsored collateralized mortgage obligations			
Due after five years through ten years	8,229	8,451	1.40 %
Due after ten years	20,451	20,965	1.39 %
	28,680	29,416	1.39 %
Agency commercial mortgage-backed securities			
Due less than one year	5,466	5,523	1.91 %
Due after one year through five years	19,455	20,299	2.23 %
Due after five years through ten years	4,197	4,368	1.74 %
	29,118	30,190	2.10 %
SBA pool securities			
Due after one year through five years	234	233	2.61 %
Due after five years through ten years	4,622	4,697	2.30 %
Due after ten years	6,585	6,441	2.21 %
	11,441	11,371	2.26 %
	$ 148,632	$ 153,233	2.29 %

	Investment Securities Held to Maturity		
	Amortized Cost	Fair Value	Weighted Average Yield
Obligations of states and political subdivisions			
Due less than one year	$ 1,443	$ 1,462	1.72 %
Due after one year through five years	1,963	2,052	2.46 %
Due after five years through ten years	2,183	2,231	3.03 %
Due after ten years	4,005	4,031	5.87 %
	9,594	9,776	3.90 %
Government-sponsored agency securities			
Due after ten years	5,000	5,163	3.34 %
	5,000	5,163	3.34 %
Residential government-sponsored mortgage-backed securities			
Due after five years through ten years	1,503	1,556	2.01 %
Due after ten years	23,534	24,208	1.23 %
	25,037	25,764	1.28 %
Residential government-sponsored collateralized mortgage obligations			
Due after ten years	1,090	1,129	1.56 %
	1,090	1,129	1.56 %
	$ 40,721	$ 41,832	2.16 %

Deposits and Other Borrowings

The market for deposits is competitive. We offer a line of traditional deposit products that currently include noninterest-bearing and interest-bearing checking (or NOW accounts), commercial checking, money market accounts, savings accounts and certificates of deposit. We compete for deposits through our banking branches with competitive pricing, advertising and online banking. We use deposits as a principal source of funding for our lending, purchasing of investment securities and for other business purposes.

Total deposits increased 14.5% to $2.43 billion at December 31, 2020 from $2.12 billion at December 31, 2019. Noninterest-bearing demand deposits increased from a year-end 2019 level of $339.2 million to $440.7 million as of December 31, 2020. Time deposits decreased from $783.0 million to $490.0 million and savings accounts increased from $144.5 million to $183.8 million over the same period. As of December 31, 2020, we had brokered certificates of deposit in the amount of $270 thousand and brokered money market deposits of $55.2 million. At December 31, 2019, we had brokered certificates of deposit in the amount of $114.1 million, and we had brokered money market deposits of $24.4 million.

The following table sets forth the average balance and average rate paid on each of the deposit categories for the years ended December 31, 2020, 2019 and 2018:

	2020		2019		2018	
	Average Balance	Average Rate	Average Balance	Average Rate	Average Balance	Average Rate
			(in thousands)			
Noninterest-bearing demand deposits	$ 416,249		$ 332,924		$ 336,380	
Interest-bearing deposits:						
Savings accounts	167,567	0.29 %	145,855	0.32 %	159,865	0.32 %
Money market accounts	508,260	0.82 %	439,097	1.76 %	328,142	0.93 %
NOW and other demand accounts	481,470	0.73 %	360,254	0.83 %	324,797	0.46 %
Time deposits	645,123	1.88 %	868,420	2.23 %	808,718	1.63 %
Total interest-bearing deposits	1,802,420	1.13 %	1,813,626	1.69 %	1,621,521	1.12 %
Total deposits	$ 2,218,669		$ 2,146,550		$ 1,957,902	

The variety of deposit accounts we offer allows us to be competitive in obtaining funds and in responding to the threat of disintermediation (the flow of funds away from depository institutions such as banking institutions into direct investment vehicles such as government and corporate securities). Our ability to attract and maintain deposits, and the effect of such retention on our cost of funds, has been, and will continue to be, significantly affected by the general economy and market rates of interest.

The following table sets forth the maturities of certificates of deposit of $100 thousand and over as of December 31, 2020 (in thousands):

Within 3 Months	3 to 6 Months	6 to 12 Months	Over 12 Months	Total
$ 100,793	$ 85,056	$ 74,773	$ 81,738	$ 342,360

We use borrowed funds to support our liquidity needs and to temporarily satisfy our funding needs from increased loan demand and for other shorter term purposes. We are a member of the FHLB and are authorized to obtain advances from the FHLB from time to time as needed. The FHLB has a credit program for members with different maturities and interest rates, which may be fixed or variable. We are required to collateralize our borrowings from the FHLB with our FHLB stock and other collateral acceptable to the FHLB. At December 31, 2020 and 2019, total FHLB borrowings were $100.0 million and $121.6 million, respectively. At December 31, 2020, we had $689.1 million of unused and available FHLB lines of credit.

Other borrowings can consist of FHLB convertible advances, FHLB overnight advances, other FHLB advances maturing within one year, federal funds purchased and securities sold under agreements to repurchase (“repo”) that

mature within one year, which are secured transactions with customers. The balance in repo accounts at December 31, 2020 and 2019 was $16.1 million and $12.9 million, respectively.

Other borrowings consist of the following (in thousands):

	December 31,		
	2020	2019	2018
FHLB convertible advances maturing 3/1/2030	$ 100,000	$ —	$ —
FHLB overnight advances	—	81,000	5,500
Short-term FHLB advances maturing 3/10/2020	—	40,640	—
Short-term FHLB advances maturing 6/27/2019	—	—	40,000
Short-term FHLB advances maturing 6/18/2019	—	—	27,200
Short-term FHLB advances maturing 6/12/2019	—	—	10,000
Short-term FHLB advances maturing 6/11/2019	—	—	80,640
Total FHLB advances	100,000	121,640	163,340
Securities sold under agreements to repurchase	16,065	12,883	18,721
Total	$ 116,065	$ 134,523	$ 182,061
Weighted average interest rate at year end	3.55 %	1.75 %	2.68 %
For the periods ended December 31, 2020, 2019 and 2018:			
Average outstanding balance	$ 118,099	$ 125,340	$ 324,155
Average interest rate during the year	0.89 %	2.30 %	1.91 %
Maximum month-end outstanding balance	$ 273,893	$ 174,739	$ 411,511

Junior Subordinated Debt and Senior Subordinated Notes

The Company has $10.3 million of trust preferred securities that were issued on September 17, 2003 and placed through a Trust in a pooled underwriting totaling approximately $650 million. The trust issuer invested the total proceeds from the sale of the trust preferred securities in Floating Rate Junior Subordinated Deferrable Interest Debentures (“Junior Subordinated Debt”). At December 31, 2020 and 2019, we had $9.7 million and $9.6 million, respectively, of Junior Subordinated Debt outstanding. The trust preferred securities pay cumulative cash distributions quarterly at a variable rate per annum, reset quarterly, equal to the three-month LIBOR plus 2.95%. As of December 31, 2020 and 2019, the interest rate was 3.18% and 4.85%, respectively. The dividends paid to holders of the trust preferred securities, which are recorded as interest expense, are deductible for income tax purposes.

The trust preferred securities may be included in Tier 1 capital for regulatory capital adequacy determination purposes up to 25% of Tier 1 capital after its inclusion. At December 31, 2020, all of the trust preferred securities qualified as Tier 1 capital.

Subject to certain exceptions and limitations, Southern National is permitted to elect from time to time to defer regularly scheduled interest payments on its outstanding Junior Subordinated Debt relating to its trust preferred securities. If Southern National defers interest payments on the Junior Subordinated Debt for more than 20 consecutive quarters, Southern National would be in default under the governing agreements for such notes and the amount due under such agreements would be immediately due and payable.

On January 20, 2017, Southern National completed the sale of $27.0 million of its fixed-to-floating rate Subordinated Notes due 2027 (the “SNBV Senior Subordinated Notes”). The SNBV Senior Subordinated Notes will initially bear interest at 5.875% per annum until January 31, 2022; thereafter, the SNBV Senior Subordinated Notes will be payable at an annual floating rate equal to three-month LIBOR plus a spread of 3.95% until maturity or early redemption. At December 31, 2020, all of the SNBV Senior Subordinated Notes qualified as Tier 2 capital.

In 2017, the Company assumed the Senior Subordinated Note Purchase Agreement dated April 22, 2015 with certain institutional accredited investors, pursuant to which $20.0 million in aggregate principal amount of its 6.50% Fixed-to-

Floating Rate Subordinated Notes due 2025 was sold to the investors. At December 31, 2020, 80% of the Senior Subordinated Notes qualified as Tier 2 capital. On February 1, 2021, 100% of the notes were redeemed.

On August 25, 2020, Southern National completed the sale of $60.0 million of its fixed-to-floating rate Subordinated Notes due 2030 (the “SNBV Subordinated Notes”). The SNBV Subordinated Notes will bear interest at an initial rate of 5.40% per annum, payable semi-annually in arrears on March 1 and September 1 of each year, commencing on March 1, 2021. From and including September 1, 2025 to, but excluding the maturity date or the date of earlier redemption (the “floating rate period”), the interest rate will reset quarterly to an annual interest rate equal to the Benchmark Rate, which is expected to be three-month Term SOFR, plus 531 basis points for each quarterly interest period during the floating rate period, payable quarterly in arrears on March 1, June 1, September 1, and December 1 of each year, commencing on December 1, 2025. Notwithstanding the foregoing, in the event that the Benchmark Rate is less than zero, the Benchmark Rate shall be deemed to be zero. At December 31, 2020, all of the SNBV Subordinated Notes qualified as Tier 2 capital.

Interest Rate Sensitivity and Market Risk

We are engaged primarily in the business of investing funds obtained from deposits and borrowings into interest-earning loans and investments. Consequently, our earnings depend to a significant extent on our net interest income, which is the difference between the interest income on loans and other investments and the interest expense on deposits and borrowings. To the extent that our interest-bearing liabilities do not reprice or mature at the same time as our interest-earning assets, we are subject to interest rate risk and corresponding fluctuations in net interest income. Our Asset-Liability Committee (“ALCO”) meets regularly and is responsible for reviewing our interest rate sensitivity position and establishing policies to monitor and limit exposure to interest rate risk. The policies established by the ALCO are reviewed and approved by our Board of Directors. We have employed asset/liability management policies that seek to manage our net interest income, without having to incur unacceptable levels of credit or investment risk.

We use simulation modeling to manage our interest rate risk, and review quarterly interest sensitivity. This approach uses a model which generates estimates of the change in our economic value of equity (“EVE”) over a range of interest rate scenarios. EVE is the present value of expected cash flows from assets, liabilities and off-balance sheet contracts using assumptions about estimated loan prepayment rates, reinvestment rates and deposit decay rates.

The following tables are based on an analysis of our interest rate risk as measured by the estimated change in EVE resulting from instantaneous and sustained parallel shifts in the yield curve (plus 400 basis points or minus 100 basis points, measured in 100 basis point increments) as of December 31, 2020 and 2019. All changes are within our Asset/Liability Risk Management Policy guidelines except for the change resulting from the 100 basis point decrease in interest rates at December 31, 2020 and 2019.

	Sensitivity of Economic Value of Equity As of December 31, 2020				
	Economic Value of Equity			Economic Value of Equity as a % of	
Change in Interest Rates in Basis Points (Rate Shock)	Amount	$ Change From Base	% Change From Base	Total Assets	Equity Book Value
	(dollar amounts in thousands)				
Up 400	$ 339,057	$ 5,568	1.67 %	10.98 %	86.81 %
Up 300	341,652	8,163	2.45 %	11.06 %	87.48 %
Up 200	342,561	9,072	2.72 %	11.09 %	87.71 %
Up 100	343,842	10,353	3.10 %	11.13 %	88.04 %
Base	333,489	—	— %	10.80 %	85.39 %
Down 100	282,586	(50,903)	(15.26)%	9.15 %	72.36 %

Change in Interest Rates in Basis Points (Rate Shock)	Sensitivity of Economic Value of Equity As of December 31, 2019				
	Economic Value of Equity			Economic Value of Equity as a % of	
	Amount	$ Change From Base	% Change From Base	Total Assets	Equity Book Value
	(dollar amounts in thousands)				
Up 400	$ 323,871	$ (45,102)	(12.22)%	11.90 %	85.85 %
Up 300	336,822	(32,151)	(8.71)%	12.37 %	89.29 %
Up 200	349,192	(19,781)	(5.36)%	12.83 %	92.56 %
Up 100	363,935	(5,038)	(1.37)%	13.37 %	96.47 %
Base	368,973	—	0.00 %	13.55 %	97.81 %
Down 100	353,371	(15,602)	(4.23)%	12.98 %	93.67 %

Our interest rate sensitivity is also monitored by management through the use of a model that generates estimates of the change in the net interest income ("NII") over a range of interest rate scenarios. NII depends upon the relative amounts of interest-earning assets and interest-bearing liabilities and the interest rates earned or paid on them. In this regard, the model assumes that the composition of our interest sensitive assets and liabilities existing at December 31, 2020 and 2019 remains constant over the period being measured and also assumes that a particular change in interest rates is reflected uniformly across the yield curve regardless of the duration to maturity or repricing of specific assets and liabilities. All changes are within our ALM Policy guidelines at December 31, 2020 and 2019.

Change in Interest Rates in Basis Points (Rate Shock)	Sensitivity of Net Interest Income As of December 31, 2020			
	Adjusted Net Interest Income		Net Interest Margin	
	Amount	$ Change From Base	Percent	% Change From Base
	(dollar amounts in thousands)			
Up 400	$ 78,988	$ (4,760)	2.89 %	(0.17)%
Up 300	80,341	(3,407)	2.94 %	(0.12)%
Up 200	81,604	(2,144)	2.99 %	(0.07)%
Up 100	83,039	(709)	3.04 %	(0.02)%
Base	83,748	—	3.06 %	— %
Down 100	82,667	(1,081)	3.02 %	(0.04)%

Change in Interest Rates in Basis Points (Rate Shock)	Sensitivity of Net Interest Income As of December 31, 2019			
	Adjusted Net Interest Income		Net Interest Margin	
	Amount	$ Change From Base	Percent	% Change From Base
	(dollar amounts in thousands)			
Up 400	$ 74,096	$ (8,158)	3.00 %	(0.33)%
Up 300	76,355	(5,899)	3.09 %	(0.24)%
Up 200	78,458	(3,796)	3.18 %	(0.15)%
Up 100	80,649	(1,605)	3.27 %	(0.06)%
Base	82,254	—	3.33 %	— %
Down 100	81,273	(981)	3.29 %	(0.04)%

Certain shortcomings are inherent in the methodology used in the above interest rate risk measurements. Modeling changes in EVE requires the making of certain assumptions that may or may not reflect the manner in which actual yields and costs respond to changes in market interest rates. Accordingly, although the EVE tables and NII tables provide an indication of our interest rate risk exposure at a particular point in time, such measurements are not intended to, and do not, provide a precise forecast of the effect of changes in market interest rates on our net worth and NII. Sensitivity of EVE and NII are modeled using different assumptions and approaches.

Liquidity and Funds Management

The objective of our liquidity management is to ensure the ability to meet our financial obligations. These obligations include the payment of deposits on demand or at maturity, the repayment of borrowings at maturity and the ability to

fund commitments and other new business opportunities. We obtain funding from a variety of sources, including customer deposit accounts, customer certificates of deposit and payments on our loans and investments. Historically, our level of core deposits has been insufficient to fully fund our lending activities. As a result, we have sought funding from additional sources, including institutional certificates of deposit and the sale of available for sale investment securities. In addition, we maintain lines of credit with the FHLB of Atlanta, federal funds lines of credit with three correspondent banks and utilize securities sold under agreements to repurchase and reverse repurchase agreement borrowings from approved securities dealers. For additional information about borrowings and anticipated principal repayments refer to the discussion about Contractual Obligations below and "Item 8. Financial Statements and Supplementary Data, Note 9 – Securities Sold Under Agreements To Repurchase And Other Short-Term Borrowings and Note 10 – Junior Subordinated Debt and Senior Subordinated Notes."

We prepare a cash flow forecast on a 30, 60 and 90 day basis along with a one and a two year basis. The projections incorporate expected cash flows on loans, investment securities, and deposits based on data used to prepare our interest rate risk analyses. To estimate loan growth, the projection incorporates the scheduled loan closings in the Loan Pipeline Report along with other management estimates.

During the year ended December 31, 2020, we funded our financial obligations with deposits and borrowings from the FHLB of Atlanta. At December 31, 2020, we had $355.3 million of unfunded lines of credit and undisbursed construction loan funds. The amount of certificate of deposit accounts maturing in less than one year was $369.7 million as of December 31, 2020. Management anticipates that funding requirements for these commitments can be met from the normal sources of funds.

On August 25, 2020, Southern National completed the sale of $60.0 million of its fixed-to-floating rate Subordinated Notes due 2030 (the "SNBV Subordinated Notes"). The SNBV Subordinated Notes will bear interest at an initial rate of 5.40% per annum, payable semi-annually in arrears on March 1 and September 1 of each year, commencing on March 1, 2021. From and including September 1, 2025 to, but excluding the maturity date or the date of earlier redemption (the "floating rate period"), the interest rate will reset quarterly to an annual interest rate equal to the Benchmark rate, which is expected to be three-month Term SOFR plus 531 basis points, for each quarterly interest period during the floating rate period, payable quarterly in arrears on March 1, June 1, September 1, and December 1 of each year, commencing on December 1, 2025. Notwithstanding the foregoing, in the event that the Benchmark rate is less than zero, the Benchmark rate shall be deemed to be zero.

While the Company believes that wholesale funding markets have remained open to us in the economic environment caused by COVID-19, the rates for short term funding have recently been volatile. If funding costs are elevated for an extended period of time, it could have an adverse effect on the Company's net interest margin. If an extended recession causes a large number of the Company's deposit customers to withdraw their funds, the Company might become more reliant on volatile or more expensive sources of funding. As of December 31, 2020, Southern National was not aware of any other known trends, events or uncertainties that have or are reasonably likely to have a material impact on our liquidity. As of December 31, 2020, Southern National has no material commitments or long-term debt for capital expenditures.

Capital Resources

Capital management consists of providing equity to support both current and future operations. We and the Bank are subject to risk-based capital adequacy requirements imposed by the Federal Reserve.

See "Item 1. Business, Supervision and Regulation—Capital Requirements."

The following table provides a comparison of the leverage and risk-weighted capital ratios of Sonabank at the periods indicated to the minimum and well-capitalized required regulatory standards:

	Minimum Required for Capital Adequacy Purposes	To Be Categorized as Well Capitalized (1)	Actual Ratio at December 31, 2020	December 31, 2019
Sonabank				
Common equity tier 1 capital ratio	7.00 %	6.50 %	15.83 %	14.81 %
Tier 1 risk-based capital ratio	8.50 %	8.00 %	15.83 %	14.81 %
Total risk-based capital ratio	10.50 %	10.00 %	17.09 %	15.29 %
Leverage ratio	4.00 %	5.00 %	11.25 %	12.07 %

(1) Prompt corrective action provisions are not applicable at the bank holding company level.

Impact of Inflation and Changing Prices

The financial statements and related financial data presented in this Annual Report on Form 10-K concerning Southern National have been prepared in accordance with U.S. GAAP, which require the measurement of financial position and operating results in terms of historical dollars, without considering changes in the relative purchasing power of money over time due to inflation. The primary impact of inflation on our operations is reflected in increased operating costs. Unlike most industrial companies, substantially all of the assets and liabilities of a financial institution are monetary in nature. As a result, changes in interest rates have a more significant impact on our performance than do the effects of changes in the general rate of inflation and changes in prices. Interest rates do not necessarily move in the same direction or in the same magnitude as the prices of goods and services. Many factors impact interest rates, including the FRB, inflation, recession, changes in unemployment, the money supply, and international disorder and instability in domestic and foreign financial markets. Like most financial institutions, changes in interest rates can impact our net interest income which is the difference between interest earned from interest-earning assets, such as loans and investment securities, and interest paid on interest-bearing liabilities, such as deposits and borrowings, as well as the valuation of our assets and liabilities.

Our interest rate risk management is the responsibility of the Bank's Asset/Liability Management Committee (the "Asset/Liability Committee"). The Asset/Liability Committee has established policies and limits for management to monitor, measure and coordinate our sources, uses and pricing of funds. The Asset/Liability Committee makes reports to the board of directors on a quarterly basis.

Seasonality and Cycles

We do not consider our commercial banking business to be seasonal.

Contractual Obligations

The following table reflects the contractual maturities of our term liabilities as of December 31, 2020. The amounts shown do not reflect contractual interest, early withdrawal or prepayment assumptions.

	Contractual Obligations				
	Less Than One Year	One to Three Years	Three to Five Years	More Than Five Years	Total
	(in thousands)				
Certificates of deposit [1]	$ 369,743	$ 105,008	$ 15,262	$ 35	$ 490,048
Repurchase agreements	16,065	—	—	—	16,065
FHLB advances	100,000	—	—	—	100,000
Junior subordinated debt	—	—	—	10,310	10,310
Senior subordinated notes	—	—	—	107,000	107,000
Operating leases	2,542	3,791	1,123	1,376	8,832
Total	$ 488,350	$ 108,799	$ 16,385	$ 118,721	$ 732,255

(1) Certificates of deposit give customers rights to early withdrawal. Early withdrawals may be subject to penalties. The penalty amount depends on the remaining time to maturity at the time of early withdrawal.

Off-Balance Sheet Arrangements

Southern National is a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit, standby letters of credit and guarantees of credit card accounts. These instruments involve elements of credit and funding risk in excess of the amount recognized in the consolidated balance sheet. Letters of credit are written conditional commitments issued by Southern National to guarantee the performance of a customer to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loans to customers. We had letters of credit outstanding totaling $15.9 million and $17.7 million as of December 31, 2020 and 2019, respectively.

Our exposure to credit loss in the event of nonperformance by the other party to the financial instruments for commitments to extend credit and letters of credit is based on the contractual amount of these instruments. We use the same credit policies in making commitments and conditional obligations as we do for on-balance sheet instruments. Unless noted otherwise, we do not require collateral or other security to support financial instruments with credit risk.

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 are made predominately for adjustable rate loans, and generally have fixed expiration dates of up to three months or other termination clauses and usually require payment of a fee. Since many of the commitments may expire without being completely drawn upon, the total commitment amounts do not necessarily represent future cash requirements. We evaluate each customer's creditworthiness on a case-by-case basis.

At December 31, 2020 and 2019, we had unfunded lines of credit and undisbursed construction loan funds totaling $355.3 million and $324.8 million, respectively. Virtually all of our unfunded lines of credit and undisbursed construction loan funds are variable rate.

Allowance For Credit Losses - Off-Balance-Sheet Credit Exposures

The allowance for credit losses on off-balance-sheet credit exposures is a liability account, calculated in accordance with ASC 326, representing expected credit losses over the contractual period for which we are exposed to credit risk resulting from a contractual obligation to extend credit. No allowance is recognized if we have the unconditional right to cancel the obligation. Off-balance-sheet credit exposures primarily consist of amounts available under outstanding lines of credit and letters of credit detailed above. For the period of exposure, the estimate of expected credit losses considers both the likelihood that funding will occur and the amount expected to be funded over the estimated remaining life of the commitment or other off-balance-sheet exposure. The likelihood and expected amount of funding are based on historical utilization rates. The amount of the allowance represents management's best estimate of expected credit losses on

commitments expected to be funded over the contractual life of the commitment. Estimating credit losses on amounts expected to be funded uses the same methodology as described for loans in Note 3 - Loans and Allowance, as if such commitments were funded.

Item 7A. Quantitative and Qualitative Disclosures about Market Risk

This information is incorporated herein by reference from “Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations” of this Annual Report on Form 10-K.

Item 8. Financial Statements and Supplementary Data

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Shareholders and the Board of Directors
Southern National Bancorp of Virginia, Inc.

Opinion on the Consolidated Financial Statements

We have audited the accompanying consolidated balance sheets of Southern National Bancorp of Virginia, Inc. (the "Company") as of December 31, 2020 and 2019, the related consolidated statements of income and comprehensive income, changes in stockholders' equity, and cash flows, for each of the three years in the period ended December 31, 2020, and the related notes (collectively referred to as the "financial statements"). In our opinion, based on our audits and the report of the other auditors, the financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2020 and 2019, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2020, in conformity with U.S. generally accepted accounting principles.

We did not audit the financial statements of Southern Trust Mortgage, LLC ("STM") as of and for the year ended December 31, 2020. STM, an affiliate of the Company, is accounted for as an equity method investment. The Company's financial statements for the year ended December 31, 2020 reported an equity gain from mortgage affiliate totaling $10.8 million, or approximately 36% of the Company's income before income taxes. STM's financial statements were audited by other auditors whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for STM, is based solely on the report of the other auditors.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) ("PCAOB"), the Company's internal control over financial reporting as of December 31, 2020, based on criteria established in *Internal Control - Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated March 16, 2021 expressed an unqualified opinion thereon.

Adoption of New Accounting Standard

As discussed in Note 1 to the financial statements, the Company changed its method of accounting for credit losses effective January 1, 2020 due to the adoption of Accounting Standards Codification (ASC) Topic 326, *Financial Instruments – Credit Losses*.

Basis for Opinion

These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the Company's financial statements based on our audits. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud.

Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits and the report of the other auditors provide a reasonable basis for our opinion.

Critical Audit Matters

The critical audit matters communicated below are matters arising from the current period audit of the financial statements that were communicated or required to be communicated to the audit committee and that: (1) relate to accounts or disclosures that are material to the financial statements and (2) involved our especially challenging, subjective, or complex judgments. The communication of critical audit matters does not alter in any way our opinion on the financial statements, taken as a whole, and we are not, by communicating the critical audit matter(s) below, providing separate opinions on the critical audit matters or on the accounts or disclosures to which they relate.

Allowance for Credit Losses

As described in Notes 1 and 3 to the financial statements, the Company's allowance for credit losses was $36.3 million at December 31, 2020. As further described in Notes 1 and 3, the Company adopted ASC Topic 326 *Financial Instruments – Credit Losses* as of January 1, 2020.

The Company's allowance for credit losses ("ACL") is measured on a pooling basis when similar risk characteristics exist, and by individually evaluating loans that do not share similar risk characteristics. The Company measures the ACL using a combination of probability of default (PD), probability of attrition (PA), loss given default (LGD), and exposure at default (EAD), calculated based on the application of historical loss experience, and adjusted for a reasonable and supportable forecast. Estimates are qualitatively adjusted for risk factors that are not considered within the quantitative modeling process. Estimating an appropriate allowance requires management to make numerous assumptions about losses that will occur over the remaining contractual life of loans recorded as of the balance sheet date. The most significant judgments in the ACL as of December 31, 2020 include the determination of a reasonable and supportable forecast and the impact of qualitative factors.

We identified the ACL as a critical audit matter. The principal considerations for our determination of the ACL as a critical audit matter included the high degree of judgment and subjectivity relating to management's determination of reasonable and supportable forecasts and the identification and measurement of the qualitative factors. In turn, auditing management's judgments regarding credit loss estimates and assumptions, specifically the determination of reasonable and supportable forecasts and qualitative factors involved a high degree of subjectivity and an increased extent of audit effort.

The primary procedures we performed to address this critical audit matter included:

- Tested the design and operating effectiveness of controls relating to management's determination of the ACL, including controls relating to the:
  - Completeness and accuracy of input into the model used to determine the ACL.
  - Performance of an independent model validation and appropriate responses to any findings.
  - The determination of a reasonable and supportable forecast.
  - The determination of qualitative factors.
- We evaluated management's application of qualitative adjustments, including testing the accuracy of the supporting calculations, evaluating whether the qualitative factors appropriately addressed risks that were not fully accounted for in the quantitative ACL component of the methodology, and evaluating the appropriateness and level of the qualitative factor adjustments.

- We evaluated management’s determination of a reasonable and supportable forecast, including testing the application of the forecast in quantitative ACL calculation. We also utilized our internal specialists to assist us in testing the application of the forecast to the ACL calculation.

Goodwill Impairment Assessment

As described in Notes 1 and 7 to the financial statements, the Company’s goodwill balance was $101.9 million at December 31, 2020, which is allocated to the Company’s reporting units. Goodwill is tested for impairment at least annually at the reporting unit level. The determination of the fair value of the reporting units requires management to make significant estimates and assumptions in determining the appropriate valuation methodology and key inputs to the selected methodology.

We identified the Company’s goodwill impairment assessment as a critical audit matter. Management makes estimates and assumptions for each reporting unit. As a result, auditing the reasonableness of management’s significant estimates and assumptions involves a higher degree of judgment and subjectivity.

The primary procedures we performed to address this critical audit matter included:

- We tested the design and operating effectiveness of controls relating to management’s goodwill impairment test, including the evaluation of key assumptions used in the quantitative assessment of the fair value, particularly the selection of a peer group and the control premium incorporated into the methodologies used to determine fair value of the reporting units.
- We tested key financial data used within the valuation to supporting evidence.
- We evaluated, with the assistance of our internal valuation specialists, appropriateness of valuation methodologies, the selection of a control premium and of a peer group, and the overall reasonableness of the estimated fair value of the reporting units.

/s/ Dixon Hughes Goodman LLP

We have served as the Company's auditor since 2013.

Greenville, NC
March 16, 2021

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Shareholders and the Board of Directors
Southern National Bancorp of Virginia, Inc.

Opinion on Internal Control Over Financial Reporting

We have audited Southern National Bancorp of Virginia, Inc.'s (the "Company")'s internal control over financial reporting as of December 31, 2020, based on criteria established in *Internal Control—Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission. In our opinion, Southern National Bancorp of Virginia, Inc. maintained, in all material respects, effective internal control over financial reporting as of December 31, 2020, based on criteria established in *Internal Control—Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) ("PCAOB"), the consolidated financial statements of Southern National Bancorp of Virginia, Inc. as of December 31, 2020 and 2019, and for each of the three years in the period ended December 31, 2020, and our report dated March 16, 2021, expressed an unqualified opinion on those consolidated financial statements.

Basis for Opinion

The Company's management is responsible for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audit in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

Definition and Limitations of Internal Control Over Financial Reporting

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ Dixon Hughes Goodman LLP

Greenville, NC
March 16, 2021

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors
Southern Trust Mortgage, LLC
Virginia Beach, Virginia

Opinion on the Financial Statements

We have audited the accompanying balance sheets of Southern Trust Mortgage, LLC (the Company) as of December 31, 2020 and 2019, and the related statements of operations, changes in members′ equity, and cash flows for each of the three years in the period ended December 31, 2020, and the related notes (collectively, referred to as the financial statements). In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company at December 31, 2020 and 2019, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2020, in conformity with accounting principles generally accepted in the United States of America.

Basis for Opinion

These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the Company's financial statements based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (PCAOB) and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. As part of our audits we are required to obtain an understanding of internal control over financial reporting 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.

Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

Critical Audit Matters

Critical audit matters are matters arising from the current period audit of the financial statements that were communicated or required to be communicated to the audit committee and that: (1) relate to accounts or disclosures that are material to the financial statements and (2) involved our especially challenging, subjective, or complex judgements. We determined that there are no critical audit matters.

/s/ Richey, May & Co., LLP.

We have served as Southern Trust Mortgage, LLC's auditor since 2014.

Englewood, Colorado
March 12, 2021

SOUTHERN NATIONAL BANCORP OF VIRGINIA, INC.
CONSOLIDATED BALANCE SHEETS
(dollars in thousands, except per share amounts)

	December 31, 2020	December 31, 2019
ASSETS		
Cash and cash equivalents:		
Cash and due from financial institutions	$ 8,585	$ 7,909
Interest-bearing deposits in other financial institutions	187,600	24,019
Total cash and cash equivalents	196,185	31,928
Securities available for sale, at fair value	153,233	164,820
Securities held to maturity, at amortized cost (fair value of $41,832 and $72,666, respectively)	40,721	72,448
Total loans	2,440,496	2,186,047
Less allowance for credit losses	(36,345)	(10,261)
Net loans	2,404,151	2,175,786
Stock in Federal Reserve Bank (FRB) and Federal Home Loan Bank (FHLB)	16,927	17,832
Equity method investment in mortgage affiliate	12,652	5,020
Preferred investment in mortgage affiliate	3,305	3,305
Bank premises and equipment, net	30,306	31,184
Operating lease right-of-use assets	7,511	8,013
Goodwill	101,954	101,954
Core deposit intangibles, net	5,826	7,191
Bank-owned life insurance	65,409	63,850
Other real estate owned	3,078	6,224
Deferred tax assets, net	14,646	11,788
Accrued interest receivable	19,998	8,210
Other assets	12,771	12,617
Total assets	$ 3,088,673	$ 2,722,170
LIABILITIES AND STOCKHOLDERS' EQUITY		
Noninterest-bearing demand deposits	$ 440,674	$ 339,153
Interest-bearing deposits:		
NOW accounts	714,752	391,172
Money market accounts	603,318	466,867
Savings accounts	183,814	144,486
Time deposits	490,048	783,040
Total interest-bearing deposits	1,991,932	1,785,565
Total deposits	2,432,606	2,124,718
Securities sold under agreements to repurchase - short term	16,065	12,883
FHLB advances	100,000	121,640
Junior subordinated debt - long term	9,682	9,632
Senior subordinated notes - long term	105,647	47,051
Operating lease liabilities	8,238	8,469
Other liabilities	25,881	20,536
Total liabilities	2,698,119	2,344,929
Commitments and contingencies (See Note 14)		
Stockholders' equity:		
Preferred stock, $0.01 par value. Authorized 5,000,000 shares; no shares issued and outstanding	—	—
Common stock, $0.01 par value. Authorized 45,000,000 shares; 24,368,612 and 24,181,534 shares issued and outstanding at December 31, 2020 and December 31, 2019, respectively	243	241
Additional paid in capital	308,870	306,755
Retained earnings	77,956	69,462
Accumulated other comprehensive income	3,485	783
Total stockholders' equity	390,554	377,241
Total liabilities and stockholders' equity	$ 3,088,673	$ 2,722,170

See accompanying notes to consolidated financial statements.

SOUTHERN NATIONAL BANCORP OF VIRGINIA, INC.
CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME
(dollars in thousands, except per share amounts)

	For the Years Ended December 31,		
	2020	2019	2018
Interest and dividend income:			
Interest and fees on loans	$ 111,647	$ 112,181	$ 110,213
Interest and dividends on taxable securities	4,244	5,639	5,752
Interest and dividends on tax exempt securities	486	585	634
Interest and dividends on other earning assets	1,402	2,119	2,308
Total interest and dividend income	117,779	120,524	118,907
Interest expense:			
Interest on deposits	20,332	30,602	18,235
Interest on FRB borrowings	424	—	—
Interest on repurchase agreements	96	87	97
Interest on junior subordinated debt	426	589	575
Interest on senior subordinated notes	3,909	2,847	2,847
Interest on other borrowings	952	2,799	6,087
Total interest expense	26,139	36,924	27,841
Net interest income	91,640	83,600	91,066
Provision for credit losses	19,450	350	4,200
Net interest income after provision for credit losses	72,190	83,250	86,866
Noninterest income:			
Account maintenance and deposit service fees	6,520	7,159	5,959
Income from bank-owned life insurance	1,559	1,699	1,983
Equity gain (loss) from mortgage affiliate	10,789	1,191	(894)
Realized losses on sales of investment securities	(620)	—	—
Recoveries related to acquired charged-off loans and investment securities	6,500	1,537	2,610
Other	703	1,000	541
Total noninterest income	25,451	12,586	10,199
Noninterest expenses:			
Salaries and benefits	36,675	26,261	27,706
Occupancy expenses	6,142	6,204	6,628
Furniture and equipment expenses	2,725	2,719	2,795
Amortization of core deposit intangible	1,364	1,418	1,445
Virginia franchise tax expense	2,457	2,251	1,839
Data processing expense	3,178	2,381	1,885
Telephone and communication expense	1,497	1,615	2,035
Net (gain) loss on other real estate owned	960	(38)	360
Professional fees	4,726	3,612	1,644
Other operating expenses	8,016	10,169	7,423
Total noninterest expenses	67,740	56,592	53,760
Income before income taxes	29,901	39,244	43,305
Income tax expense	6,614	6,077	9,614
Net income	$ 23,287	$ 33,167	$ 33,691
Other comprehensive income:			
Unrealized gain (loss) on available for sale securities	$ 2,789	$ 4,256	$ (1,548)
Reclassification of loss on sales of investment securities	620	—	—
Accretion of amounts previously recorded upon transfer to held to maturity from available for sale	12	13	16
Net unrealized gain (loss)	3,421	4,269	(1,532)
Tax effect	719	897	(324)
Other comprehensive income (loss)	2,702	3,372	(1,208)
Comprehensive income	$ 25,989	$ 36,539	$ 32,483
Earnings per share, basic	$ 0.96	$ 1.38	$ 1.40
Earnings per share, diluted	$ 0.96	$ 1.36	$ 1.39

See accompanying notes to consolidated financial statements.

SOUTHERN NATIONAL BANCORP OF VIRGINIA, INC.
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY
FOR THE YEARS ENDED DECEMBER 31, 2020, 2019 AND 2018
(dollars in thousands, except per share amounts)

	Common Stock	Additional Paid in Capital	Retained Earnings	Accumulated Other Comprehensive (Loss) Income	Total
Balance - December 31, 2017	**$ 239**	**$ 304,932**	**$ 18,753**	**$ (1,152)**	**$ 322,772**
Reclassification adjustment from accumulated other comprehensive income to retained earnings for adoption of ASU 2018-02			229	(229)	—
Adjusted beginning balance	239	304,932	18,982	(1,381)	322,772
Net income	—	—	33,691	—	33,691
Changes in other comprehensive loss on investment securities (net of tax, $(324))	—	—	—	(1,208)	(1,208)
Dividends on common stock ($0.32 per share)	—	—	(7,688)	—	(7,688)
Issuance of common stock under Stock Incentive Plan	1	442	—	—	443
Stock-based compensation expense	—	280	—	—	280
Balance - December 31, 2018	**$ 240**	**$ 305,654**	**$ 44,985**	**$ (2,589)**	**$ 348,290**
Net income	—	—	33,167	—	33,167
Changes in other comprehensive income on investment securities (net of tax, $897)	—	—	—	3,372	3,372
Dividends on common stock ($0.36 per share)	—	—	(8,690)	—	(8,690)
Issuance of common stock under Stock Incentive Plan	1	669	—	—	670
Stock-based compensation expense	—	432	—	—	432
Balance - December 31, 2019	**$ 241**	**$ 306,755**	**$ 69,462**	**$ 783**	**$ 377,241**
Impact of adoption of ASU 2016-13	—	—	(5,056)	—	(5,056)
Adjusted beginning balance	241	306,755	64,406	783	372,185
Net income	—	—	23,287	—	23,287
Changes in other comprehensive income on investment securities (net of tax, $719)	—	—	—	2,702	2,702
Dividends on common stock ($0.40 per share)	—	—	(9,737)	—	(9,737)
Issuance of common stock under Stock Incentive Plan	1	708	—	—	709
Vesting of restricted stock	1	(1)	—	—	—
Repurchase of restricted stock	—	(135)	—	—	(135)
Stock-based compensation expense	—	1,543	—	—	1,543
Balance - December 31, 2020	**$ 243**	**$ 308,870**	**$ 77,956**	**$ 3,485**	**$ 390,554**

See accompanying notes to consolidated financial statements.

SOUTHERN NATIONAL BANCORP OF VIRGINIA, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(dollars in thousands)

	For the Year Ended December 31, 2020	2019	2018
Operating activities:			
Net income	$ 23,287	$ 33,167	$ 33,691
Adjustments to reconcile net income to net cash and cash equivalents provided by operating activities:			
Depreciation and amortization	5,285	5,632	7,403
Amortization of operating lease right-of-use assets	2,909	2,546	—
Accretion of loan discount	(4,346)	(3,859)	(4,534)
Amortization of FDIC indemnification asset	—	649	704
Provision for credit losses	19,450	350	4,200
Earnings on bank-owned life insurance	(1,559)	(1,565)	(1,633)
Equity (gain) loss on mortgage affiliate	(10,789)	(1,191)	894
Stock-based compensation expense	1,543	432	280
Loss on sales of investment securities	620	—	—
Gain on bank-owned life insurance death benefit	—	(134)	(350)
(Gain) loss on other real estate owned	960	(38)	360
Provision (benefit) for deferred income taxes	(1,618)	1,420	3,121
Net (increase) decrease in other assets	(11,942)	(2,203)	213
Net increase (decrease) in other liabilities	5,863	1,558	(2,909)
Net cash and cash equivalents provided by operating activities	29,663	36,764	41,440
Investing activities:			
Proceeds from sales of held to maturity investment securities	1,660	—	—
Proceeds from sales of available for sale investment securities	1,910	—	—
Purchases of held to maturity investment securities	(15,197)	(15,260)	—
Purchases of available for sale investment securities	(38,938)	(45,135)	—
Proceeds from paydowns, maturities and calls of available for sale investment securities	50,068	26,283	14,360
Proceeds from paydowns, maturities and calls of held to maturity investment securities	44,738	35,006	5,955
Net decrease of FRB and FHLB stock	905	1,690	7,253
Net increase in loans	(251,000)	(7,059)	(113,845)
Purchase of bank-owned life insurance	—	—	(12,000)
Proceeds from bank-owned life insurance death benefit	—	344	2,278
Sales of other real estate owned, net of improvements	2,663	214	2,140
Proceeds from sales of bank premise and equipment and assets held for sale	—	—	2,136
Purchases of bank premises and equipment	(1,082)	(1,101)	(1,973)
Net cash and cash equivalents used in investing activities	(204,273)	(5,018)	(93,696)
Financing activities:			
Net increase in deposits	307,888	27,129	231,671
Cash dividends paid on common stock	(9,737)	(8,690)	(7,688)
Issuance of common stock under Stock Incentive Plan	709	670	443
Repurchase of restricted stock	(135)	—	—
Issuance of subordinated notes, net of cost	58,600	—	—
Net decrease in other borrowings	(18,458)	(47,538)	(169,022)
Net cash and cash equivalents provided by (used in) financing activities	338,867	(28,429)	55,404
Increase in cash and cash equivalents	164,257	3,317	3,148
Cash and cash equivalents at beginning of period	31,928	28,611	25,463
Cash and cash equivalents at end of period	$ 196,185	$ 31,928	$ 28,611
Supplemental disclosure of cash flow information			
Cash payments for:			
Interest	$ 27,988	$ 36,002	$ 26,129
Income taxes	7,693	4,897	6,672
Supplemental schedule of noncash investing and financing activities:			
Transfer from loans to other real estate owned	477	1,323	—

See accompanying notes to consolidated financial statements.

1. ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES

Southern National Bancorp of Virginia, Inc. ("Southern National" or "SNBV" or the "Company") is a corporation that was formed on July 28, 2004 under the laws of the Commonwealth of Virginia and is the holding company for Sonabank ("Sonabank" or the "Bank") a Virginia state-chartered bank which commenced operations on April 14, 2005.

Sonabank provides a range of financial services to individuals and small and medium sized businesses. At December 31, 2020, Sonabank had forty-two full-service branches in Virginia and Maryland and through certain internet and mobile applications. Thirty-seven full-service retail branches are in Virginia, located in Ashland, Burgess, Callao, Central Garage, Charlottesville, Chester, Clifton Forge, Colonial Heights, Courtland, Deltaville, Fairfax, Front Royal, Gloucester, Gloucester Point, Hampton, Hartfield, Heathsville, Kilmarnock, Leesburg, McLean, Mechanicsville (2), Middleburg, Midlothian, New Market, Newport News, Quinton, Reston, Richmond, South Riding, Surry, Tappahannock (2), Urbanna, Warrenton, Waverly, and Williamsburg, and five full-service retail branches in Maryland, located in Bethesda, Brandywine, Owings, Rockville, and Upper Marlboro. We have administrative offices in Warrenton and Glen Allen, Virginia.

The accounting policies and practices of Southern National and its subsidiaries conform to U.S. generally accepted accounting principles ("U.S. GAAP") and to general practice within the banking industry. Major policies and practices are described below:

Principles of Consolidation

The consolidated financial statements include the accounts of Southern National and its subsidiaries Sonabank and EVB Statutory Trust I (the "Trust"). Significant inter-company accounts and transactions have been eliminated in consolidation. Southern National consolidates subsidiaries in which it holds, directly or indirectly, more than 50 percent of the voting rights or where it exercises control. Entities where Southern National holds 20 to 50 percent of the voting rights, or has the ability to exercise significant influence, or both, are accounted for under the equity method. Southern National owns the Trust which is an unconsolidated subsidiary and the junior subordinated debt owed to the Trust is reported as a liability of Southern National. In addition, Sonabank has an interest in one affiliate, Southern Trust Mortgage, LLC ("STM"). Sonabank owns 48.9% and 100% of STM's common and preferred stock, respectively. To comply with Regulation S-X, Rule 3-09, audited financial statements of STM as of and for the year ended December 31, 2020 are being filed with Southern National's Annual Report on Form 10-K as Exhibit 99.1.

Investments in Mortgage Affiliate

Sonabank's investment in STM's common stock is accounted for using the equity method. Under the equity method, the carrying value of Sonabank's investment in STM was originally recorded at cost but is adjusted periodically to record Sonabank's proportionate share of STM's earnings or losses through noninterest income and decreased by the amount of cash dividends or similar distributions received from STM. Our equity investment in STM as of December 31, 2020 and 2019 was $12.7 million and $5.0 million, respectively.

Sonabank's investment in STM's preferred stock is considered to be a non-marketable equity security that does not have a readily determinable fair value. Equity securities with no recurring market value data available are reviewed periodically and any observable market value change are adjusting through net income. Sonabank evaluated this non-marketable equity security for impairment and recoverability of the recorded investment by considering positive and negative evidence, including the profitability and asset quality of STM, dividend payment history and recent redemption experience. Impairment is assessed at each reporting period and if identified, is recognized in noninterest income. Our preferred investment in STM was $3.3 million as of December 31, 2020 and 2019.

Operating Segments

Operating segments are defined as components of a company about which separate financial information is available that is evaluated regularly by the chief operating decision maker in deciding how to allocate resources and in assessing

performance. The Company has determined it has one unconsolidated reportable segment, which consists of the Sonabank's investment in STM. Sonabank's share of equity in earnings (losses) from STM for the years ended December 31, 2020, 2019 and 2018 were $10.8 million, $1.2 million and $(894) thousand, respectively.

The chief operating decision maker evaluates segment performance based on STM's net income (loss). Net income (loss) was $22.2 million, $2.7 million and $(1.6) million for the years ended December 31, 2020, 2019 and 2018, respectively. The primary source of revenue for this segment is gains on sale of mortgage loans held for sale, net of direct costs. For the years ended December 31, 2020, 2019 and 2018, gains on sale of mortgage loans held for sale, net of direct costs were $107.1 million, $45.7 million and $27.2 million, respectively. In evaluating STM's net income (loss), the chief operating decision maker also assesses salaries, commissions and benefits, which were $84.1 million, $39.0 million and $24.6 million for the years ended December 31, 2020, 2019 and 2018, respectively.

Also, the chief operating decision maker evaluates segments performance based on STM's balance sheet. Total mortgage loans held for sale by STM were $143.4 million and $100.2 million as of December 31, 2020 and 2019, respectively. Warehouse lines of credit were $136.1 million and $92.1 million as of December 31, 2020 and 2019, respectively. STM's total members' equity was $26.4 million and $11.1 million as of December 31, 2020 and 2019.

Use of Estimates

The preparation of the consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from these estimates. Estimates that are particularly susceptible to change in the near term include: the determination of the allowance for credit losses (formerly the allowance for loan losses), the fair value of investment securities, credit impairment of investment securities, the valuation of goodwill, other real estate owned ("OREO") and deferred tax assets.

Investment Securities

Debt securities that Southern National has the positive intent and ability to hold to maturity are classified as held-to-maturity and carried at amortized cost.

Securities classified as available for sale are those debt securities that may be sold in response to changes in interest rates, liquidity needs or other similar factors. Securities available for sale are carried at fair value, with unrealized gains or losses net of deferred taxes, included in accumulated other comprehensive income (loss) in stockholders' equity.

Premiums and discounts are generally amortized using the interest method with a constant effective yield without anticipating prepayments, except for mortgage-backed securities where prepayments are anticipated. Premiums on callable securities are amortized to their earliest call date. Prior to the adoption of Financial Accounting Standards Board (FASB) Accounting Standards Update (ASU) 2017-08 in 2019, premiums and discounts were recognized in interest income using the interest method over the terms of the securities without anticipating prepayments, except for mortgage-backed securities where prepayments were anticipated. Gains and losses on the sale of investment securities are recorded on the settlement date and are determined using the specific identification method.

Southern National purchases amortizing investment securities in which the underlying assets are residential mortgage loans subject to prepayments. The actual principal reduction on these assets varies from the expected contractual principal reduction due to principal prepayments resulting from the borrowers' election to refinance the underlying mortgage based on market and other conditions. The purchased premiums and discounts associated with these assets are amortized or accreted to interest income over the estimated life of the related assets. The estimated life is calculated by projecting future prepayments and the resulting principal cash flows until maturity. Prepayment rate projections utilize actual prepayment speed experience and available market information on like-kind instruments. The prepayment rates form the basis for income recognition of premiums and discounts on the related assets. Changes in prepayment estimates may cause the earnings recognized on these assets to vary over the term that the assets are held, creating volatility in the

net interest margin. Prepayment rate assumptions are monitored and updated monthly to reflect actual activity and the most recent market projections.

Other investments include stock acquired for regulatory purposes. The Bank is a member of the FHLB system. Members are required to own a certain amount of stock based on the level of borrowings and other factors, and may invest in additional amounts. The Bank is also required to own FRB stock with a par value equal to 6% of capital and FHLB stock of 4.25% of borrowings outstanding. FHLB and FRB stock are carried at cost, classified as a restricted security, and periodically evaluated for impairment based on ultimate recovery of par value. Both cash and stock dividends are reported as income.

Loans

Southern National provides mortgage loans purchased from STM, commercial and consumer loans to customers. A substantial portion of the loan portfolio is represented by loans secured by real estate throughout its market area. The ability of Southern National's debtors to honor their contracts is in varying degrees dependent upon the real estate market conditions and general economic conditions in this area.

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 the allowance for credit losses, purchased premiums and discounts and any deferred loan 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 the interest method without anticipating prepayments.

Commercial real estate consists of borrowings secured by owner occupied and non-owner occupied commercial real estate. Repayment of these loans is dependent upon rental income or the subsequent sale of the property for loans secured by non-owner occupied commercial real estate and by cash flows from business operations for owner occupied commercial real estate. Loans for which the source of repayment is rental income are primarily impacted by local economic conditions which dictate occupancy rates and the amount of rent charged. Commercial real estate loans that are dependent on cash flows from operations can also be adversely affected by current market conditions for their product or service.

Construction and land development primarily consist of borrowings to purchase and develop raw land into residential and non-residential properties. Construction loans are extended to individuals as well as corporations for the construction of an individual or multiple properties and are secured by raw land and the subsequent improvements. Repayment of the loans to real estate developers is dependent upon the sale or lease of properties to third parties in a timely fashion upon completion. Should there be delays in construction or a downturn in the market for those properties, there may be significant erosion in value which may be absorbed by Southern National.

Commercial loans consist of borrowings for commercial purposes to individuals, corporations, partnerships, sole proprietorships, and other business enterprises. Commercial loans are generally secured by business assets such as equipment, accounts receivable, inventory, or any other asset excluding real estate and generally made to finance capital expenditures or operations. Southern National's risk exposure is related to deterioration in the value of collateral securing the loan should foreclosure become necessary. Generally, business assets used or produced in operations do not maintain their value upon foreclosure which may require Southern National to write-down the value significantly to sell.

Residential real estate loans consist of loans to individuals for the purchase of primary residences with repayment primarily through wage or other income sources of the individual borrower. Southern National's loss exposure to these loans is dependent on local market conditions for residential properties as loan amounts are determined, in part, by the fair value of the property at origination.

STM is a regional mortgage banking company headquartered in Virginia Beach, Virginia that has mortgage banking originators in Delaware, Virginia, Maryland, North Carolina and South Carolina. STM only originates retail mortgage products.

Sonabank has established underwriting guidelines with STM under which it will purchase residential construction, construction loans that convert to permanent, and permanent loans primarily in its Virginia and Maryland footprint from STM. These will typically be loans that do not conform to FNMA or FHLMC standards because of size or acreage.

Other consumer loans are comprised of loans to individuals both unsecured and secured and home equity loans secured by real estate (closed and open-end), with repayment dependent on individual wages and other income. The risk of loss on consumer loans is elevated as the collateral securing these loans, if any, rapidly depreciate in value or may be worthless and/or difficult to locate if repossession is necessary. Losses in this portfolio are generally relatively low, however, due to the small individual loan size and the balance outstanding as a percentage of Southern National’s entire portfolio.

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

All interest accrued but not collected for loans that are placed on nonaccrual status 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 status. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

Most of Southern National’s business activity is with customers located within Virginia and Maryland. Therefore, our exposure to credit risk is significantly affected by changes in the economy in those areas. We are not dependent on any single customer or group of customers whose insolvency would have a material adverse effect on operations.

Southern National has purchased, primarily through acquisitions, individual loans and groups of loans, some of which have shown evidence of credit deterioration since origination. These purchased loans are recorded at fair value such that there is no carryover of the seller’s allowance for credit losses. We adopted ASU 2016-13, Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments, on January 1, 2020 which now requires us to record purchased financial assets with credit deterioration (PCD assets), defined as a more-than-insignificant deterioration in credit quality since origination or issuance, at the purchase price plus the allowance for credit losses expected at the time of acquisition. Under this method, there is no credit loss expense affecting net income on acquisition of PCD assets. Changes in estimates of expected credit losses after acquisition are recognized as credit loss expense (or reversal of credit loss expense) in subsequent periods as they arise. Any non-credit discount or premium resulting from acquiring a pool of purchased financial assets with credit deterioration shall be allocated to each individual asset. At the acquisition date, the initial allowance for credit losses determined on a collective basis shall be allocated to individual assets to appropriately allocate any non-credit discount or premium. The non-credit discount or premium, after the adjustment for the allowance for credit losses, shall be accreted to interest income using the interest method based on the effective interest rate determined after the adjustment for credit losses at the adoption date.

A purchased financial asset that does not qualify as a PCD asset is accounted for similar to an originated financial asset. Generally, this means that an entity recognizes the allowance for credit losses for non-PCD assets through net income at the time of acquisition. In addition, both the credit discount and non-credit discount or premium resulting from acquiring a pool of purchased financial assets that do not qualify as PCD assets shall be allocated to each individual asset. This combined discount or premium shall be accreted to interest income using the effective yield method.

Allowance for Credit Losses (“ACL”)

As further discussed below, we adopted ASU 2016-13, Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments, on January 1, 2020. Accounting Standards Codification (“ASC”) Topic 326 (“ASC 326”) replaced the previous “incurred loss” model for measuring credit losses, which encompassed allowances for current known and inherent losses within the portfolio, with an “expected loss” model, which encompasses allowances for losses expected to be incurred over the life of the portfolio. The new current expected credit loss (“CECL”) model requires the measurement of all expected credit losses for financial assets measured at amortized cost and certain off-balance-sheet credit exposures based on historical experience, current conditions, and

reasonable and supportable forecasts. In connection with the adoption of ASC 326, we revised certain accounting policies and implemented certain accounting policy elections. The revised accounting policies are described below.

Allowance For Credit Losses - Held-to-Maturity Securities

The allowance for credit losses on held-to-maturity securities is a contra-asset valuation account, calculated in accordance with ASC 326 that is deducted from the amortized cost basis of held-to-maturity securities to present management's best estimate of the net amount expected to be collected. Held-to-maturity securities are charged-off against the allowance when deemed uncollectible by management. Adjustments to the allowance are reported in our income statement as a component of credit loss expense. Management measures expected credit losses on held-to-maturity securities on a collective basis by major security type with each type sharing similar risk characteristics and considers historical credit loss information that is adjusted for current conditions and reasonable and supportable forecasts. Management has made the accounting policy election to exclude accrued interest receivable on held-to-maturity securities from the estimate of credit losses. Further information regarding our policies and methodology used to estimate the allowance for credit losses on held-to-maturity securities is presented in Note 2 – Investment Securities.

Allowance For Credit Losses - Available-for-Sale Securities

For available-for-sale securities in an unrealized loss position, we first assess whether (i) we intend to sell or (ii) it is more likely than not that we will be required to sell the security before recovery of its amortized cost basis. If either case is affirmative, any previously recognized allowances are charged-off and the security's amortized cost is written down to fair value through income. If neither case is affirmative, the security is evaluated to determine whether the decline in fair value has resulted from credit losses or other factors. In making this assessment, management considers the extent to which fair value is less than amortized cost, any changes to the rating of the security by a rating agency and any adverse conditions specifically related to the security, among other factors. If this assessment indicates that a credit loss exists, the present value of cash flows expected to be collected from the security are compared to the amortized cost basis of the security. If the present value of cash flows expected to be collected is less than the amortized cost basis, a credit loss exists and an allowance for credit losses is recorded for the credit loss, limited by the amount that the fair value is less than the amortized cost basis. Any impairment that has not been recorded through an allowance for credit losses is recognized in other comprehensive income. Adjustments to the allowance are reported in our income statement as a component of credit loss expense. Management has made the accounting policy election to exclude accrued interest receivable on available-for-sale securities from the estimate of credit losses. Available-for-sale securities are charged-off against the allowance or, in the absence of any allowance, written down through income when deemed uncollectible by management or when either of the aforementioned criteria regarding intent or requirement to sell is met.

Prior to the adoption of ASU 2016-13, declines in the fair value of held-to-maturity and available-for-sale securities below their cost that were deemed to be other than temporary were reflected in earnings as realized losses. In estimating other-than-temporary impairment losses prior to January 1, 2020, management considered, among other things, (i) the length of time and the extent to which the fair value had been less than cost, (ii) the financial condition and near-term prospects of the issuer and (iii) the intent and our ability to retain our investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value.

Allowance for Credit Losses – Loans

The allowance for credit losses on loans is a contra-asset valuation account, calculated in accordance with ASC 326, which is deducted from the amortized cost basis of loans to present management's best estimate of the net amount expected to be collected. Loans are charged-off against the allowance when deemed uncollectible by management. Expected recoveries do not exceed the aggregate of amounts previously charged-off and expected to be charged-off. Adjustments to the allowance are reported in our income statement as a component of credit loss expense. Management has made the accounting policy election to exclude accrued interest receivable on loans from the estimate of credit losses. Further information regarding our policies and methodology used to estimate the allowance for credit losses on loans is presented in Note 3 – Loans and Allowance.

Prior to the adoption of ASU 2016-13, the allowance for loan losses on loans was a contra-asset valuation account established through a provision for loan losses charged to expense, which represented management's best estimate of inherent losses that had been incurred within the existing portfolio of loans. The allowance for loan losses on loans included allowance allocations calculated in accordance with ASC Topic 310, "Receivables" and allowance allocations calculated in accordance with ASC Topic 450, "Contingencies."

Allowance For Credit Losses - Off-Balance-Sheet Credit Exposures

The allowance for credit losses on off-balance-sheet credit exposures is a liability account, calculated in accordance with ASC 326, representing expected credit losses over the contractual period for which we are exposed to credit risk resulting from a contractual obligation to extend credit. No allowance is recognized if we have the unconditional right to cancel the obligation. The allowance is reported as a component of accrued interest payable and other liabilities in our consolidated balance sheets. Adjustments to the allowance are reported in our income statement as a component of credit loss expense. Further information regarding our policies and methodology used to estimate the allowance for credit losses on off-balance-sheet credit exposures is presented in Note 14 – Financial Instruments with Off-Balance-Sheet Risks.

As discussed above, effective January 1, 2020 we adopted the provisions of ASC 326 using the modified retrospective method for all financial assets measured at amortized cost and off-balance-sheet credit exposures. Upon adoption, we recognized an after-tax cumulative effect reduction to retained earnings totaling $5.1 million, as detailed in the table below. Operating results for periods after January 1, 2020 are presented in accordance with ASC 326 while prior period amounts continue to be reported in accordance with previously applicable standards and the accounting policies.

The following table details the impact of the adoption of ASC 326 on the allowance for credit losses as of January 1, 2020 (in thousands):

	Pre-Adoption Allowance	Impact of Adoption	Post-Adoption Allowance	After-tax Cumulative Effect On Retained Earnings
Securities Held To Maturity:				
Obligations of states and political subdivisions	$ —	$ (1)	$ (1)	$ —
Total	$ —	$ (1)	$ (1)	$ —
Loans:				
Commercial real estate - owner occupied	$ 810	$ 1,704	$ 2,514	$ (994)
Commercial real estate - non-owner occupied [1]	1,720	2,706	4,426	(1,578)
Construction and land development	683	674	1,357	(393)
Commercial loans	5,418	(3,246)	2,172	1,893
Paycheck Protection Program loans	—	—	—	-
Residential 1-4 family [2]	1,266	4,169	5,435	(2,431)
Other consumer loans	190	187	377	(109)
PCD Loans	—	2,272	2,272	(1,325)
Unallocated	174	(174)	—	101
Total loans	$ 10,261	$ 8,292	$ 18,553	$ (4,836)
Off-Balance Sheet Exposures	$ —	$ 360	$ 360	$ (220)

(1) Includes loans secured by farmland and multi-family residential loans.
(2) Includes home equity lines of credit.

Transfers of Financial Assets

Transfers of financial assets are accounted for as sales, when control over the assets has been relinquished. Control over transferred assets is deemed to be surrendered when the assets have been isolated from Southern National, the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange

the transferred assets, and Southern National does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

Bank Premises and Equipment

Land is carried at cost. Premises and equipment are stated at cost less accumulated depreciation. Buildings and related components are depreciated using the straight-line method with useful lives of 30 years. Leasehold improvements are amortized on the straight-line method over the shorter of the estimated useful lives of the improvements or the terms of the related leases including lease renewals only when the Company is reasonably assured of the aggregate term of the lease. Furniture, fixtures and equipment are depreciated using the straight-line method with useful lives ranging from 3 to 10 years.

Operating Leases

The Company leases certain properties and equipment under operating leases. The Company recognizes a liability to make lease payments, the operating lease liability, and an asset representing the right to use the underlying asset during the lease term, the right-of-use asset. In recognizing lease right-of-use assets and related right-of-use liabilities, we account for lease and non-lease components (such as taxes, insurance, and common area maintenance costs) separately as such amounts are generally readily determinable under our lease contracts. The operating lease liability is measured at the present value of the remaining lease payments, discounted at the Company’s incremental borrowing rate at inception. The right-of-use asset is measured at the amount of the operating lease liability adjusted for the remaining balance of any lease incentives received, any cumulative prepaid or accrued rent if the lease payments are uneven throughout the lease term, any unamortized initial direct costs, and any impairment of the right-of-use-asset. Lease expense consists of a single lease cost calculated so that the remaining cost of the lease is allocated over the remaining lease term on a straight-line basis, variable lease payments not included in the operating lease liability, and any impairment of the right-of-use asset. Lease renewal options are generally not included in the calculation of the operating lease liabilities, unless they are not reasonably certain to be exercised. The Company does not recognize short-term leases on the balance sheet.

Goodwill and Intangible Assets

Goodwill resulting from business combinations after January 1, 2009, is generally determined as the excess of the fair value of the consideration transferred, plus the fair value of any noncontrolling interests in the acquiree, over the fair value of the net assets acquired and liabilities assumed as of the acquisition date. Goodwill and intangible assets acquired in a business combination and determined to have an indefinite useful life are not amortized, but evaluated for impairment on an annual basis or more frequently if events or circumstances warrant. Intangible assets with definite useful lives are amortized over their estimated useful lives to their estimated residual values. Goodwill is the only intangible asset with an indefinite life on our balance sheet.

In response to the effects of COVID-19, management determined there to be a triggering event in the third quarter of 2020 warranting a goodwill assessment. For the third quarter 2020 assessment, we performed a step one quantitative assessment to determine if the fair value of all our reporting units was less than its carrying amount. We concluded that the fair value of all our reporting units exceeded its carrying amount and no impairment was present based on management’s assessment.

Other intangible assets consist of loan servicing rights and core deposit intangible assets arising from whole-bank and branch acquisitions and are amortized over their estimated useful lives, which range from 6 to 15 years.

Stock Based Compensation

Compensation cost is recognized for stock options issued to employees, based on the fair value of these awards at the date of grant. A Black-Scholes option-pricing model is utilized to estimate the fair value of stock options. Compensation cost for grants of restricted shares is accounted for based on the closing price of Southern National’s common stock on the date the restricted shares are awarded. Compensation cost for stock options and restricted shares is recognized over

the required service period, generally defined as the vesting period. For awards with graded vesting, compensation cost is recognized on a straight-line basis over the requisite service period for the entire award.

Bank-Owned Life Insurance

Southern National has purchased, and acquired through acquisitions, life insurance policies on certain former and current key executives. Bank-owned life insurance is recorded at the amount that can be realized under the insurance contract at the balance sheet date, which is the cash surrender value adjusted for other charges or other amounts due that are probable at settlement.

Other Real Estate Owned ("OREO")

Real estate acquired through or instead of foreclosure is held for sale and initially recorded at fair value less costs to sell when acquired, establishing a new cost basis. If fair value declines subsequent to foreclosure, a direct charge-off is recorded through expense. Operating costs after acquisition are expensed as incurred.

Impairment of Long-Lived Assets

Premises and equipment, core deposit intangible assets, right of use assets, and other long-term assets are reviewed for impairment when events indicate their carrying amount may not be recoverable from future undiscounted cash flows. If impaired, the assets are recorded at fair value.

Retirement Plans

Employee 401(k) plan expense is the amount of matching contributions. Supplemental retirement plan expense allocates the benefits over years of service.

Loss Contingencies

Loss contingencies, including claims and legal actions arising in the ordinary course of business, are recorded as liabilities when the likelihood of loss is probable and an amount or range of loss can be reasonably estimated. Management does not believe there are such matters that will have a material effect on the financial statements.

Dividend Restriction

Banking regulations require maintaining certain capital levels and may limit the dividends paid by the Bank to Southern National or by Southern National to shareholders.

Estimates and Uncertainties

Estimates including the carrying value of investment securities, other than temporary impairment of investment securities, the determination of the allowance for credit losses and the valuation of goodwill and intangible assets involves uncertainties and matters of significant judgement regarding interest rates, credit risk, repayments and prepayments, and other factors, especially in the absence of broad markets for particular items. Changes in assumptions or in market conditions could significantly affect the estimates.

Advertising Costs

Advertising costs are expensed as incurred.

Income Taxes

Income tax expense is the total of the current year income tax due or refundable and the change in deferred tax assets and liabilities. Deferred tax assets and liabilities are the expected future tax amounts for the temporary differences between carrying amounts and tax bases of assets and liabilities, computed using enacted tax rates. A valuation allowance, if needed, reduces deferred tax assets to the amount expected to be realized.

A tax position is recognized as a benefit only if it is “more likely than not” that the tax position would be sustained in a tax examination, with a tax examination being presumed to occur. The amount recognized is the largest amount of tax benefit that is greater than 50% likely of being realized on examination. For tax positions not meeting the “more likely than not” test, no tax benefit is recorded. We have no unrecognized tax benefits and do not anticipate any increase in unrecognized tax benefits during the next twelve months. Should the accrual of any interest or penalties relative to unrecognized tax benefits be necessary, it is our policy to record such accruals in our income tax accounts; no such accruals exist as of December 31, 2020 and 2019. Southern National and its subsidiaries file a consolidated U.S. federal tax return; Sonabank files a Maryland state income tax return and Southern National files a franchise tax return. These returns are subject to examination by taxing authorities for all years after 2017.

Restrictions on Cash

No regulatory reserve or clearing requirements with the FRB were needed at December 31, 2020 and 2019.

Consolidated Statements of Cash Flows

For purposes of reporting cash flows, Southern National defines cash and cash equivalents as cash due from financial institutions, interest-bearing deposits and federal funds sold in other financial institutions with maturities less than 90 days. Net cash flows are reported for customer loan and deposit transactions and short-term borrowings.

Earnings Per Share (“EPS”)

Basic EPS is computed by dividing net income by the weighted average number of common shares outstanding during the year. Diluted EPS reflects additional common shares that would have been outstanding if dilutive potential common shares had been issued, as well as any adjustment to net income that would result from the assumed issuance. Potential common shares that may be issued by Southern National relate solely to outstanding stock options and warrants and are determined using the treasury stock method.

Comprehensive Income

Comprehensive income consists of net income and other comprehensive (loss) income. Other comprehensive (loss) income includes unrealized gains and losses on investment securities available for sale and the non-credit component of other than temporary impairment of investment securities held-to-maturity which are also recognized as a separate component of equity.

Off Balance Sheet Credit Related Financial Instruments

In the ordinary course of business, Southern National has entered into commitments to extend credit, standby letters of credit, and guarantees of previously sold credit card accounts. The face amount for these items represents the exposure to loss, before considering customer collateral or ability to repay.

Fair Value Measurements

In general, fair values of financial instruments are based upon quoted market prices, where available. If such quoted market prices are not available, fair value is based upon observable market-based parameters. Valuation assumptions may be made to ensure that financial instruments are recorded at fair value. These assumptions may reflect assumptions

that market participants would use in pricing an asset or liability, among other things, as well as unobservable parameters. Any such valuation assumptions are applied consistently over time.

Recent Accounting Pronouncements

New Accounting Standards Adopted:

In August 2018, FASB issued ASU 2018-13, *Fair Value Measurement (Topic 820)*. This ASU adds, eliminates and modifies certain disclosure requirements for fair value measurements. The amendments in ASU 2018-13 were effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019. Early adoption was permitted. The disclosures were adopted using the prospective method for certain disclosures and retrospective for a majority of the disclosures. The Company adopted ASU 2018-13 in the first quarter of 2020 and it did not have a material impact on the Company's consolidated financial statements.

In June 2016, the FASB issued ASU 2016-13, *Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*, which along with several other subsequent codification updates related to accounting for credit losses, set forth a "current expected credit loss" ("CECL") model requiring the Company to measure all expected credit losses for financial instruments recorded at amortized cost held at the reporting date. The estimate was to be based on historical experience, current conditions and reasonable and supportable forecasts. This replaced the existing incurred loss model and was applicable to the measurement of credit losses on financial assets measured at amortized cost and applied to some off-balance sheet credit exposures. The amendments were effective for the Company beginning January 1, 2020. The Company elected to defer adoption of CECL until the earlier of the termination date of the current national emergency, declared on March 31, 2020, under the National Emergencies Act in connection with the COVID-19 outbreak, or December 31, 2020. The Company adopted ASU 2016-13 effective January 1, 2020 with cumulative adjustment of $5.1 million to retained earnings and implemented as of December 31, 2020 with an adjustment between the allowance for credit losses and the incurred loss model. The adoption of this ASU resulted in an increase of $8.3 million in our allowance for credit losses, including transfers of non-accretable discount on purchased credit-impaired loans. The increase is a result of changing from an "incurred loss" model, which encompasses allowances for current known and inherent losses within the portfolio, to an "expected loss" model, which encompasses allowances for losses expected to be incurred over the life of the portfolio. The adoption of this ASU required that we establish an allowance for expected credit losses for certain debt securities and other financial assets which are not material. We did not elect the federal banking agencies' rule providing for an optional three-year phase-in period for the day-one adverse regulatory capital effects upon adopting the standard.

New Accounting Standards Not Yet Adopted:

In December 2019, FASB issued ASU 2019-12, *Simplifying the Accounting for Income Taxes (Topic 740)*. This ASU simplifies the accounting for income taxes by eliminating certain exceptions to the guidance in ASC 740 related to the approach for intraperiod tax allocation, the methodology for calculating income taxes in an interim period and the recognition for deferred tax liabilities for outside basis differences. This ASU also simplifies aspects of the accounting for franchise taxes and enacted changes in tax laws or rates and clarifies the accounting transactions that result in a step-up in the tax basis of goodwill. ASU 2019-12 is effective for annual periods beginning after December 15, 2020, including interim periods within those annual periods. Early adoption is permitted. Southern National is currently in the process of evaluating the impact of adopting the new guidance on its consolidated financial statements and disclosures.

In March 2020, FASB issued ASU 2020-04, *Reference Rate Reform (Topic 848) - Facilitation of the Effects of Reference Rate Reform on Financial Reporting*. This ASU provides temporary optional guidance to ease the potential burden in accounting for reference rate reform. The new guidance provides optional expedients and exceptions for applying generally accepted accounting principles to contract modifications and hedging relationships, subject to meeting certain criteria, that reference the London Interbank Offered Rate ("LIBOR") or another reference rate expected to be discontinued. The ASU is intended to help stakeholders during the global market-wide reference rate transition period. ASU 2020-04 is effective upon issuance and can be applied through December 31, 2022. Southern National is currently in the process of evaluating the impact of adopting the new guidance on its consolidated financial statements and disclosures.

In October 2020, FASB issued ASU 2020-08, *Codification Improvements to Subtopic 310-20, Receivables - Nonrefundable Fees and Other Costs.* This ASU clarifies the accounting for the amortization of purchase premiums for callable debt securities with multiple call dates. ASU 2020-08 is effective for annual periods beginning after December 15, 2020, including interim periods within those annual periods. Early adoption is not permitted. Southern National is currently in the process of evaluating the impact of adopting the new guidance on its consolidated financial statements and disclosures.

In October 2020, FASB issued ASU 2020-10, *Codification Improvements.* This ASU clarifies various topics in the Codification, including the addition of existing disclosure requirements to the relevant disclosure sections. ASU 2020-10 is effective for annual periods beginning after December 15, 2020, including interim periods within those annual periods. Early adoption is permitted. Southern National is currently in the process of evaluating the impact of adopting the new guidance on its consolidated financial statements and disclosures.

2. INVESTMENT SECURITIES

The amortized cost and fair value of available for sale investment securities and the related gross unrealized gains and losses recognized in accumulated other comprehensive income (loss) were as follows (in thousands):

	Amortized	Gross Unrealized		Fair
	Cost	Gains	Losses	Value
December 31, 2020				
Residential government-sponsored mortgage-backed securities	$ 35,442	$ 1,618	$ —	$ 37,060
Obligations of states and political subdivisions	22,966	1,076	—	24,042
Corporate securities	15,000	81	(2)	15,079
Residential government-sponsored collateralized mortgage obligations	28,680	737	(1)	29,416
Government-sponsored agency securities	5,985	90	—	6,075
Agency commercial mortgage-backed securities	29,118	1,087	(15)	30,190
SBA pool securities	11,441	80	(150)	11,371
Total	$ 148,632	$ 4,769	$ (168)	$ 153,233

	Amortized	Gross Unrealized		Fair
	Cost	Gains	Losses	Value
December 31, 2019				
Residential government-sponsored mortgage-backed securities	$ 48,540	$ 455	$ (16)	$ 48,979
Obligations of states and political subdivisions	17,041	541	—	17,582
Corporate securities	2,004	8	—	2,012
Trust preferred securities	2,530	283	(245)	2,568
Residential government-sponsored collateralized mortgage obligations	36,511	217	(39)	36,689
Government-sponsored agency securities	14,823	47	(48)	14,822
Agency commercial mortgage-backed securities	27,557	192	(18)	27,731
SBA pool securities	14,622	11	(196)	14,437
Total	$ 163,628	$ 1,754	$ (562)	$ 164,820

The amortized cost, gross unrecognized gains and losses, allowance for credit losses and fair value of investment securities held to maturity were as follows (in thousands):

	Amortized Cost	Gross Unrecognized Gains	Gross Unrecognized Losses	Allowance for Credit Losses	Fair Value
December 31, 2020					
Residential government-sponsored mortgage-backed securities	$ 25,037	$ 729	$ (2)	$ —	$ 25,764
Obligations of states and political subdivisions	9,594	183	—	(1)	9,776
Residential government-sponsored collateralized mortgage obligations	1,090	39	—	—	1,129
Government-sponsored agency securities	5,000	163	—	—	5,163
Total	$ 40,721	$ 1,114	$ (2)	$ (1)	$ 41,832

	Amortized Cost	Gross Unrecognized Gains	Gross Unrecognized Losses	Fair Value
December 31, 2019				
Residential government-sponsored mortgage-backed securities	$ 22,925	$ 62	$ (52)	$ 22,935
Obligations of states and political subdivisions	15,071	165	(1)	15,235
Trust preferred securities	1,938	99	(2)	2,035
Residential government-sponsored collateralized mortgage obligations	3,128	10	(9)	3,129
Government-sponsored agency securities	29,386	108	(162)	29,332
Total	$ 72,448	$ 444	$ (226)	$ 72,666

During 2020 and 2019, $38.9 million and $45.1 million, respectively, of available for sale investment securities and $15.2 million and $15.3 million, respectively, of held to maturity investment securities were purchased. During 2020, $1.9 million and $1.7 million, respectively, of available for sale investment securities and held to maturity investment securities were sold. No investment securities were sold during 2019. Realized losses on sales of investment securities of $620 thousand were recorded for the year ended December 31, 2020.

The fair value and carrying amount of debt investment securities as of December 31, 2020, by contractual maturity were as follows (in thousands). Investment securities not due at a single maturity date are shown separately.

	Available for Sale		Held to Maturity	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Due in one to five years	$ 5,841	$ 6,057	$ 3,406	$ 3,513
Due in five to ten years	19,253	19,696	2,183	2,231
Due after ten years	18,857	19,443	9,005	9,195
Residential government-sponsored mortgage-backed securities	35,442	37,060	25,037	25,764
Residential government-sponsored collateralized mortgage obligations	28,680	29,416	1,090	1,129
Agency commercial mortgage-backed securities	29,118	30,190	—	—
SBA pool securities	11,441	11,371	—	—
Total	$ 148,632	$ 153,233	$ 40,721	$ 41,832

Investment securities with a carrying amount of approximately $125.3 million and $120.5 million at December 31, 2020 and 2019, respectively, were pledged to secure public deposits, certain other deposits, a line of credit for advances from the FHLB of Atlanta, and repurchase agreements.

Management measures expected credit losses on held-to-maturity securities on a collective basis by major security type with each type sharing similar risk characteristics, and considers historical credit loss information that is adjusted for current conditions and reasonable and supportable forecasts. With regard to U.S. Treasury and residential mortgage-backed securities issued by the U.S. government, or agencies thereof, it is expected that the securities will not be settled at prices less than the amortized cost bases of the securities as such securities are backed by the full faith and credit of and/or guaranteed by the U.S. government. Accordingly, no allowance for credit losses has been recorded for these securities. With regard to securities issued by States and political subdivisions and other held-to-maturity securities, management considers (i) issuer bond ratings, (ii) historical loss rates for given bond ratings, (iii) whether issuers continue to make timely principal and interest payments under the contractual terms of the securities and (iv) internal

forecasts. As of December 31, 2020, Southern National has $1 thousand as allowance for credit losses on held-to-maturity securities.

The following tables present information regarding investment securities available for sale and held to maturity in a continuous unrealized loss position as of December 31, 2020 and 2019 by duration of time in a loss position (in thousands):

December 31, 2020	**Less than 12 months**		**12 Months or More**		**Total**	
Available for Sale	**Fair value**	**Unrealized Losses**	**Fair value**	**Unrealized Losses**	**Fair value**	**Unrealized Losses**
Corporate securities	$ 998	$ (2)	$ —	$ —	$ 998	$ (2)
Residential government-sponsored collateralized mortgage obligations	954	(1)	—	—	954	(1)
Agency commercial mortgage-backed securities	2,170	(15)	—	—	2,170	(15)
SBA pool securities	—	—	8,119	(150)	8,119	(150)
Total	$ 4,122	$ (18)	$ 8,119	$ (150)	$ 12,241	$ (168)

December 31, 2020	**Less than 12 months**		**12 Months or More**		**Total**	
Held to Maturity	**Fair value**	**Unrecognized Losses**	**Fair value**	**Unrecognized Losses**	**Fair value**	**Unrecognized Losses**
Residential government-sponsored mortgage-backed securities	$ 331	$ (1)	$ 126	$ (1)	$ 457	$ (2)
Total	$ 331	$ (1)	$ 126	$ (1)	$ 457	$ (2)

December 31, 2019	**Less than 12 months**		**12 Months or More**		**Total**	
Available for Sale	**Fair value**	**Unrealized Losses**	**Fair value**	**Unrealized Losses**	**Fair value**	**Unrealized Losses**
Residential government-sponsored mortgage-backed securities	$ 2,686	$ (7)	$ 1,758	$ (9)	$ 4,444	$ (16)
Trust preferred securities	—	—	795	(245)	795	(245)
Residential government-sponsored collateralized mortgage obligations	4,253	(25)	3,133	(14)	7,386	(39)
Government-sponsored agency securities	4,924	(48)	—	—	4,924	(48)
Agency commercial mortgage-backed securities	2,833	(6)	3,126	(12)	5,959	(18)
SBA pool securities	1,148	(2)	9,420	(194)	10,568	(196)
Total	$ 15,844	$ (88)	$ 18,232	$ (474)	$ 34,076	$ (562)

December 31, 2019	**Less than 12 months**		**12 Months or More**		**Total**	
Held to Maturity	**Fair value**	**Unrecognized Losses**	**Fair value**	**Unrecognized Losses**	**Fair value**	**Unrecognized Losses**
Residential government-sponsored mortgage-backed securities	$ 14,978	$ (41)	$ 1,402	$ (11)	$ 16,380	$ (52)
Obligations of states and political subdivisions	2,011	(1)	—	—	2,011	(1)
Trust preferred securities	—	—	53	(2)	53	(2)
Residential government-sponsored collateralized mortgage obligations	1,162	(3)	571	(6)	1,733	(9)
Government-sponsored agency securities	—	—	20,833	(162)	20,833	(162)
Total	$ 18,151	$ (45)	$ 22,859	$ (181)	$ 41,010	$ (226)

During 2020, we sold all of the pooled trust preferred investment securities.

Changes in accumulated other comprehensive income (loss) by component for the years ended December 31, 2020, 2019 and 2018 are shown in the table below. All amounts are net of tax (in thousands).

For the year ended December 31, 2020	Unrealized Holding Gains on Available for Sale	Held to Maturity Securities	Total
Beginning balance	$ 943	$ (160)	$ 783
Current period other comprehensive income	2,693	9	2,702
Ending balance	$ 3,636	$ (151)	$ 3,485

For the year ended December 31, 2019	Unrealized Holding Gains (Losses) on Available for Sale	Held to Maturity Securities	Total
Beginning balance	$ (2,419)	$ (170)	$ (2,589)
Current period other comprehensive income	3,362	10	3,372
Ending balance	$ 943	$ (160)	$ 783

For the year ended December 31, 2018	Unrealized Holding Losses on Available for Sale	Held to Maturity Securities	Total
Beginning balance	$ (999)	$ (153)	$ (1,152)
Amounts reclassified from accumulated other comprehensive loss due to the adoption of ASU 2018-02	(199)	(30)	(229)
Subtotal	(1,198)	(183)	(1,381)
Current period other comprehensive (loss) income	(1,221)	13	(1,208)
Ending balance	$ (2,419)	$ (170)	$ (2,589)

3. LOANS AND ALLOWANCE

Loans, net of deferred fees, consist of the following at year end (in thousands):

	December 31, 2020
Loans secured by real estate:	
Commercial real estate - owner occupied	$ 435,078
Commercial real estate - non-owner occupied	600,706
Secured by farmland	11,662
Construction and land loans	103,264
Residential 1-4 family	557,257
Multi- family residential	107,267
Home equity lines of credit	91,606
Total real estate loans	1,906,840
Commercial loans	187,060
Paycheck Protection Program loans	319,428
Consumer loans	22,290
Total Non-PCD loans	2,435,618
PCD loans	8,908
Plus (less) deferred costs (fees) on loans	(4,030)
Total loans	$ 2,440,496

	December 31, 2019
Loans secured by real estate:	
Commercial real estate - owner occupied	$ 414,479
Commercial real estate - non-owner occupied	559,195
Secured by farmland	17,622
Construction and land loans	150,750
Residential 1-4 family	604,777
Multi- family residential	82,055
Home equity lines of credit	109,006
Total real estate loans	1,937,884
Commercial loans	221,447
Paycheck Protection Program loans	—
Consumer loans	26,304
Subtotal	2,185,635
Plus deferred costs on loans	412
Total loans	$ 2,186,047

Accounting policy related to the allowance for credit losses is considered a critical policy given the level of estimation, judgment, and uncertainty in the levels of the allowance required to account for the inherent probable losses in the loan portfolio and the material effect such estimation, judgment, and uncertainty can have on the consolidated financial results.

Accrued Interest Receivable

Accrued interest receivable on loans totaled $16.4 million and $6.8 million at December 31, 2020 and 2019, respectively and is included in accrued interest receivable in the consolidated balance sheets.

COVID-19 Loan Deferments

The Interagency Statement on Loan Modifications and Reporting for Financial Institutions Working with Customers Affected by the Coronavirus was published by banking regulators in April 2020 to clarify expectations around loan modifications and the determination of TDRs for borrowers experiencing COVID-19-related financial difficulty.

Southern National applied this regulatory guidance during its troubled debt restructurings (“TDR”) identification process for short-term loan forbearance agreements as a result of COVID-19 and in most cases is not recording these as TDRs.

Certain borrowers are currently unable to meet their contractual payment obligations because of the adverse effects of COVID-19. To help mitigate these effects, loan customers may apply for a deferral of payments, or portions thereof, for up to 90 days. After 90 days, customers may apply for an additional deferral, and a small proportion of our customers have requested such an additional deferral. In the absence of other intervening factors, such short-term modifications made on a good faith basis are not categorized as TDR, nor are loans granted payment deferrals related to COVID-19 reported as past due or placed on non-accrual status (provided the loans were not past due or on non-accrual status prior to the deferral). We implemented deferral arrangements for TDRs in accordance with the CARES Act and bank regulatory guidance. At December 31, 2020, there were 44 loans in COVID-19 related deferment with an aggregate outstanding balance of $122.0 million and were current as of December 31, 2019.

Accretion

Accretable discount on the acquired loans totaled $6.2 million and $11.2 million at December 31, 2020 and 2019, respectively. Accretion associated with the acquired loans held for investment of $4.3 million, $3.9 million and $4.5 million was recognized during the twelve months ended December 31, 2020, 2019 and 2018, respectively.

Impaired Loans

Prior to the adoption of ASC 326 on January 1, 2020, loans were reported as impaired when, based on then current information and events, it was probable we would 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 was evaluated in total for smaller-balance loans of a similar nature and on an individual loan basis for other loans. If a loan was impaired, a specific valuation allowance was allocated, if necessary, so that the loan was reported net, at the present value of estimated future cash flows using the loan’s existing rate or at the fair value of collateral if repayment was expected solely from the collateral. Interest payments on impaired loans were typically applied to principal unless collectability of the principal amount was reasonably assured, in which case interest was recognized on a cash basis. Impaired loans, or portions thereof, were charged off when deemed uncollectible.

Impaired loans for the portfolio as of December 31, 2019 were as follows (in thousands):

December 31, 2019	Total Loans		
	Recorded Investment [1]	Unpaid Principal Balance	Related Allowance
With no related allowance recorded			
Commercial real estate - owner occupied	$ 6,890	$ 8,530	$ —
Commercial real estate - non-owner occupied [2]	3,120	3,363	—
Construction and land development	345	747	—
Commercial loans	5,049	8,490	—
Residential 1-4 family [3]	1,021	2,719	—
Other consumer loans	—	—	—
Total	$ 16,425	$ 23,849	$ —
With an allowance recorded			
Commercial real estate - owner occupied	$ —	$ —	$ —
Commercial real estate - non-owner occupied [2]	176	281	1
Construction and land development	—	—	—
Commercial loans	2,498	2,533	957
Residential 1-4 family [3]	2,841	3,243	92
Other consumer loans	39	39	1
Total	$ 5,554	$ 6,096	$ 1,051
Grand total	$ 21,979	$ 29,945	$ 1,051

(1) Recorded investment is after cumulative prior charge offs of $1.5 million as of December 31, 2019. These loans also have aggregate SBA guarantees of $4.4 million as of December 31, 2019.
(2) Includes loans secured by farmland and multi-family residential loans.
(3) Includes home equity lines of credit.

The following tables present the average recorded investment and interest income recognized for impaired loans recognized by class of loans for the years ended December 31, 2019 and 2018 (in thousands):

Year Ended December 31, 2019	Total Loans	
	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded		
Commercial real estate - owner occupied	$ 7,387	$ 453
Commercial real estate - non-owner occupied [1]	3,205	191
Construction and land development	398	57
Commercial loans	5,254	214
Residential 1-4 family [2]	1,061	149
Other consumer loans	—	—
Total	$ 17,305	$ 1,064
With an allowance recorded		
Commercial real estate - owner occupied	$ —	$ —
Commercial real estate - non-owner occupied [1]	182	19
Construction and land development	—	—
Commercial loans	3,027	176
Residential 1-4 family [2]	2,944	111
Other consumer loans	39	—
Total	$ 6,192	$ 306
Grand total	$ 23,497	$ 1,370

For the Year Ended December 31, 2018	Total Loans Average Recorded Investment	Total Loans Interest Income Recognized
With no related allowance recorded		
Commercial real estate - owner occupied	$ 2,780	$ 179
Commercial real estate - non-owner occupied [(1)]	169	22
Construction and land development	—	—
Commercial loans	3,319	92
Paycheck Protection Program Loans	—	—
Residential 1-4 family [(2)]	1,582	125
Other consumer loans	—	—
Total	$ 7,850	$ 418
With an allowance recorded		
Commercial real estate - owner occupied	$ —	$ —
Commercial real estate - non-owner occupied [(1)]	—	—
Construction and land development	—	—
Commercial loans	2,530	200
Paycheck Protection Program loans	—	—
Residential 1-4 family [(2)]	1,422	67
Other consumer loans	—	—
Total	$ 3,952	$ 267
Grand total	$ 11,802	$ 685

(1) Includes loans secured by farmland and multi-family residential loans.
(2) Includes home equity lines of credit.

Non-Accrual and Past Due Loans

Loans are considered past due if the required principal and interest payments have not been received as of the date such payments were due. Loans are placed on non-accrual status when, in management's opinion, the borrower may be unable to meet payment obligations as they become due, as well as when required by regulatory provisions. In determining whether or not a borrower may be unable to meet payment obligations for each class of loans, we consider the borrower's debt service capacity through the analysis of current financial information, if available, and/or current information with regards to our collateral position. Regulatory provisions would typically require the placement of a loan on non-accrual status if (i) principal or interest has been in default for a period of 90 days or more unless the loan is both well secured and in the process of collection or (ii) full payment of principal and interest is not expected. Loans may be placed on non-accrual status regardless of whether or not such loans are considered past due. When interest accrual is discontinued, all unpaid accrued interest is reversed. Interest income on non-accrual loans is recognized only to the extent that cash payments are received in excess of principal due. A loan may be returned to accrual status when all the principal and interest amounts contractually due are brought current and future principal and interest amounts contractually due are reasonably assured, which is typically evidenced by a sustained period (at least six months) of repayment performance by the borrower.

The following tables present the aging of the recorded investment in past due loans by class of loans as of December 31, 2020 and 2019 (in thousands):

December 31, 2020	30 - 59 Days Past Due	60 - 89 Days Past Due	90 Days or More	Total Past Due	Loans Not Past Due	Total Loans [4]
Commercial real estate - owner occupied	$ —	$ —	$ —	$ —	$ 435,078	$ 435,078
Commercial real estate - non-owner occupied [1]	—	—	—	—	719,635	719,635
Construction and land development	23	39	—	62	103,202	103,264
Commercial loans	64	33	—	97	186,963	187,060
Paycheck Protection Program loans	—	—	—	—	319,428	319,428
Residential 1-4 family [2]	1,545	388	—	1,933	646,930	648,863
Other consumer loans	207	4	—	211	22,079	22,290
Total Non-PCD loans	1,839	464	—	2,303	2,433,315	2,435,618
PCD loans	—	—	—	—	8,908	8,908
Total	$ 1,839	$ 464	$ —	$ 2,303	$ 2,442,223	$ 2,444,526

December 31, 2019	30 - 59 Days Past Due	60 - 89 Days Past Due	90 Days or More	Total Past Due	Nonaccrual Loans [3]	Loans Not Past Due	Total Loans
Commercial real estate - owner occupied	$ 813	$ —	$ —	$ 813	$ —	$ 413,666	$ 414,479
Commercial real estate - non-owner occupied [1]	936	—	—	936	—	657,936	658,872
Construction and land development	746	275	—	1,021	—	149,729	150,750
Commercial loans	234	62	—	296	6,337	214,814	221,447
Residential 1-4 family [2]	4,060	—	—	4,060	2,524	707,199	713,783
Other consumer loans	107	—	—	107	39	26,158	26,304
Total	$ 6,896	$ 337	$ —	$ 7,233	$ 8,900	$ 2,169,502	$ 2,185,635

(1) Includes loans secured by farmland and multi-family residential loans.
(2) Includes home equity lines of credit.
(3) Nonaccrual loans include SBA guaranteed amounts totaling $4.1 million at December 31, 2019.
(4) Includes $122.0 million of loans that were subject to deferrals at December 31, 2020.

The amortized cost, by class, of loans and leases on nonaccrual status, and loans and leases greater than 90 days past due and still accruing at December 31, 2020, were as follows (in thousands):

December 31, 2020	90 Days or More	Loans Not Past Due	Total Nonaccrual Loans [3]
Commercial real estate - owner occupied	$ 2,641	$ —	$ 2,641
Commercial real estate - non-owner occupied [1]	1,098	4,481	5,579
Commercial loans	2,104	228	2,332
Residential 1-4 family [2]	2,035	13	2,048
Other consumer loans	9	—	9
Total Non-PCD loans	7,887	4,722	12,609
PCD loans	1,853	—	1,853
Total	$ 9,740	$ 4,722	$ 14,462

(1) Includes loans secured by farmland and multi-family residential loans.
(2) Includes home equity lines of credit.
(3) Nonaccrual loans include SBA guaranteed amounts totaling $3.1 million at December 31, 2020.

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The following table presents year-end non-accrual loans as of December 31, 2020, segregated by class of loans (in thousands):

December 31, 2020	Total Non-Accrual [3]	Non-Accrual With No Credit Loss Allowance [4]
Commercial real estate - owner occupied	$ 2,641	$ 2,641
Commercial real estate - non-owner occupied [1]	5,579	5,579
Commercial loans	2,332	582
Residential 1-4 family [2]	2,048	687
Other consumer loans	9	9
Total non-PCD loans	12,609	9,498
PCD loans	1,853	—
Total non-accrual loans	$ 14,462	$ 9,498

(1) Includes loans secured by farmland and multi-family residential loans.
(2) Includes home equity lines of credit.
(3) Nonaccrual loans include SBA guaranteed amounts totaling $3.1 million at December 31, 2020.
(4) Nonaccrual loans with no credit loss allowance include SBA guaranteed amounts totaling $1.7 million at December 31, 2020.

The following table presents non-accrual loans as of December 31, 2020 by class and year of origination (in thousands):

	2020	2019	2018	2017	2016	Prior	Revolving Loans	Revolving Loans Converted To Term	Total [3]
Commercial real estate - owner occupied	$ —	$ —	$ —	$ —	$ —	$ 2,641	$ —	$ —	$ 2,641
Commercial real estate - non-owner occupied [1]	—	—	—	1,098	4,481	—	—	—	5,579
Construction and land development	—	—	—	—	—	—	—	—	—
Commercial loans	—	—	—	107	—	2,225	—	—	2,332
Paycheck Protection Program loans	—	—	—	—	—	—	—	—	—
Residential 1-4 family [2]	—	—	—	151	—	1,374	523	—	2,048
Other consumer loans	—	—	—	—	—	9	—	—	9
Total non-PCD non-accruals	—	—	—	1,356	4,481	6,249	523	—	12,609
PCD loans	—	—	—	1,853	—	—	—	—	1,853
Total non-accrual loans	$ —	$ —	$ —	$ 3,209	$ 4,481	$ 6,249	$ 523	$ —	$ 14,462

(1) Includes loans secured by farmland and multi-family residential loans.
(2) Includes home equity lines of credit.
(3) Nonaccrual loans include SBA guaranteed amounts totaling $3.1 million at December 31, 2020.

Had non-accrual loans performed in accordance with their original contract terms, we would have recognized additional interest income, net of tax, of approximately $630 thousand in 2020.

Troubled Debt Restructurings

A modification is classified as a TDR if both of the following exist: (1) the borrower is experiencing financial difficulty and (2) the Bank has granted a concession to the borrower. The Bank determines that a borrower may be

experiencing financial difficulty if the borrower is currently delinquent on any of its debt, or if the Bank is concerned that the borrower may not be able to perform in accordance with the current terms of the loan agreement in the foreseeable future. Many aspects of the borrower's financial situation are assessed when determining whether they are experiencing financial difficulty, particularly as it relates to commercial borrowers due to the complex nature of the loan structure, business/industry risk and borrower/guarantor structures. Concessions may include the reduction of an interest rate at a rate lower than current market rates for a new loan with similar risk, extension of the maturity date, reduction of accrued interest, or principal forgiveness. When evaluating whether a concession has been granted, the Bank also considers whether the borrower has provided additional collateral or guarantors and whether such additions adequately compensate the Bank for the restructured terms, or if the revised terms are consistent with those currently being offered to new loan customers. The assessments of whether a borrower is experiencing (or is likely to experience) financial difficulty and whether a concession has been granted is subjective in nature and management's judgment is required when determining whether a modification is a TDR.

Although each occurrence is unique to the borrower and is evaluated separately, for all portfolio segments, TDRs are typically modified through reduction in interest rates, reductions in payments, changing the payment terms from principal and interest to interest only, and/or extensions in term maturity.

For the year ended December 31, 2020, there were seven TDR loans in the amount of $987 thousand primarily due to the economic impact of COVID-19. There have been no defaults of TDRs modified during the past twelve months.

Credit Quality Indicators

Through its system of internal controls, Southern National evaluates and segments loan portfolio credit quality on a quarterly basis using regulatory definitions for Special Mention, Substandard and Doubtful. Special Mention loans are considered to be criticized. Substandard and Doubtful loans are considered to be classified. Southern National had no loans classified Doubtful at December 31, 2020 or 2019.

Special Mention loans are loans that have a potential weakness that deserve management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or of the institution's credit position.

Substandard loans may be inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged if any. Loans so classified have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the institution will sustain some loss if the deficiencies are not corrected.

Doubtful loans have all the weaknesses inherent in those classified as substandard, with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable. Southern National had no loans classified Doubtful at December 31, 2020 or 2019.

In monitoring credit quality trends in the context of assessing the appropriate level of the allowance for credit losses on loans, we monitor portfolio credit quality by the weighted-average risk grade of each class of loan.

The following table present weighted-average risk grades for all loans, by class and year of origination/renewal as of December 31, 2020 (in thousands):

	2020	2019	2018	2017	2016	Prior	Revolving Loans	Revolving Loans Converted To Term	Total
Commercial real estate - owner occupied									
Not Rated	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —
Pass	22,473	43,484	41,006	46,847	61,758	188,074	3,608	6,698	413,948
Special Mention	—	—	—	149	1,692	11,822	—	—	13,663
Substandard	2,007	—	—	—	2,449	3,011	—	—	7,467
	$ 24,480	$ 43,484	$ 41,006	$ 46,996	$ 65,899	$ 202,907	$ 3,608	$ 6,698	$ 435,078
Weighted average risk grade	3.70	3.41	3.62	3.64	3.70	3.55	3.30	4.00	3.59
Commercial real estate - nonowner occupied (1)									
Not Rated	$ —	$ —	$ —	$ —	$ —	$ 362	$ —	$ —	$ 362
Pass	73,178	32,275	101,150	96,427	141,460	224,554	11,406	44	680,494
Special Mention		—	—	1,035	221	12,890	—	—	14,146
Substandard	—	—	—	1,069	4,481	18,783	300	—	24,633
	$ 73,178	$ 32,275	$ 101,150	$ 98,531	$ 146,162	$ 256,589	$ 11,706	$ 44	$ 719,635
Weighted average risk grade	3.55	3.78	3.32	3.59	3.70	3.90	3.79	3.00	3.70
Construction and land development									
Not Rated	$ 7,666	$ 8,332	$ 56	$ 746	$ 385	$ 2,026	$ —	$ —	$ 19,211
Pass	20,805	19,231	14,473	11,726	4,804	12,174	799	41	84,053
Special Mention	—	—	—	—	—	—	—	—	—
Substandard	—	—	—	—	—	—	—	—	—
	$ 28,471	$ 27,563	$ 14,529	$ 12,472	$ 5,189	$ 14,200	$ 799	$ 41	$ 103,264
Weighted average risk grade	3.34	3.90	3.68	4.00	3.97	3.41	4.00	4.00	3.67
Commercial loans									
Not Rated	$ —	$ —	$ —	$ 1,919	$ —	$ —	$ —	$ —	$ 1,919
Pass	11,372	18,852	13,569	14,335	3,405	24,568	87,118	5,306	178,525
Special Mention	—	—	—	—	—	—	—	—	—
Substandard	13	—	1,350	107	66	4,093	987	—	6,616
	$ 11,385	$ 18,852	$ 14,919	$ 16,361	$ 3,471	$ 28,661	$ 88,105	$ 5,306	$ 187,060
Weighted average risk grade	3.30	3.66	3.69	3.62	3.97	4.06	3.66	3.94	3.71
Paycheck Protection Program loans									
Not Rated	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —
Pass	319,428	—	—	—	—	—	—	—	319,428
Special Mention	—	—	—	—	—	—	—	—	—
Substandard	—	—	—	—	—	—	—	—	—
	$ 319,428	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ 319,428
Weighted average risk grade	2.00	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Residential 1-4 family (2)									
Not Rated	$ 52,416	$ 104,378	$ 68,889	$ 62,047	$ 35,767	$ 96,827	$ 75,214	$ 2,729	$ 498,267
Pass	15,497	14,654	18,557	9,809	10,033	64,106	13,810	521	146,987
Special Mention	—	—	—	52	—	48	277	201	578
Substandard	—	—	—	151	—	2,118	719	43	3,031
	$ 67,913	$ 119,032	$ 87,446	$ 72,059	$ 45,800	$ 163,099	$ 90,020	$ 3,494	$ 648,863
Weighted average risk grade	3.33	3.59	3.44	3.41	3.57	3.92	3.55	4.18	3.68
Other consumer loans									
Not Rated	$ 3,811	$ 1,921	$ 1,803	$ 943	$ 6,458	$ 2,767	$ 3,534	$ —	$ 21,237
Pass	585	244	—	—	—	62	37	—	928
Special Mention	—	—	—	—	—	115	—	—	115
Substandard	—	—	—	—	—	10	—	—	10
	$ 4,396	$ 2,165	$ 1,803	$ 943	$ 6,458	$ 2,954	$ 3,571	$ —	$ 22,290
Weighted average risk grade	3.63	3.28	N/A	N/A	N/A	4.72	4.00	N/A	3.76
PCD									
Not Rated	$ —	$ —	$ —	$ —	$ —	$ 1,176	$ 31	$ —	$ 1,207
Pass	—	—	—	—	400	2,997	—	—	3,397
Special Mention	—	—	—	—	—	1,448	—	—	1,448
Substandard	—	—	—	1,825	—	1,031	—	—	2,856
	$ —	$ —	$ —	$ 1,825	$ 400	$ 6,652	$ 31	$ —	$ 8,908
Weighted average risk grade	N/A	N/A	N/A	6.00	4.00	4.63	N/A	N/A	4.92
Total	$ 529,251	$ 243,371	$ 260,853	$ 249,187	$ 273,379	$ 675,062	$ 197,840	$ 15,583	$ 2,444,526
Weighted average risk grade	2.47	3.63	3.45	3.64	3.71	3.99	3.65	3.98	3.39

(1) Includes loans secured by farmland and multi-family residential loans.

(2) Includes home equity lines of credit.

As of December 31, 2019, the risk category of loans by class of loans is as follows (in thousands):

December 31, 2019	Total Loans			
	Special Mention	Substandard (3)	Pass	Total
Commercial real estate - owner occupied	$ 3,821	$ 3,975	$ 406,683	$ 414,479
Commercial real estate - non-owner occupied (1)	4,193	176	654,503	658,872
Construction and land development	—	690	150,060	150,750
Commercial loans	3,432	4,462	213,553	221,447
Residential 1-4 family (2)	666	1,194	711,923	713,783
Other consumer loans	122	—	26,182	26,304
Total loans	$ 12,234	$ 10,497	$ 2,162,904	$ 2,185,635

(1) Includes loans secured by farmland and multi-family residential loans.
(2) Includes home equity lines of credit.
(3) Includes SBA guarantees of $4.1 million as of December 31, 2019.

Revolving loans that converted to term during 2020 were as follows (in thousands):

	Total
Commercial real estate - owner occupied	$ 6,536
Commercial real estate - non-owner occupied (1)	44
Construction and land development	—
Commercial loans	330
Paycheck Protection Program loans	—
Residential 1-4 family (2)	731
Other consumer loans	—
Total loans	$ 7,641

(1) Includes loans secured by farmland and multi-family residential loans.
(2) Includes home equity lines of credit.

The amount of foreclosed residential real estate property held at December 31, 2020 and 2019 was $1.0 million and $1.4 million, respectively. The recorded investment in consumer mortgage loans collateralized by residential real estate property that are in the process of foreclosure was $1.4 million and $1.9 million at December 31, 2020 and 2019, respectively.

Allowance For Credit Losses – Loans

The allowance for credit losses on loans is a contra-asset valuation account, calculated in accordance with ASC 326 that is deducted from the amortized cost basis of loans to present the net amount expected to be collected. The amount of the allowance represents management's best estimate of current expected credit losses on loans considering available information, from internal and external sources, relevant to assessing collectability over the loans' contractual terms, adjusted for expected prepayments when appropriate. The contractual term excludes expected extensions, renewals and modifications unless (i) management has a reasonable expectation that a trouble debt restructuring will be executed with an individual borrower or (ii) such extension or renewal options are not unconditionally cancellable by us and, in such cases, the borrower is likely to meet applicable conditions and likely to request extension or renewal. Relevant available information includes historical credit loss experience, current conditions and reasonable and supportable forecasts. While historical credit loss experience provides the basis for the estimation of expected credit losses, adjustments to historical loss information may be made for differences in current portfolio-specific risk characteristics, environmental conditions or other relevant factors. The allowance for credit losses is measured on a collective basis for portfolios of loans when similar risk characteristics exist. Loans that do not share risk characteristics are evaluated for expected credit losses on an individual basis and excluded from the collective evaluation. Expected credit losses for collateral dependent loans, including loans where the borrower is experiencing financial difficulty but foreclosure is not probable, are based on the fair value of the collateral at the reporting date, adjusted for selling costs as appropriate.

Credit loss expense related to loans reflects the totality of actions taken on all loans for a particular period including any necessary increases or decreases in the allowance related to changes in credit loss expectations associated with specific loans or pools of loans. Portions of the allowance may be allocated for specific credits; however, the entire allowance is available for any credit that, in management's judgment, should be charged off. While management utilizes its best judgment and information available, the ultimate appropriateness of the allowance is dependent upon a variety of factors beyond our control, including the performance of our loan portfolio, the economy, changes in interest rates and the view of the regulatory authorities toward loan classifications.

In calculating the allowance for credit losses, most loans are segmented into pools based upon similar characteristics and risk profiles. Common characteristics and risk profiles include the type/purpose of loan, underlying collateral, geographical similarity and historical/expected credit loss patterns. In developing these loan pools for the purposes of modeling expected credit losses, we also analyzed the degree of correlation in how loans within each portfolio respond when subjected to varying economic conditions and scenarios as well as other portfolio stress factors. For allowance modeling purposes, our loan pools include (i) commercial real estate - owner occupied, (ii) commercial real estate - non-owner occupied, (iii) construction and land development, (iv) commercial, (v) agricultural loans, (vi) residential 1-4 family and (vii) consumer loans. We periodically reassess each pool to ensure the loans within the pool continue to share similar characteristics and risk profiles and to determine whether further segmentation is necessary.

For each loan pool, we measure expected credit losses over the life of each loan utilizing a combination of inputs: (i) probability of default ("PD"), which is the likelihood that loan will stop performing/default, (ii) probability of attrition ("PA"), which is the likelihood that a loan will pay-off prior to maturity, (iii) loss given default ("LGD"), which is the expected loss rate for loans in default and (iv) exposure at default ("EAD"), which is the estimated outstanding principal balance of the loans upon default, including the expected funding of unfunded commitments outstanding as of the measurement date. Inputs are pool-specific, though not necessarily solely reliant on internally-sourced data. Internal data is supplemented by, but not replaced by, peer data when required, primarily to determine the PD input. The various pool-specific inputs may be adjusted for current macroeconomic assumptions, as further discussed below, and other factors such as differences in underwriting standards, portfolio mix, or when historical asset terms do not reflect the contractual terms of the financial assets being evaluated as of the measurement date. Each time we measure expected credit losses, we assess the relevancy of historical information and consider any necessary adjustments to address any differences in current asset-specific characteristics.

Significant macroeconomic variables utilized in our allowance models include, among other things, (i) VA Gross Domestic Product, (ii) VA House Price Index, and (iii) VA unemployment rates. The macroeconomic variables utilized as inputs in forecast modeling were subjected to a variety of analysis procedures and were selected primarily based on statistical relevancy and correlation to historical credit losses, where historical credit losses may be fully internally-sourced or supplemented with peer data.

PDs were estimated by analyzing the relationship between the historical performance of each loan pool and historical economic trends over a complete economic cycle. Again, historical performance data is either fully internally-sourced or supplemented with peer data where necessary. PDs are adjusted to reflect the current impact of certain macroeconomic variables as well as their expected changes over a reasonable and supportable forecast period. We have determined that we are reasonably able to forecast the macroeconomic variables used in our forecast modeling processes with an acceptable degree of confidence for a total of four quarters. This forecast period is followed by an additional eight quarter reversion process whereby the forecasted macroeconomic variables are reverted to their historical mean on a straight-line basis. By reverting these economic inputs to their historical mean and considering loan/borrower specific attributes, our allowance models are intended to yield a measurement of expected credit losses that reflects average historical loss rates (which may be supplemented by peer data) for periods subsequent to the initial twelve-quarters consisting of the forecast and reversion periods. The LGD is linked to PD based on benchmark historical loss averages for each loan pool. That is, LGD is dynamic with PD; as PD increases, so will LGD, and vice versa. In this context, "benchmark" refers to the use of third-party data, and "historical loss averages" refers to the fraction of defaulted balance that tends to be lost. By nature of its connection to PD, LGD is by extension adjusted to reflect the current impact of certain macroeconomic variables as well as their expected changes over the four-quarter forecast period and eight-quarter reversion process, which management considers to be both reasonable and supportable. This same forecast/reversion period is used for all macroeconomic variables used in all of our economic forecast models. PA and EAD are estimated using either a Discounted Cash Flow or Remaining

Life model, both of which use various timing inputs to estimate the loan balance that remains at various future points in time, and thus also at the time of a default event.

Management qualitatively adjusts allowance model results for risk factors that are not considered within our quantitative modeling processes but are nonetheless relevant in assessing the expected credit losses within our loan pools. These qualitative factor (“Q-Factor”) adjustments may increase or decrease management's estimate of expected credit losses by a calculated percentage or amount based upon the estimated level of risk. The various risks that may be considered in making Q-Factor adjustments include, among other things, the impact of (i) changes in lending policies and procedures, including changes in underwriting standards and practices for collections, write-offs, and recoveries, (ii) actual and expected changes in international, national, regional, and local economic and business conditions and developments that affect the collectability of the loan pools, (iii) changes in the nature and volume of the loan pools and in the terms of the underlying loans, (iv) changes in the experience, ability, and depth of our lending management and staff, (v) changes in volume and severity of past due financial assets, the volume of non-accrual assets, and the volume and severity of adversely classified or graded assets, (vi) changes in the quality of our credit review function, (vii) changes in the value of the underlying collateral for loans that are non-collateral dependent, (viii) the existence, growth, and effect of any concentrations of credit and (ix) other factors such as the regulatory, legal and technological environments; competition; and events such as natural disasters or health pandemics.

In some cases, management may determine that an individual loan exhibits unique risk characteristics which differentiate the loan from other loans within our loan pools. In such cases, the loans are evaluated for expected credit losses on an individual basis and excluded from the collective evaluation. Specific allocations of the allowance for credit losses are determined by analyzing the borrower’s ability to repay amounts owed, collateral deficiencies, the relative risk grade of the loan and economic conditions affecting the borrower’s industry, among other things. A loan is considered to be collateral dependent when, based upon management's assessment, the borrower is experiencing financial difficulty and repayment is expected to be provided substantially through the operation or sale of the collateral. In such cases, expected credit losses are based on the fair value of the collateral at the measurement date, adjusted for estimated selling costs if satisfaction of the loan depends on the sale of the collateral. We reevaluate the fair value of collateral supporting collateral dependent loans on a quarterly basis. The fair value of real estate collateral supporting collateral dependent loans is evaluated by our internal appraisal services using a methodology that is consistent with the Uniform Standards of Professional Appraisal Practice. The fair value of collateral supporting collateral dependent construction loans is based on an “as is” valuation.

The following table presents details of the allowance for credit losses on loans segregated by loan portfolio segment as of December 31, 2020, calculated in accordance with the CECL methodology described above (in thousands).

December 31, 2020	Commercial Real Estate Owner Occupied	Commercial Real Estate Non-owner Occupied (1)	Construction and Land Development	Commercial Loans	Paycheck Protection Program	1-4 Family Residential (2)	Other Consumer Loans	PCD Loans	Total
Modeled expected credit losses	$ 2,565	$ 4,666	$ 1,297	$ 544	$ —	$ 5,113	$ 306	$ —	$ 14,491
Q-factor and other qualitative adjustments	4,134	8,276	516	917	—	5,330	194	—	19,367
Specific allocations	—	—	2	37	—	37	17	2,394	2,487
Total	$ 6,699	$ 12,942	$ 1,815	$ 1,498	$ —	$ 10,480	$ 517	$ 2,394	$ 36,345

(1) Includes loans secured by farmland and multi-family residential loans.
(2) Includes home equity lines of credit.

No allowance for credit losses has been recognized for PPP loans as such loans are fully guaranteed by the SBA.

Activity in the allowance for credit losses by class of loan for the year ended December 31, 2020 and allowance for loan losses by class of loan for the years ended December 31, 2019 and 2018 is summarized below (in thousands):

Year Ended December 31, 2020	Commercial Real Estate Owner Occupied	Commercial Real Estate Non-owner Occupied (1)	Construction and Land Development	Commercial Loans	1-4 Family Residential (2)	Other Consumer Loans	PCD Loans	Unallocated	Total
Allowance for credit losses:									
Beginning balance	$ 810	$ 1,720	$ 683	$ 5,418	$ 1,266	$ 190	$ —	$ 174	$ 10,261
Adoption of ASC 326	1,704	2,706	674	(3,246)	4,169	187	2,272	(174)	8,292
Balance	2,514	4,426	1,357	2,172	5,435	377	2,272	—	18,553
Provision (credits)	4,232	8,381	458	966	5,060	231	122	—	19,450
Charge offs	(52)	—	—	(1,734)	(433)	(124)	—	—	(2,343)
Recoveries	5	135	—	94	418	33	—	—	685
Ending balance	$ 6,699	$ 12,942	$ 1,815	$ 1,498	$ 10,480	$ 517	$ 2,394	$ —	$ 36,345
Year Ended December 31, 2019									
Allowance for loan losses:									
Beginning balance	$ 802	$ 1,669	$ 821	$ 7,097	$ 1,106	$ 224	$ —	$ 564	$ 12,283
Provision (recovery) for non-purchased loans	587	904	(138)	(1,708)	596	199	—	(390)	50
Provision for purchase credit impaired loans	—	—	—	300	—	—	—	—	300
Total Provision (recovery)	587	904	(138)	(1,408)	596	199	—	(390)	350
Charge offs	(782)	(863)	—	(622)	(742)	(269)	—	—	(3,278)
Recoveries	203	10	—	351	306	36	—	—	906
Ending balance	$ 810	$ 1,720	$ 683	$ 5,418	$ 1,266	$ 190	$ —	$ 174	$ 10,261
Year ended December 31, 2018									
Allowance for loan losses:									
Beginning balance	$ 690	$ 1,321	$ 692	$ 4,496	$ 1,586	$ 612	$ —	$ —	$ 9,397
Provision (recovery) for non-purchased loans	497	348	129	1,941	237	(116)	—	564	3,600
Provision for purchase credit impaired loans	—	—	—	600	—	—	—	—	600
Provision (recovery)	497	348	129	2,541	237	(116)	—	564	4,200
Charge offs	(400)	—	—	(1,566)	(842)	(290)	—	—	(3,098)
Recoveries	15	—	—	1,626	125	18	—	—	1,784
Ending balance	$ 802	$ 1,669	$ 821	$ 7,097	$ 1,106	$ 224	$ —	$ 564	$ 12,283

(1) Includes loans secured by farmland and multi-family residential loans.
(2) Includes home equity lines of credit.

Generally, a commercial loan, or a portion thereof, is charged-off when it is determined, through the analysis of any available current financial information with regards to the borrower, that the borrower is incapable of servicing unsecured debt, there is little or no prospect for near term improvement and no realistic strengthening action of significance is pending or, in the case of secured debt, when it is determined, through analysis of current information with regards to our collateral position, that amounts due from the borrower are in excess of the calculated current fair value of the collateral. Losses on installment loans are recognized in accordance with regulatory guidelines. All other consumer loan losses are recognized when delinquency exceeds 120 cumulative days.

The following table presents loans that were evaluated for expected credit losses on an individual basis and the related specific allocations, by loan portfolio segment as of December 31, 2020 (in thousands):

December 31, 2020	Loan Balance [3]	Specific Allocations
Commercial real estate - owner occupied	$ 23,397	$ —
Commercial real estate - non-owner occupied [1]	8,536	—
Construction and land development	77	2
Commercial loans	5,515	37
Paycheck Protection Program loans	—	—
Residential 1-4 family [2]	2,399	37
Other consumer loans	17	17
Total non-PCD loans	39,941	93
PCD loans	8,908	2,394
Total loans	$ 48,849	$ 2,487

(1) Includes loans secured by farmland and multi-family residential loans.
(2) Includes home equity lines of credit.
(3) Includes SBA guarantees of $2.5 million as of December 31, 2020.

The following table presents the balance in the allowance for loan losses and the recorded investment in loans by portfolio segment and based on impairment method as of December 31, 2019 (in thousands):

December 31, 2019	Commercial Real Estate Owner Occupied	Commercial Real Estate Non-owner Occupied [1]	Construction and Land Development	Commercial Loans	Paycheck Protection Program	1-4 Family Residential [2]	Other Consumer Loans	Unallocated	Total
Ending allowance balance attributable to loans:									
Individually evaluated for impairment	$ —	$ —	$ —	$ 957	$ —	$ 85	$ —	$ —	$ 1,042
Collectively evaluated for impairment	810	1,720	683	4,461	—	1,181	190	174	9,219
Total ending allowance	$ 810	$ 1,720	$ 683	$ 5,418	$ —	$ 1,266	$ 190	$ 174	$ 10,261
Loans:									
Individually evaluated for impairment	$ 6,890	$ 3,120	$ 345	$ 7,544	$ —	$ 1,443	$ —	$ —	$ 19,342
Collectively evaluated for impairment	407,589	655,752	150,405	213,903	—	712,340	26,304	—	2,166,293
Total ending loan balances	$ 414,479	$ 658,872	$ 150,750	$ 221,447	$ —	$ 713,783	$ 26,304	$ —	$ 2,185,635

(1) Includes loans secured by farmland and multi-family residential loans.
(2) Includes home equity lines of credit.

Purchased Loans

The following table presents the carrying amount of purchased impaired and non-impaired loans from the acquisitions as of December 31, 2019 (in thousands):

	December 31, 2019		
	Purchased Impaired Loans	Purchased Non-impaired Loans	Total
Commercial real estate [1]	$ 3,978	$ 307,289	$ 311,267
Construction and land development	26	21,111	21,137
Commercial loans	2,354	34,729	37,083
Residential 1-4 family [2]	2,841	232,887	235,728
Other consumer loans	—	15,153	15,153
Total	$ 9,199	$ 611,169	$ 620,368

(1) Includes owner occupied and non-owner occupied as well as loans secured by farmland and multi-family residential loans.
(2) Includes home equity lines of credit.

Changes in the carrying amount and accretable yield for purchased impaired and non-impaired loans from the acquisitions were as follows for the years ended December 31, 2019 (in thousands):

	December 31, 2019			
	Purchased Impaired		Purchased Non-impaired	
	Accretable Yield	Carrying Amount of Loans	Accretable Discount	Carrying Amount of Loans
Balance at beginning of the period	$ 174	$ 11,449	$ 13,474	$ 795,759
Accretion	(72)	72	(3,549)	3,549
Payments received	—	(2,322)	—	(188,139)
Balance at end of the period	$ 102	$ 9,199	$ 9,925	$ 611,169

4. FAIR VALUE

ASC 820 establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair value:

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

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

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

The following is a description of the valuation methodologies used for instruments measured at fair value, as well as the general classification of such instruments pursuant to the valuation hierarchy:

Assets Measured on a Recurring Basis:

Investment Securities Available for Sale

Where quoted prices are available in an active market, investment securities are classified within Level 1 of the valuation hierarchy. Level 1 investment securities include highly liquid government bonds and mortgage products. If quoted market prices are not available, then fair values are estimated by using pricing models, quoted prices of investment securities with similar characteristics or discounted cash flow. Level 2 investment securities include U.S. agency securities, mortgage-backed securities, obligations of states and political subdivisions and certain corporate, asset-backed and other securities. In certain cases where there is limited activity or less transparency around inputs to the valuation, investment securities are classified within Level 3 of the valuation hierarchy. Currently, a majority of Southern National's available for sale debt investment securities are considered to be Level 2 investment securities, except for a few corporate securities that are classified as Level 3 investment securities.

Assets measured at fair value on a recurring basis are summarized below:

		Fair Value Measurements Using		
(dollars in thousands)	**Total at December 31, 2020**	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**
Available for sale securities				
Residential government-sponsored mortgage-backed securities	$ 37,060	$ —	$ 37,060	$ —
Obligations of states and political subdivisions	24,042	—	24,042	—
Corporate securities	15,079	—	14,079	1,000
Residential government-sponsored collateralized mortgage obligations	29,416	—	29,416	—
Government-sponsored agency securities	6,075	—	6,075	—
Agency commercial mortgage-backed securities	30,190	—	30,190	—
SBA pool securities	11,371	—	11,371	—
Total	$ 153,233	$ —	$ 152,233	$ 1,000

		Fair Value Measurements Using		
(dollars in thousands)	**Total at December 31, 2019**	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**
Available for sale securities				
Residential government-sponsored mortgage-backed securities	$ 48,979	$ —	$ 48,979	$ —
Obligations of states and political subdivisions	17,582	—	17,582	—
Corporate securities	2,012	—	1,012	1,000
Trust preferred securities	2,568	—	2,568	—
Residential government-sponsored collateralized mortgage obligations	36,689	—	36,689	—
Government-sponsored agency securities	14,822	—	14,822	—
Agency commercial mortgage-backed securities	27,731	—	27,731	—
SBA pool securities	14,437	—	14,437	—
Total	$ 164,820	$ —	$ 163,820	$ 1,000

No corporate securities that are classified as Level 3 above were purchased or sold during 2020 or 2019. These corporate securities did not have a material impact on the income statement for the year ended December 31, 2020 or 2019.

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Assets and Liabilities Measured on a Non-recurring Basis:

Loans

We may be required to measure certain financial assets at fair value on a nonrecurring basis. These adjustments to fair value usually result from the application of lower of amortized cost or fair value accounting or write-downs of individual assets due to impairment.

Following the adoption of ASC 326, the population of loans measured at fair value on a non-recurring basis has greatly diminished and is limited to collateral-dependent loans evaluated individually. These collateral-dependent loans are deemed to be at fair value if there is an associated allowance for credit losses or if a charge-off has been recorded in the previous 12 months. Collateral values are determined using appraisals or other third-party value estimates of the subject property discounted based on estimated selling costs, generally between 5% and 10%, and immaterial adjustments for other external factors that may impact the marketability of the collateral. The weighted average discount for estimated selling costs applied was 6%.

Prior to the adoption of ASC 326, we measured the impairment for impaired loans considering the fair value of the loan's collateral (if the loan was collateral dependent). Fair value of the loan's collateral was determined by an independent appraisal or evaluation less estimated costs related to selling the collateral. In some cases appraised value was net of costs to sell. Estimated selling costs ranged from 5% to 10% of collateral valuation at December 31, 2019. Fair value was classified as Level 3 in the fair value hierarchy. Loans identified as impaired totaled $22.0 million (including SBA guarantees of $4.4 million) with a $1.1 million allocation made to the allowance for loan losses at December 31, 2019.

Other Real Estate Owned

OREO is evaluated at the time of acquisition and recorded at fair value as determined by independent appraisal or evaluation less cost to sell. In some cases appraised value is net of costs to sell. Selling costs have been in the range from 5% to 10% of collateral valuation at December 31, 2020 and 2019. Fair value is classified as Level 3 in the fair value hierarchy. OREO is further evaluated quarterly for any additional impairment. At December 31, 2020 and 2019, the total amount of OREO was $3.1 million and $6.2 million, respectively.

Assets measured at fair value on a non-recurring basis are summarized below:

		Fair Value Measurements Using		
(dollars in thousands)	**Total at December 31, 2020**	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**
Collateral dependent loans	$ 47,001	$ —	$ —	$ 47,001
Other real estate owned:				
Commercial real estate - non-owner occupied [(1)]	865	—	—	865
Construction and land development	1,221	—	—	1,221
Residential 1-4 family [(2)]	992	—	—	992

(dollars in thousands)	Total at December 31, 2019	Fair Value Measurements Using: Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Impaired loans:				
Commercial real estate - owner occupied	$ 6,890	$ —	$ —	$ 6,890
Commercial real estate - non-owner occupied (1)	3,296	—	—	3,296
Construction and land development	345	—	—	345
Commercial loans	7,547	—	—	7,547
Residential 1-4 family (2)	3,862	—	—	3,862
Consumer	39	—	—	39
Other real estate owned:				
Commercial real estate - non-owner occupied (1)	1,984	—	—	1,984
Construction and land development	2,874	—	—	2,874
Residential 1-4 family (2)	1,366	—	—	1,366

(1) Includes loans secured by farmland and multi-family residential loans.
(2) Includes home equity lines of credit.

Fair Value of Financial Instruments

The carrying amount, estimated fair values and fair value hierarchy levels (previously defined) of financial instruments were as follows (in thousands) for the periods indicated:

	Fair Value Hierarchy Level	December 31, 2020 Carrying Amount	December 31, 2020 Fair Value	December 31, 2019 Carrying Amount	December 31, 2019 Fair Value
Financial assets:					
Cash and cash equivalents	Level 1	$ 196,185	$ 196,185	$ 31,928	$ 31,928
Securities available for sale	Level 2 & Level 3	153,233	153,233	164,820	164,820
Securities held to maturity	Level 2	40,721	41,832	72,448	72,666
Stock in Federal Reserve Bank and Federal Home Loan Bank	Level 2	16,927	16,927	17,832	17,832
Equity investment in mortgage affiliate	Level 3	12,652	12,652	5,020	5,020
Preferred investment in mortgage affiliate	Level 3	3,305	3,305	3,305	3,305
Net loans	Level 3	2,404,151	2,435,612	2,175,786	2,180,487
Accrued interest receivable	Level 2	17,405	17,405	8,210	8,210
Financial liabilities:					
Demand deposits and NOW accounts	Level 2	$ 1,155,426	$ 1,155,426	$ 730,325	$ 730,325
Money market and savings accounts	Level 2	787,132	787,132	611,353	611,353
Time deposits	Level 3	490,048	495,022	783,040	786,420
Securities sold under agreements to repurchase	Level 1	16,065	16,065	12,883	12,883
FHLB advances	Level 1	100,000	100,000	121,640	121,640
Junior subordinated debt	Level 2	9,682	8,863	9,632	9,206
Senior subordinated notes	Level 2	105,647	109,276	47,051	48,156
Accrued interest payable	Level 2	3,057	3,057	4,907	4,907

Carrying amount is the estimated fair value for cash and cash equivalents (including federal funds sold), accrued interest receivable and payable, demand deposits, savings accounts, money market accounts and FHLB advances and securities sold under agreements to repurchase.

The investment in common stock of our mortgage affiliate is accounted for using the equity method. Under the equity method, the carrying value of Southern National's investment in STM was originally recorded at cost but is adjusted periodically to record Southern National's proportionate share of STM's earnings or losses through noninterest income and decreased by the amount of cash dividends or similar distributions received from STM. The investment in

preferred stock of our mortgage affiliate is considered to be a non-marketable equity security that does not have a readily determinable fair value. Non-marketable equity securities with no recurring market value data available are reviewed periodically and any observable market value change is adjusted through noninterest income. Southern National evaluates its investments in this non-marketable equity security for impairment and recoverability of the recorded investment by considering positive and negative evidence, including the profitability and asset quality of STM, dividend payment history and recent redemption experience. Impairment is assessed at each reporting period and if identified, is recognized in noninterest income. No impairment was recorded for the year ended December 31, 2020 and 2019.

Fair value of long-term debt is based on current rates for similar financing. Carrying amount of Federal Reserve Bank and Federal Home Loan Bank stock is a reasonable estimate of fair value as these securities are not readily marketable and are based on the ultimate recoverability of the par value. The fair value of off-balance-sheet items is not considered material. Fair value of net loans, time deposits, junior subordinated debt, and senior subordinated notes are measured using the exit-price notion.

5. BANK PREMISES AND EQUIPMENT

Bank premises and equipment as of December 31, 2020 and 2019 were as follows (in thousands):

	2020	2019
Land	$ 8,139	$ 8,139
Land improvements	1,558	1,558
Building and improvements	23,164	23,164
Leasehold improvements	3,001	2,933
Furniture and equipment	8,962	8,789
Construction in progress	1,441	719
	46,265	45,302
Less accumulated depreciation and amortization	15,959	14,118
Bank premises and equipment, net	$ 30,306	$ 31,184

Depreciation and amortization expense related to bank premises and equipment for 2020, 2019 and 2018 was $2.0 million, $2.3 million and $3.3 million, respectively.

6. LEASES

The Company leases certain premises and equipment under operating leases. In recognizing lease right-of-use assets and related liabilities, we account for lease and non-lease components (such as taxes, insurance, and common area maintenance costs) separately as such amounts are generally readily determinable under our lease contracts. At December 31, 2020 and 2019, the Company had operating lease liabilities totaling $8.2 million and $8.5 million, respectively, and right-of-use assets totaling $7.5 million and $8.0 million, respectively, related to these leases. Operating lease liabilities and right-of-use assets are reflected in our consolidated balance sheets. We do not currently have any financing leases. For the year ended December 31, 2020 and 2019, our net operating lease cost was $2.9 million and $2.5 million, respectively, and were reflected in occupancy expenses on our income statements.

The following table presents supplemental cash flow and other information related to our operating leases:

	For the Year Ended	
(in thousands except for percent and period data)	**December 31, 2020**	**December 31, 2019**
Supplemental cash flow information:		
Cash paid for amounts included in the measurement of lease liabilities	$ 5,062	$ 4,883
Other information:		
Weighted-average remaining lease term - operating leases, in years	4.8	5.7
Weighted-average discount rate - operating leases	2.5 %	2.8 %

The following table summarizes the maturity of remaining lease liabilities:

(dollars in thousands)	As of December 31, 2020
Lease payments due:	
Less than one year	$ 2,542
One to three years	3,791
Three to five years	1,123
More than five years	1,376
Total lease payments	8,832
Less: imputed interest	(594)
Lease liabilities	$ 8,238

As of December 31, 2020 and 2019, the Company did not have any operating leases that have not yet commenced that will create additional lease liabilities and right-of-use assets for the Company.

7. GOODWILL AND INTANGIBLE ASSETS

Goodwill

Southern National has recorded $101.9 million of goodwill at December 31, 2020 and 2019. Goodwill is primarily related to the acquisition of other banks.

Goodwill is evaluated for impairment on an annual basis or more frequently if events or circumstances warrant. Our annual assessment occurs during the third calendar quarter. In response to the effects of COVID-19, management determined there to be a triggering event in the third quarter of 2020 warranting a goodwill assessment. For the third quarter 2020 assessment, we performed a step one quantitative assessment to determine if the fair value of all our reporting units was less than its carrying amount. We concluded that the fair value of all our reporting units exceeded their carrying amounts and no impairment was present based on management's assessment. No impairment was indicated in 2020, 2019 or 2018.

Intangible Assets

Intangible assets were as follows at year end (in thousands):

	December 31, 2020		
	Gross Carrying Value	Accumulated Amortization	Net Carrying Value
Amortizable core deposit intangibles	$ 17,503	$ (11,677)	$ 5,826

	December 31, 2019		
	Gross Carrying Value	Accumulated Amortization	Net Carrying Value
Amortizable core deposit intangibles	$ 17,503	$ (10,312)	$ 7,191

Estimated amortization expense of intangibles for the years ended December 31 were as follows (in thousands):

2021	$ 1,364
2022	1,325
2023	1,269
2024	1,266
2025	602
Total	$ 5,826

8. DEPOSITS

The aggregate amount of time deposits in denominations of $250 thousand or more at December 31, 2020 and 2019 was $165.7 million and $163.2 million, respectively.

At December 31, 2020, the scheduled maturities of time deposits are as follows (in thousands):

2021	$ 369,743
2022	77,081
2023	27,927
2024	10,662
2025	4,600
2026	35
Total	$ 490,048

The following table sets forth the maturities of certificates of deposit of $250 thousand and over as of December 31, 2020 (in thousands):

Within 3 Months	3 to 6 Months	6 to 12 Months	Over 12 Months	Total
$ 36,234	$ 38,192	$ 39,515	$ 51,807	$ 165,748

As of December 31, 2020, we had brokered certificates of deposit in the amount of $270 thousand and brokered money market deposits of $55.2 million. At December 31, 2019, we had brokered certificates of deposit in the amount of $114.1 million, and we had brokered money market deposits of $24.4 million.

For our deposit agreements with certain customers, we hold the collateral in a segregated custodial account. We are required to maintain adequate collateral levels. In the event the collateral fair value falls below stipulated levels, we will pledge additional securities. We closely monitor collateral levels to ensure adequate levels are maintained, while mitigating the potential risk of over-collateralization.

9. SECURITIES SOLD UNDER AGREEMENTS TO REPURCHASE AND OTHER BORROWINGS

Other borrowings can consist of FHLB convertible advances, FHLB of Atlanta overnight advances, FHLB advances maturing within one year, federal funds purchased and securities sold under agreements to repurchase (“repo”) that mature within one year, which are secured transactions with customers. The balance in repo accounts at December 31, 2020 and 2019 was $16.0 million and $12.9 million, respectively.

At December 31, 2020 and 2019, we have pledged callable agency securities, residential government-sponsored mortgage-backed securities and collateralized mortgage obligations with a carrying value of $31.1 million and $22.0 million, respectively, to customers who require collateral for overnight repurchase agreements and deposits.

Other borrowings consist of the following (in thousands):

	December 31, 2020	December 31, 2019
FHLB collateral advances maturing 3/1/2030	$ 100,000	$ —
FHLB overnight advances	—	81,000
Short-term FHLB advances maturing 3/10/2020	—	40,640
Total FHLB advances	100,000	121,640
Securities sold under agreements to repurchase	16,065	12,883
Total	$ 116,065	$ 134,523
Weighted average interest rate at year end	3.55 %	1.75 %

Each FHLB advance is payable at its maturity date, with a prepayment penalty for fixed rate advances paid off earlier than maturity. Residential 1-4 family mortgage loans in the amount of approximately $390.7 million and $376.3 million were pledged as collateral for FHLB advances as of December 31, 2020 and 2019, respectively. HELOCs in the amount of approximately $37.2 million and $46.9 million were pledged as collateral for FHLB advances at December 31, 2020 and 2019, respectively. Commercial mortgage loans in the amount of approximately $189.0 million and $76.6 million were pledged as collateral for FHLB advances as of December 31, 2020 and 2019, respectively. Investment securities in the amount of $6.4 million and $17.6 million were pledged as collateral for FHLB advances at December 31, 2020 and 2019, respectively. At December 31, 2020, Sonabank had available collateral to borrow an additional $689.1 million from the FHLB.

10. JUNIOR SUBORDINATED DEBT AND SENIOR SUBORDINATED NOTES

In 2017, the Company assumed $10.3 million of trust preferred securities that were issued on September 17, 2003 and placed through a trust in a pooled underwriting totaling approximately $650 million. The trust issuer invested the total proceeds from the sale of the trust preferred securities in Floating Rate Junior Subordinated Deferrable Interest Debentures (“Junior Subordinated Debt”). At December 31, 2020 and 2019, we had $9.7 million and $9.6 million, respectively, of Junior Subordinated Debt outstanding. The trust preferred securities pay cumulative cash distributions quarterly at a variable rate per annum, reset quarterly, equal to the three-month LIBOR plus 2.95%. As of December 31, 2020 and 2019, the interest rate was 3.18% and 4.85%, respectively. The dividends paid to holders of the trust preferred securities, which are recorded as interest expense, are deductible for income tax purposes.

The trust preferred securities may be included in Tier 1 capital for regulatory capital adequacy determination purposes up to 25% of Tier 1 capital after its inclusion. At December 31, 2020, all of the trust preferred securities qualified as Tier 1 capital.

On January 20, 2017, Southern National completed the sale of $27.0 million of its fixed-to-floating rate Subordinated Notes due 2027 (the “SNBV Senior Subordinated Notes”). The SNBV Senior Subordinated Notes will initially bear interest at 5.875% per annum until January 31, 2022; thereafter, the SNBV Senior Subordinated Notes will be payable at an annual floating rate equal to three-month LIBOR plus a spread of 3.95% until maturity or early redemption. At December 31, 2020, all of the SNBV Senior Subordinated Notes qualified as Tier 2 capital.

In 2017, the Company assumed the Senior Subordinated Note Purchase Agreement dated April 22, 2015 with certain institutional accredited investors, pursuant to which $20.0 million in aggregate principal amount of its 6.50% Fixed-to-Floating Rate Subordinated Notes due 2025 was sold to the investors. At December 31, 2020, 80% of the Senior Subordinated Notes qualified as Tier 2 capital. On February 1, 2021, 100% of the notes were redeemed.

On August 25, 2020, Southern National completed the sale of $60.0 million of its fixed-to-floating rate Subordinated Notes due 2030 (the “SNBV Subordinated Notes”). The SNBV Subordinated Notes will bear interest at an initial rate of 5.40% per annum, payable semi-annually in arrears on March 1 and September 1 of each year, commencing on March 1, 2021. From and including September 1, 2025 to, but excluding the maturity date or the date of earlier redemption (the

"floating rate period"), the interest rate will reset quarterly to an annual interest rate equal to the Benchmark rate, which is expected to be three-month Term SOFR, plus 531 basis points, for each quarterly interest period during the floating rate period, payable quarterly in arrears on March 1, June 1, September 1, and December 1 of each year, commencing on December 1, 2025. Notwithstanding the foregoing, in the event that the Benchmark rate is less than zero, the Benchmark rate shall be deemed to be zero. At December 31, 2020, all of the SNBV Subordinated Notes qualified as Tier 2 capital.

At December 31, 2020, the remaining unamortized debt issuance costs related to the Subordinated Notes totaled $1.9 million.

11. INCOME TAXES

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting and income tax purposes. Net deferred tax assets at December 31, 2020 and 2019 consist primarily of the following (in thousands):

	2020	2019
Deferred tax assets:		
Allowance for credit losses	$ 8,028	$ 2,235
Unearned loan fees and other	2,583	1,064
Other real estate owned write-downs	567	748
Lease liability	1,779	1,829
Other than temporary impairment charge	—	229
Purchase accounting	—	949
Federal AMT credit carryforward	1,137	1,137
Federal low income housing credit carryforward	444	3,226
Deferred compensation	1,734	1,573
Depreciation	274	218
Other	1,012	511
Total deferred tax assets	17,558	13,719
Deferred tax liabilities:		
Right-of-use assets	1,576	1,731
Net unrealized gain on investment securities available for sale	916	200
Purchase accounting	420	—
Total deferred tax liabilities	2,912	1,931
Net deferred tax assets	$ 14,646	$ 11,788

No valuation allowance was deemed necessary on deferred tax assets in 2020 or 2019. Management believes that the realization of the deferred tax assets is more likely than not based on the expectation that Southern National will generate the necessary taxable income in future periods.

We have no unrecognized tax benefits and do not anticipate any increase in unrecognized tax benefits during the next twelve months. Should the accrual of any interest or penalties relative to unrecognized tax benefits be necessary, it is our policy to record such accruals in our income tax accounts; no such accruals existed as of December 31, 2020, 2019 or 2018. Southern National and its subsidiaries file a consolidated U.S. federal income tax return, and Southern National files a Virginia state income tax return. Sonabank files a Maryland and an Arkansas state income tax return. These returns are subject to examination by taxing authorities for all years after 2016.

The provision for income taxes consists of the following for the years ended December 31, 2020, 2019 and 2018 (in thousands):

	2020	2019	2018
Current tax expense			
Federal	$ 7,825	$ 4,429	$ 6,244
State	407	228	249
Total current tax expense	8,232	4,657	6,493
Deferred tax expense (benefit)			
Federal	(1,496)	1,350	2,692
State	(122)	70	429
Total deferred tax expense (benefit)	(1,618)	1,420	3,121
Total income tax expense	$ 6,614	$ 6,077	$ 9,614

The income tax expense differed from the amount of income tax determined by applying the U.S. Federal income tax rate of 21% to pretax income for the years ended December 31, 2020, 2019 and 2018 due to the following (in thousands):

	2020	2019	2018
Computed expected tax expense at statutory rate	$ 6,279	$ 8,241	$ 9,094
Increase (decrease) in tax expense resulting from:			
Remeasurement of deferred tax assets and liabilities	(31)	(1,659)	1,130
Low income housing tax credits, net of amortization	225	(255)	(502)
Income from bank-owned life insurance	(327)	(357)	(416)
Other, net	468	107	308
Income tax expense	$ 6,614	$ 6,077	$ 9,614

During 2018, the Company determined that certain net operating loss carryforwards were impaired due to Section 382 limitations. During 2019, the Company completed its formal assessment of the Section 382 limitation and rebooked $1.2 million deferred tax asset stemming from a $5.5 million acquired net operating loss carryforward that was written off in the fourth quarter of 2018. Additionally, the Company remeasured the depreciation deferred tax liability by $0.6 million, net, to reflect a 2018 adjustment to the assets held for sale not previously included.

12. EMPLOYEE BENEFITS

Southern National has a 401(k) plan that allows employees to make pre-tax contributions for retirement. The 401(k) plan provides for discretionary matching contributions by Southern National. Expense for 2020, 2019 and 2018 was $795 thousand, $704 thousand and $784 thousand, respectively.

The Bank maintains a deferred compensation plan in the form of Supplemental Executive Retirement Plan (“SERP”) for four (4) former executives. Under the plan, the Bank pays each participant, or their beneficiary, compensation deferred plus accrued interest for a period of 15 to 17 years after their retirement or age 62 depending on the terms and conditions of each plan. A liability is accrued for the obligations under these plans.

The expense incurred for the deferred compensation plans in 2020, 2019 and 2018 was $1.3 million, $1.2 million and $1.2 million, respectively. The deferred compensation plan liability was $8.0 million and $7.3 million as of December 31, 2020 and 2019, respectively.

13. STOCK-BASED COMPENSATION

At the June 21, 2017 Annual Meeting of Stockholders of Southern National, the 2017 Equity Compensation Plan (the “2017 Plan”) was approved as recommended by the Board of Directors. The 2017 Plan replaced the 2010 Plan and has a maximum number of 750,000 shares reserved for issuance. The purpose of the 2017 Plan is to promote the success of the

Company by providing greater incentives to employees, non-employee directors, consultants and advisors to associate their personal interests with the long-term financial success of the Company, including its subsidiaries, and with growth in stockholder value, consistent with the Company's risk management practices. Because the 2017 Plan was approved, shares under the 2004 stock-option plan and 2010 Plan are no longer awarded.

A summary of the activity in the stock option plan for 2020 follows:

	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value (in thousands)
Options outstanding, beginning of period	555,750	$ 10.02	4.3	$ 3,518
Forfeited	(11,700)	10.91		
Exercised	(93,250)	7.60		
Options outstanding, end of period	450,800	$ 10.50	3.8	$ 727
Exercisable at end of period	437,700	$ 10.37	3.7	$ 726

Stock-based compensation expense associated with stock options was $118 thousand, $62 thousand and $122 thousand for the years ended December 31, 2020, 2019 and 2018, respectively. As of December 31, 2020, we do not have any unrecognized compensation expense associated with the stock options.

A summary of the activity in the restricted stock plan for 2020 follows:

	Shares	Weighted Average Grant-Date Fair Value Per Share	Weighted Average Remaining Contractual Term
Unvested restricted stock outstanding, beginning of period	86,500	$ 14.85	3.8
Granted	102,500	14.56	
Vested	(92,700)	15.22	
Unvested restricted stock outstanding, end of period	96,300	$ 14.17	3.8

Restricted stock compensation expense totaled $1.4 million, $370 thousand and $158 thousand for the years ended December 31, 2020, 2019 and 2018, respectively. As of December 31, 2020, unrecognized compensation expense associated with restricted stock was $1.2 million, which is expected to be recognized over a weighted average period of 3.9 years.

14. FINANCIAL INSTRUMENTS WITH OFF-BALANCE SHEET RISK

Financial Instruments with off-balance sheet risk

Southern National is a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit, standby letters of credit and guarantees of credit card accounts. These instruments involve elements of credit and funding risk in excess of the amount recognized in the consolidated balance sheet. Letters of credit are written conditional commitments issued by Southern National to guarantee the performance of a customer to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loans to customers. We had letters of credit outstanding totaling $15.9 million and $17.7 million as of December 31, 2020 and 2019, respectively.

Our exposure to credit loss in the event of nonperformance by the other party to the financial instruments for commitments to extend credit and letters of credit is based on the contractual amount of these instruments. We use the same credit policies in making commitments and conditional obligations as we do for on-balance sheet instruments. Unless noted otherwise, we do not require collateral or other security to support financial instruments with credit risk.

Allowance For Credit Losses - Off-Balance-Sheet Credit Exposures

The allowance for credit losses on off-balance-sheet credit exposures is a liability account, calculated in accordance with ASC 326, representing expected credit losses over the contractual period for which we are exposed to credit risk resulting from a contractual obligation to extend credit. No allowance is recognized if we have the unconditional right to cancel the obligation. Off-balance-sheet credit exposures primarily consist of amounts available under outstanding lines of credit and letters of credit detailed above. For the period of exposure, the estimate of expected credit losses considers both the likelihood that funding will occur and the amount expected to be funded over the estimated remaining life of the commitment or other off-balance-sheet exposure. The likelihood and expected amount of funding are based on historical utilization rates. The amount of the allowance represents management's best estimate of expected credit losses on commitments expected to be funded over the contractual life of the commitment. Estimating credit losses on amounts expected to be funded uses the same methodology as described for loans in Note 3 - Loans and Allowance, as if such commitments were funded.

The following table details activity in the allowance for credit losses on off-balance-sheet credit exposures:

	2020
Balance as of January 1	$ —
Impact of adopting ASU 2016-13	360
Credit loss expense	380
Balance as of December 31,	$ 740

Commitments

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 are made predominately for adjustable rate loans, and generally have fixed expiration dates of up to three months or other termination clauses and usually require payment of a fee. Since many of the commitments may expire without being completely drawn upon, the total commitment amounts do not necessarily represent future cash requirements. We evaluate each customer’s creditworthiness on a case-by-case basis.

At December 31, 2020 and 2019, we had unfunded lines of credit and undisbursed construction loan funds totaling $355.3 million and $324.8 million, respectively. Virtually all of our unfunded lines of credit and undisbursed construction loan funds are variable rate.

15. EARNINGS PER SHARE

The following is a reconciliation of the denominators of the basic and diluted EPS computations for 2020, 2019 and 2018 (amounts in thousands, except per share data):

	Income (Numerator)	Weighted Average Shares (Denominator)	Per Share Amount
For the year ended December 31, 2020			
Basic EPS	$ 23,287	24,239	$ 0.96
Effect of dilutive stock options and unvested restricted stock	—	124	—
Diluted EPS	$ 23,287	24,363	$ 0.96
For the year ended December 31, 2019			
Basic EPS	$ 33,167	24,050	$ 1.38
Effect of dilutive stock options and unvested restricted stock	—	275	(0.02)
Diluted EPS	$ 33,167	24,325	$ 1.36
For the year ended December 31, 2018			
Basic EPS	$ 33,691	24,012	$ 1.40
Effect of dilutive stock options and unvested restricted stock	—	261	(0.01)
Diluted EPS	$ 33,691	24,273	$ 1.39

The Company had 226,300 anti-dilutive options as of December 31, 2020 and did not have any anti-dilutive options as of December 31, 2019 and 2018.

16. REGULATORY MATTERS

Southern National and its subsidiary 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 - actions by regulators that, if undertaken, could have a direct material effect on our financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action (“PCA”), we must meet specific capital guidelines that involve quantitative measures of our assets, liabilities and certain off-balance sheet items as calculated under regulatory accounting practices. The capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings and other factors. At December 31, 2020 and 2019, the most recent regulatory notifications categorized the Bank as well capitalized under regulatory framework for PCA.

Quantitative measures established by regulation to ensure capital adequacy require Southern National to maintain minimum amounts and ratios of Total and Tier I capital (as defined in the regulations) to average assets (as defined). Management believes, as of December 31, 2020, that Southern National meets all capital adequacy requirements to which it is subject.

The following table provides a comparison of the leverage and risk-weighted capital ratios of Sonabank at the periods indicated to the minimum and well-capitalized required regulatory standards:

	Actual		Required For Capital Adequacy Purposes		To Be Categorized as Well Capitalized [1]	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
December 31, 2020						
Sonabank						
Common equity tier 1 capital ratio	$ 334,540	15.83 %	$ 95,078	4.50 %	$ 137,334	6.50 %
Tier 1 risk-based capital ratio	334,540	15.83 %	126,770	6.00 %	169,027	8.00 %
Total risk-based capital ratio	361,073	17.09 %	169,027	8.00 %	211,284	10.00 %
Leverage ratio	334,540	11.25 %	124,046	4.00 %	105,642	5.00 %
December 31, 2019						
Sonabank						
Common equity tier 1 capital ratio	$ 313,354	14.81 %	$ 95,229	4.50 %	$ 137,553	6.50 %
Tier 1 risk-based capital ratio	313,354	14.81 %	126,972	6.00 %	169,296	8.00 %
Total risk-based capital ratio	323,615	15.29 %	169,296	8.00 %	211,619	10.00 %
Leverage ratio	313,354	12.07 %	103,838	4.00 %	105,810	5.00 %

(1) Prompt corrective action provisions are not applicable at the bank holding company level.

Sonabank is required to meet minimum capital requirements set forth by regulatory authorities. Bank regulatory agencies have approved regulatory capital guidelines ("Basel III") aimed at strengthening existing capital requirements for banking organizations. The Basel III Capital Rules require Sonabank to maintain (i) a minimum ratio of Common Equity Tier 1 capital to risk-weighted assets of at least 4.5%, plus a 2.5% "capital conservation buffer", (ii) a minimum ratio of Tier 1 capital to risk-weighted assets of at least 6.0%, plus the capital conservation buffer, (iii) a minimum ratio of Total capital to risk-weighted assets of at least 8.0%, plus the capital conservation buffer and (iv) a minimum leverage ratio of 4.0%. Failure to meet minimum capital requirements may result in certain actions by regulators which could have a direct material effect on the consolidated financial statements.

Sonabank remains well-capitalized under Basel III capital requirements. Sonabank had capital conservation buffer of 9.09% at December 31, 2020, which exceeded the 2.50% minimum requirement below which the regulators may impose limits on distributions.

Southern National's principal source of funds for dividend payments is dividends received from the Bank. Banking regulations limit the amount of dividends that may be paid without prior approval of regulatory agencies. Under these regulations, the amount of dividends that may be paid in any calendar year is limited to the current year's net profits, combined with the retained net profits of the preceding two years, subject to the capital requirements described above.

17. PARENT COMPANY FINANCIAL INFORMATION

Condensed financial information of Southern National Bancorp of Virginia, Inc. follows (in thousands):

CONDENSED BALANCE SHEETS
DECEMBER 31,

	2020	2019
ASSETS		
Cash	$ 59,318	$ 2,707
Investment in subsidiaries	446,116	423,591
Other assets	2,060	8,128
Total assets	$ 507,494	$ 434,426
LIABILITIES AND STOCKHOLDERS' EQUITY		
Liabilities:		
Junior subordinated debt - long term	$ 9,682	$ 9,632
Senior subordinated notes - long term	105,647	47,051
Other liabilities	1,611	502
Total liabilities	116,940	57,185
Stockholders' equity:		
Common stock	243	241
Additional paid in capital	308,870	306,755
Retained earnings	77,956	69,462
Accumulated other comprehensive income	3,485	783
Total stockholders' equity	390,554	377,241
Total liabilities and stockholders' equity	$ 507,494	$ 434,426

CONDENSED STATEMENTS OF INCOME
FOR THE YEARS ENDED DECEMBER 31,

	2020	2019	2018
Income:			
Cash dividends received from subsidiaries	$ 2,500	$ 13,300	$ 8,000
Total income	2,500	13,300	8,000
Expenses:			
Interest on junior subordinated debt	426	589	575
Interest on senior subordinated notes	3,909	2,847	2,847
Other operating expenses	841	726	765
Total expenses	5,176	4,162	4,187
Income (loss) before income tax benefit and equity in undistributed net income of subsidiaries	(2,676)	9,138	3,813
Income tax benefit	(1,084)	(862)	(872)
Equity in undistributed net income of subsidiaries	24,879	23,167	29,006
Net income	$ 23,287	$ 33,167	$ 33,691

CONDENSED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31,

	2020	2019	2018
Operating activities:			
Net income	$ 23,287	$ 33,167	$ 33,691
Adjustments to reconcile net income to net cash and cash equivalents (used in) provided by operating activities:			
Equity in undistributed net income of subsidiaries	(27,379)	(36,467)	(37,006)
Other, net	8,766	(666)	(582)
Net cash and cash equivalents provided by (used in) in operating activities	4,674	(3,966)	(3,897)
Investing activities:			
Dividend from subsidiaries	2,500	13,300	8,000
Net cash and cash equivalents provided by investing activities	2,500	13,300	8,000
Financing activities:			
Issuance of subordinated notes, net of cost	58,600	—	—
Issuance of common stock under Stock Incentive Plan	574	670	443
Cash dividends paid on common stock	(9,737)	(8,690)	(7,688)
Net cash and cash equivalents provided by (used in) financing activities	49,437	(8,020)	(7,245)
Increase (decrease) in cash and cash equivalents	56,611	1,314	(3,142)
Cash and cash equivalents at beginning of period	2,707	1,393	4,535
Cash and cash equivalents at end of period	$ 59,318	$ 2,707	$ 1,393

18. ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)

The following is a summary of the accumulated other comprehensive income (loss) balances, net of tax (in thousands):

	Balance at December 31, 2019	Current Period Change	Balance at December 31, 2020
Unrealized gain on investment securities available for sale	$ 943	$ 2,203	$ 3,146
Reclassification of loss on sales of investment securities	—	490	490
Unrecognized gain on investment securities held to maturity for which other than temporary impairment charges have been taken	311	—	311
Unrealized gain (loss) on investment securities available for sale transferred to held to maturity	(471)	9	(462)
Total	$ 783	$ 2,702	$ 3,485

19. RELATED PARTY TRANSACTIONS

Sonabank has entered into loan transactions with STM. The following table summarizes the changes in the loan amount outstanding with STM during the periods indicated (in thousands):

	2020	2019
Balance at January 1,	$ 26,760	$ 24,168
Principal advances	441,044	298,639
Principal paid	(437,033)	(296,047)
Balance at December 31,	$ 30,771	$ 26,760

We purchased loans in an aggregate amount of $80.6 million and $152.2 million during 2020 and 2019, respectively, from STM.

During the year, officers, directors, principal shareholders, and their affiliates (related parties) were customers of and had transactions with the Company. Loan activity to related parties is as follows (in thousands):

	2020
Balance at January 1,	$ 22,670
Principal advances	4,459
Principal paid	(4,420)
Balance at December 31,	$ 22,709

Sonabank has also entered into deposit transactions with its related parties including STM. The aggregate amount of these deposit accounts were $25.2 million and $20.1 million as of December 31, 2020 and 2019, respectively.

20. QUARTERLY FINANCIAL DATA (UNAUDITED)

	Interest Income	Net Interest Income	Income Before Taxes	Net Income	Earnings Per Share Basic	Earnings Per Share Diluted
	(dollars in thousands, except per share amounts)					
2020						
First quarter	$ 28,481	$ 20,515	$ 33	$ 27	$ —	$ —
Second quarter	28,672	22,473	5,897	4,709	0.19	0.19
Third quarter	28,707	22,998	12,005	9,588	0.40	0.39
Fourth quarter	31,920	25,654	11,966	8,963	0.37	0.37
2019						
First quarter	$ 30,303	$ 20,952	$ 7,524	$ 6,020	$ 0.25	$ 0.25
Second quarter	30,393	20,964	10,263	9,319	0.39	0.38
Third quarter	30,474	21,015	11,225	8,864	0.37	0.36
Fourth quarter	29,354	20,669	10,232	8,964	0.37	0.37

21. LOW INCOME HOUSING TAX CREDITS

The general purpose of housing equity funds is to encourage and assist participants in investing in low-income residential rental properties located in the Commonwealth of Virginia, develop and implement strategies to maintain projects as low-income housing, deliver Federal Low Income Housing Credits to investors, allocate tax losses and other possible tax benefits to investors, and to preserve and protect project assets. The investments in these funds were recorded as other assets on the consolidated balance sheets and were carried at $5.1 million and $6.0 million at December 31, 2020 and 2019, respectively. These investments and related tax benefits have expected terms through 2034, with the majority maturing by 2027. Tax credits, net of amortization recognized related to these investments during the years ended December 31, 2020 and 2019 were $(225) thousand and $255 thousand, respectively. Total projected tax credits to be received for 2020 are $405 thousand, which is based on the most recent quarterly estimates received from the funds. Additional capital calls expected for the funds totaled $2.9 million and $3.8 million at December 31, 2020 and 2019, respectively.

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

None.

Item 9A. Controls and Procedures

(a) Evaluation of Disclosure Controls and Procedures. As of the end of the period covered by this Annual Report on Form 10-K, under the supervision and with the participation of management, including our chief executive officer and chief financial officer, we have evaluated the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d -15(e) under the Securities Exchange Act of 1934) utilizing the framework established in “Internal Control – Integrated Framework (2013)” issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based upon that evaluation, our chief executive officer and chief financial officer have concluded that these controls and procedures are effective as of the end of the period covered by this Annual Report on Form 10-K.

Disclosure controls and procedures are our controls and other procedures that are designed to ensure that information required to be disclosed by us in the reports that we file or submit under the Securities Exchange Act of 1934 is accumulated and communicated to our management, including our principal executive officer and principal financial officer, as appropriate, to allow timely decisions regarding required disclosure.

*(b) Management’s Report on Internal Control Over Financial Reporting***.** Management of Southern National is responsible for establishing and maintaining adequate internal control over financial reporting for Southern National (“we” and “our”), as that term is defined in Exchange Act Rules 13a-15(f). Southern National conducted an evaluation of the effectiveness of our internal control over Southern National’s financial reporting as of December 31, 2020 based on the framework in “Internal Control-Integrated Framework (2013)” issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on that evaluation, we concluded that our internal control over financial reporting is effective as of December 31, 2020.

Dixon Hughes Goodman LLP, an independent registered public accounting firm, has audited the consolidated financial statements included in this Annual Report and has issued a report on the effectiveness of our internal control over financial reporting, which report is included in "Part II - Item 8. Financial Statements and Supplementary Data" of this Report.

(c) Changes in Internal Control over Financial Reporting. There have been no changes in our internal control over financial reporting that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Item 9B. Other Information

None.

PART III

Item 10. Directors, Executive Officers and Corporate Governance

The information under the captions "Election of Directors," "Continuing Directors and Executive Officers," "Corporate Governance — Committees of the Board of Directors— Audit Committee," "Corporate Governance — Director Nominations Process" and "Corporate Governance — Code of Ethics" in Southern National's definitive Proxy Statement for its 2021 Annual Meeting of Shareholders to be filed with the SEC within 120 days after December 31, 2020 pursuant to Regulation 14A under the Exchange Act (the "2021 Proxy Statement"), is incorporated herein by reference in response to this item.

Item 11. Executive Compensation

The information under the captions "Executive Compensation and Other Matters," "Director Compensation" and "Compensation Committee Report on Executive Compensation" in the 2021 Proxy Statement is incorporated herein by reference in response to this item.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Shareholder Matters

The information under the caption "Beneficial Ownership of Common Stock by Management of the Company and Principal Stockholders" in the 2021 Proxy Statement is incorporated herein by reference in response to this item.

The information required by this Item concerning securities authorized for issuance under equity compensation plans is incorporated herein by reference to Part II, Item 5 of this Annual Report on Form 10-K.

Item 13. Certain Relationships, Related Transactions and Director Independence

The information under the captions "Corporate Governance — Director Independence" and "Certain Relationships and Related Party Transactions" in the 2021 Proxy Statement is incorporated herein by reference in response to this item.

Item 14. Principal Accounting Fees and Services

The information under the caption "Fees and Services of Independent Registered Public Accounting Firm" in the 2021 Proxy Statement is incorporated herein by reference in response to this item.

PART IV

Item 15. Exhibits and Financial Statement Schedules

The following documents are filed as part of this report:

(a)(1) Financial Statements

The following consolidated financial statements and reports of independent registered public accounting firm are in Part II, Item 8:

Reports of Independent Registered Public Accounting Firm
Consolidated Balance Sheets - December 31, 2020 and 2019

Consolidated Statements of Income and Comprehensive Income - Years ended December 31, 2020, 2019 and 2018

Consolidated Statements of Changes in Stockholders' Equity - Years ended December 31, 2020, 2019 and 2018

Consolidated Statements of Cash Flows -Years ended December 31, 2020, 2019 and 2018

Notes to Consolidated Financial Statements

(a)(2) Financial Statement Schedules

All schedules are omitted since they are not required, are not applicable, or the required information is shown in the consolidated financial statements or notes thereto.

(a)(3) Exhibits

The following are filed or furnished, as noted below, as part of this Annual Report on Form 10-K and this list includes the Exhibit Index.

Exhibit No.	Description
3.1	Articles of Incorporation (incorporated herein by reference to Exhibit 3.1 to Southern National's Registration Statement on Form S-1 (Registration No. 333-136285) filed on August 4, 2006)
3.2	Certificate of Amendment to the Articles of Incorporation dated January 31, 2005 (incorporated herein by reference to Exhibit 3.2 to Southern National's Registration Statement on Form S-1 (Registration No. 333-136285) filed on August 4, 2006)
3.3	Certificate of Amendment to the Articles of Incorporation dated April 13, 2006 (incorporated herein by reference to Exhibit 3.3 to Southern National's Registration Statement on Form S-1 (Registration No. 333-136285) filed on August 4, 2006)
3.4	Amended and Restated Bylaws (incorporated by reference to Exhibit 3.1 to Southern National's Current Report on Form 8-K filed on October 22, 2020)
4.1	Specimen Stock Certificate of Southern National (incorporated herein by reference to Exhibit 4.1 to Southern National's Registration Statement on Form S-1 (Registration No. 333-136285))

Exhibit No.	Description
4.2	Form of Warrant Agreement (incorporated herein by reference to Exhibit 4.2 to Southern National's Registration Statement on Form S-1 (Registration No. 333-136285))
4.3	Form of Amendment to Warrant Agreement (incorporated herein by reference to Exhibit 4.3 to Southern National's Registration Statement on Form S-1 (Registration No. 333-136285))
4.4	Form of 5.875% Fixed-to-Floating Rate Subordinated Notes due January 31, 2027 (incorporated herein by reference to Exhibit 10.1 to Southern National's Current Report on Form 8-K filed on January 24, 2017)
4.5*	Description of Registrant's Securities

Certain instruments relating to long-term debt as to which the total amount of securities authorized there under does not exceed 10% of the total assets of Southern National Bancorp of Virginia, Inc. have been omitted in accordance with Item 601(b)(4)(iii) of Regulation S-K. The registrant will furnish a copy of any such instrument to the Securities and Exchange Commission upon its request.

Exhibit No.	Description
4.6	Subordinated Indenture, dated as of August 25, 2020, between Southern National Bancorp of Virginia, Inc. and Wilmington Trust, National Association (incorporated herein by reference to Exhibit 4.1 to Southern National's Current Report on Form 8-K filed on August 25, 2020)
4.7	First Supplemental Indenture, dated as of August 25, 2020, between Southern National Bancorp of Virginia, Inc. and Wilmington Trust, National Association (incorporated herein by reference to Exhibit 4.2 to Southern National's Current Report on Form 8-K filed on August 25, 2020)
4.8	Form of 5.40% Fixed-to-Floating Rate Subordinated Notes due 2030 (included in Exhibit 4.7)
10.1+	Form of Southern National Bancorp of Virginia, Inc. Incentive Stock Option Agreement (incorporated herein by reference to Exhibit 10.3 to Southern National's Registration Statement on Form S-1/A filed on October 29, 2009 (Registration No. 333-162467))
10.2+	Supplemental Executive Retirement Plan for Georgia Derrico (incorporated herein by reference to Exhibit 10.4 to Southern National's Registration Statement on Form S-1/A filed on October 29, 2009 (Registration No. 333-162467))
10.3+	Supplemental Executive Retirement Plan for Rod Porter (incorporated herein by reference to Exhibit 10.5 to Southern National's Registration Statement on Form S-1/A filed on October 29, 2009 (Registration No. 333-162467))
10.4+	Southern National Bancorp of Virginia, Inc. 2010 Stock Awards and Incentive Plan (incorporated herein by reference to Exhibit 4.2 to Southern National's Registration Statement on Form S-8 (Registration No. 333-166511))
10.5+	Southern National Bancorp of Virginia, Inc. 2017 Equity Compensation Plan (incorporated herein by reference to Appendix A of Southern National's Definitive Proxy Statement on Schedule 14A filed with the Securities and Exchange Commission on May 11, 2017)
10.6+	Form of Southern National Bancorp of Virginia, Inc. Incentive Stock Option Agreement (incorporated herein by reference to Exhibit 4.3 to Southern National's Registration Statement on Form S-8 (Registration No. 333-166511))

Exhibit No.	Description
10.7+	Southern National Bancorp of Virginia, Inc. Supplemental Executive Retirement Plan (incorporated herein by reference to Exhibit 10.9 to Southern National's Current Report on Form 8-K filed on June 26, 2017)
10.8+	Southern National Bancorp of Virginia, Inc. Executive Severance Plan (incorporated herein by reference to Exhibit 10.10 to Southern National's Current Report on Form 8-K filed on June 26, 2017)
10.9+	Form of Subordinated Note Purchase Agreement, dated January 20, 2017 (incorporated herein by reference to Exhibit 10.1 to Southern National's Current Report on Form 8-K filed on January 24, 2017)
10.10+	Employment Agreement, dated as of February 28, 2019, by and between George C. Sheflett and Southern National Bancorp of Virginia, Inc. (incorporated herein by reference to Exhibit 10.1 to Southern National's Quarterly Report on Form 10-Q filed on May 9, 2019)
10.11+	Supplemental Executive Retirement Plan, dated as of April 2, 2018, by and between Sonabank and Georgia S. Derrico (incorporated herein by reference to Exhibit 10.3 to Southern National's Current report on Form 8-K filed April 24, 2019)
10.12+	Supplemental Executive Retirement Plan, dated as of April 2, 2018, by and between Sonabank and R. Roderick Porter (incorporated herein by reference to Exhibit 10.4 to Southern National's Current report on Form 8-K filed April 24, 2019)
10.13+	Supplemental Executive Retirement Plan, dated as of April 2, 2018, by and between Sonabank and Joe A. Shearin (incorporated herein by reference to Exhibit 10.5 to Southern National's Current report on Form 8-K filed April 24, 2019)
10.14+	Separation Agreement, dated as of February 20, 2020, by and between Joe A. Shearin and Southern National Bancorp of Virginia, Inc. (incorporated herein by reference to Exhibit 10.1 to Southern National's Quarterly Report on Form 10-Q filed on May 8, 2020)
10.15+	Employment Agreement, dated as of February 20, 2020, by and between Dennis J. Zember, Jr. and Southern National Bancorp of Virginia, Inc. (incorporated herein by reference to Exhibit 10.2 to Southern National's Quarterly Report on Form 10-Q filed on May 8, 2020)
10.16+	Separation Agreement, dated as of March 30, 2020, by and between Georgia S. Derrico and Southern National Bancorp of Virginia, Inc. (incorporated herein by reference to Exhibit 10.3 to Southern National's Quarterly Report on Form 10-Q filed on May 8, 2020)
10.17+	Separation Agreement, dated as of March 30, 2020, by and between R. Roderick Porter and Southern National Bancorp of Virginia, Inc. (incorporated herein by reference to Exhibit 10.4 to Southern National's Quarterly Report on Form 10-Q filed on May 8, 2020)
21.0*	Subsidiaries of the Registrant
23.1*	Consent of Dixon Hughes Goodman LLP
31.1*	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes- Oxley Act of 2002
31.2*	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes- Oxley Act of 2002
32.1**	Certification of Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

Exhibit No.	Description
99.1**	Financial Statements of Southern Trust Mortgage, LLC. for the years ended December 31, 2020, 2019 and 2018 together with Independent Auditor's Reports thereon; a mortgage affiliate of the company.
101	The following materials from Southern National Bancorp of Virginia, Inc.'s Annual Report on Form 10-K for the year ended December 31, 2020, formatted in Extensible Business Reporting Language (Inline XBRL), filed herewith: (i) Consolidated Balance Sheets, (ii) Consolidated Statements of Income and Comprehensive Income, (iii) Consolidated Statements of Changes in Stockholders' Equity, (iv) Consolidated Statements of Cash Flows, and (v) Notes to Consolidated Financial Statements.
104	The cover page from Southern National Bancorp of Virginia, Inc.'s Annual Report on Form 10-K for the year ended December 31, 2020, formatted in Inline XBRL.

+ Management contract or compensatory plan or arrangement
* Filed herewith
** Furnished herewith

Item 16. - Form 10-K Summary

None.

Southern National Bancorp of Virginia, Inc. will furnish, upon written request, a copy of any exhibit listed above upon the payment of a reasonable fee covering the expense of furnishing the copy. Requests should be directed to:

Matthew Switzer, Executive Vice President and Chief Financial Officer
Southern National Bancorp of Virginia, Inc.
10900 Nuckols Road, Suite 325
Glen Allen, Virginia 23060

SIGNATURES

Pursuant to the requirements 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.

Southern National Bancorp of Virginia, Inc.

By: /s/ Dennis J. Zember, Jr. Date: March 16, 2021
Dennis J. Zember, Jr.
President and Chief Executive Officer

By: /s/ Matthew Switzer Date: March 16, 2021
Matthew Switzer
Executive Vice President and Chief Financial Officer

Pursuant to the requirements of the 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.

Date: March 16, 2021

Signature	Title
/s/ Dennis J. Zember, Jr. Dennis J. Zember, Jr.	President and Chief Executive Officer, Director
/s/ John F. Biagas John F. Biagas	Director
/s/ Robert Y. Clagett Robert Y. Clagett	Director
/s/ W. Rand Cook W. Rand Cook	Director
/s/ Deborah Diaz Deborah Diaz	Director
/s/ F. L. Garrett, III F. L. Garrett, III	Director
/s/ W. Bruce Jennings W. Bruce Jennings	Director
/s/ Eric A. Johnson Eric A. Johnson	Director
/s/ Charles A. Kabbash Charles A. Kabbash	Director

Exhibit 4.5

DESCRIPTION OF THE REGISTRANT'S SECURITIES REGISTERED PURSUANT TO SECTION 12 OF THE SECURITIES EXCHANGE ACT OF 1934

As of March 5, 2021, Southern National Bancorp of Virginia, Inc. ("SONA") has one class of securities, our common stock, registered under Section 12 of the Securities Exchange Act of 1934, as amended.

DESCRIPTION OF COMMON STOCK

The following description of the terms and provisions of our common stock is qualified in its entirety by reference to our amended Articles of Incorporation, Amended and Restated Bylaws or Virginia law applicable to us. For a more thorough understanding of the terms of our capital stock, you should refer to our amended Articles of Incorporation and Amended and Restated Bylaws, which are included as exhibits to this Annual Report on Form 10-K.

General

We are authorized to issue 50,000,000 shares of capital stock of which 45,000,000 are shares of common stock and 5,000,000 are shares of preferred stock, par value $0.01 per share. As of March 5, 2021, there were 24,438,545 shares of common stock outstanding held by 1,347 holders of record and no shares of preferred stock issued and outstanding.

Common Stock

General. Each share of SONA common stock has the same relative rights as, and is identical in all respects to, each other share of SONA common stock. SONA's common stock is traded on the NASDAQ Global Market under the symbol "SONA."

Dividends. SONA's shareholders are entitled to receive dividends or distributions that its board of directors may declare out of funds legally available for those payments. The payment of distributions by SONA is subject to the restrictions of Virginia law applicable to the declaration of distributions by a corporation. A Virginia corporation generally may not authorize and make distributions if, after giving effect to the distribution, it would be unable to meet its debts as they become due in the usual course of business or if the corporation's total assets would be less than the sum of its total liabilities plus the amount that would be needed, if it were dissolved at that time, to satisfy the preferential rights of shareholders whose rights are superior to the rights of those receiving the distribution. In addition, the payment of distributions to shareholders is subject to any prior rights of outstanding preferred stock.

As a bank holding company, SONA's ability to pay dividends is affected by the ability of Sonabank, its bank subsidiary, to pay dividends to the holding company. The ability of Sonabank, as well as SONA, to pay dividends in the future is, and could be further, influenced by bank regulatory requirements and capital guidelines.

Liquidation Rights. In the event of any liquidation, dissolution or winding up of SONA, the holders of shares of its common stock will be entitled to receive, after payment of all debts and liabilities of SONA and after satisfaction of all liquidation preferences applicable to any preferred stock, all remaining assets of SONA available for distribution in cash or in kind.

Voting Rights. The holders of SONA common stock are entitled to one vote per share and, in general, a majority of votes cast with respect to a matter is sufficient to authorize action upon routine matters. Holders of SONA common stock are not entitled to cumulative voting rights. Directors are

elected by a plurality of the votes cast, and shareholders do not have the right to cumulate their votes in the election of directors.

Directors and Classes of Directors. SONA's board of directors is divided into three classes with directors serving staggered three-year terms. Any newly created directorships or any decrease in directorships are apportioned among the classes as evenly as possible. Under SONA's articles of incorporation, directors may be removed for cause upon the affirmative vote of not less than 75% of the outstanding shares entitled to vote generally in an election of directors. Cause for removal exists only if a director whose removal is proposed has been either declared incompetent by an order of a court, convicted of a felony or of an offense punishable by imprisonment for a term of more than one year, or deemed liable by a court for gross negligence or misconduct in the performance of such director's duties to SONA.

No Preemptive Rights; Redemption and Assessment. Holders of shares of SONA will not be entitled to preemptive rights with respect to any shares that may be issued. SONA common stock is not subject to redemption or any sinking fund and the outstanding shares are fully paid and nonassessable.

Anti-Takeover Effects of Certain Provisions in Our Amended Articles of Incorporation and Amended and Restated Bylaws and Virginia Law

Subject to the application of the Virginia Stock Corporation Act (VSCA), the affirmative vote of the holders of more than two thirds of all votes entitled to be cast is generally required with respect to a merger, exchange offer or the sale of all or substantially all of our assets. Under the VSCA and our amended Articles of Incorporation, any action required or permitted to be taken by our shareholders may be taken without a meeting and without a shareholder vote if a written consent is signed by the holders of the shares of outstanding stock having not less than the minimum number of votes that would be necessary to authorize such action at a meeting of shareholders at which all shares entitled to vote on such matter were present and voted.

Virginia law provides for certain restrictions on extraordinary corporate transactions that may discourage the acquisition of control of Virginia corporations. We elected to "opt out" of those protective provisions.

The provisions described below, to the extent applicable, will have the general effect of discouraging, or rendering more difficult, unfriendly takeover or acquisition attempts. Consequently, such provisions would be beneficial to current management in an unfriendly takeover attempt, but could have an adverse effect on shareholders who might wish to participate in such a transaction. However, we believe that such provisions are advantageous to our shareholders in that they will permit management and our shareholders to carefully consider and understand a proposed acquisition, lead to higher offering prices, and require a higher level of shareholder participation in the decision if the transaction is not approved by our board of directors.

Staggered Board and Removal of Directors

One class of our three classes of directors is elected annually. Directors serve for three-year terms. There is no cumulative voting for directors provided for in the amended Articles of Incorporation. As permitted by Virginia law, our amended Articles of Incorporation provide that where a corporation's directors are elected in classes that a director, or the entire board of directors, only may be removed for cause by the affirmative vote of not less than 75% of the shares entitled to vote generally in an election of directors. The provisions contained in our amended Articles of Incorporation relating to election of directors in staggered three-year classes and the supermajority vote required to remove a director tend to discourage attempts by third parties to acquire us because of the extra time and expense involved and a greater possibility of failure. This also can affect the price that a potential purchaser would be willing to

pay for our common stock, thereby reducing the amount a shareholder would receive in, for example, a tender offer for our common stock.

Special Shareholder Meetings

Our amended Articles of Incorporation also restrict the manner in which special meetings may be called. Under the VSCA, a corporation is permitted to provide for calling of special meetings either in its bylaws or articles of incorporation. Our amended Articles of Incorporation specify that special meetings may be called by our Chairman of the Board or President or by the affirmative vote of three-fourths of the board of directors or by holders of record of not less than 40% of our then outstanding voting shares.

Evaluation of Change in Control Offers

Our amended Articles of Incorporation also provide that when evaluating any offer that may result in a change in control of our company, the board of directors may consider, consistent with the exercise of its fiduciary duties and in connection with the exercise of its judgment in determining what is in the best interests of our company and our shareholders, not only the price or other consideration being offered, but also all other relevant factors including, without limitation, the financial and management resources and future prospects of the other party, the possible effect on our business and the business of our subsidiaries and on our employees, customers, suppliers and creditors and those of our subsidiaries, the effects on the ability of our company to fulfill its corporate objectives as a holding company and on the ability of Sonabank to fulfill its objectives as a bank, and the effects on the communities in which our facilities are located.

Blank Check Preferred Stock

In addition to common stock, our amended Articles of Incorporation permit the board of directors to issue up to 5,000,000 shares of “blank check” preferred stock. Among other things, the board of directors in issuing a series of preferred stock has the power to determine voting powers, if any, of such series. Such issuance of preferred stock having voting rights could dilute the voting and ownership interest of existing shareholders. Such issuance may have the effect of discouraging unilateral attempts by third parties to obtain control of our company, since the issuance of additional shares of capital stock could be used to dilute the voting power of, or increase the cost to, any person seeking to obtain control of us. This may occur by virtue of the fact that the preferred stock may be issued in a series having rights in excess of one vote per share or having the right to vote separately by class respecting some matters.

Transfer Agent and Registrar

The transfer agent for SONA’s common stock is Computershare Inc., 250 Royall Street, Canton, Massachusetts 02021.

Exhibit 21.0

Subsidiaries of Southern National Bancorp of Virginia, Inc.

Subsidiary	State of Incorporation
Sonabank	Virginia
Eastern Virginia Statutory Trust I	Connecticut

Exhibit 23.1

CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

We consent to the incorporation by reference in the Registration Statements on Form S-3 (No. 333-237909) and Forms S-8 (Nos. 333-218976, 333-189730, 333-166511, and 333-138636) of our reports dated March 16, 2021, with respect to the consolidated financial statements of Southern National Bancorp of Virginia, Inc. (the “Company”) as of December 31, 2020 and 2019, and the related consolidated statements of income and comprehensive income, changes in stockholders’ equity and cash flows for each of the years in the three year period ended December 31, 2020, and the effectiveness of internal control over financial reporting as of December 31, 2020, which reports appear in the Company’s 2020 Annual Report on Form 10-K.

/s/ Dixon Hughes Goodman LLP

Greenville, NC
March 16, 2021

Consent of Independent Registered Public Accounting Firm

We consent to the incorporation by reference in the Registration Statements on Form S-3 (No. 333-237909) and Forms S-8 (Nos. 333-218976, 333-189730, 333-166511, and 333-138636) to the use of our reports dated March 12, 2021, with respect to the consolidated financial statements of Southern Trust Mortgage, LLC included in this Annual Report (Form 10-K) for the years ended December 31, 2020, 2019, and 2018.

/s/ Richey, May and Co., LLP

Englewood, Colorado
March 12, 2021

Exhibit 31.1

CERTIFICATIONS

I, Dennis J. Zember, Jr., certify that:

1. I have reviewed this report on Form 10-K of Southern National Bancorp of Virginia, Inc.;

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

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

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

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

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

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

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

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

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

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

Date: March 16, 2021

/s/ Dennis J. Zember, Jr.
Dennis J. Zember, Jr.,
President and Chief Executive Officer

Exhibit 31.2

CERTIFICATIONS

I, Matthew Switzer, certify that:

1. I have reviewed this report on Form 10-K of Southern National Bancorp of Virginia, Inc.;

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

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

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

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

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

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

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

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

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

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

Date: March 16, 2021

/s/ Matthew Switzer
Matthew Switzer,
Executive Vice President and Chief Financial Officer

Exhibit 32.1

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350
AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Annual Report of Southern National Bancorp of Virginia, Inc. ("Southern National") on Form 10-K for the period ending December 31, 2020 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), the undersigned Chief Executive Officer and Chief Financial Officer of Southern National hereby certify, pursuant to 18 U.S.C. §1350, as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002, that based on their knowledge and belief: 1) the Report 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 the Report fairly presents, in all material respects, the financial condition and results of operations of Southern National as of and for the periods covered in the Report.

/s/ Dennis J. Zember, Jr.
Dennis J. Zember, Jr.
President and Chief Executive Officer

/s/ Matthew Switzer
Matthew Switzer
Executive Vice President and Chief Financial Officer

March 16, 2021

Exhibit 99.1

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM AND FINANCIAL STATEMENTS FOR SOUTHERN TRUST MORTGAGE, LLC FOR THE YEARS ENDED DECEMBER 31, 2020, 2019 AND 2018

SOUTHERN TRUST MORTGAGE, LLC
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Assurance | Tax | Advisory

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors
Southern Trust Mortgage, LLC
Virginia Beach, Virginia

Opinion on the Financial Statements

We have audited the accompanying balance sheets of Southern Trust Mortgage, LLC (the Company) as of December 31, 2020 and 2019, and the related statements of operations, changes in members' equity, and cash flows for each of the three years in the period ended December 31, 2020, and the related notes (collectively, referred to as the financial statements). In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company at December 31, 2020 and 2019, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2020, in conformity with accounting principles generally accepted in the United States of America.

Basis for Opinion

These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the Company's financial statements based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (PCAOB) and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. As part of our audits we are required to obtain an understanding of internal control over financial reporting 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.

Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Critical Audit Matters

Critical audit matters are matters arising from the current period audit of the financial statements that were communicated or required to be communicated to the audit committee and that: (1) relate to accounts or disclosures that are material to the financial statements and (2) involved our especially challenging, subjective, or complex judgements. We determined that there are no critical audit matters.

Richey, May & Co., LLP.

We have served as Southern Trust Mortgage, LLC's auditor since 2014.

Richey, May & Co.

Englewood, Colorado
March 12, 2021

SOUTHERN TRUST MORTGAGE, LLC
BALANCE SHEETS

	December 31,	
ASSETS	**2020**	**2019**
CURRENT ASSETS		
Cash and cash equivalents	$ 16,100,165	$ 6,867,905
Restricted cash	1,581,252	360,458
Escrow cash	669,144	313,183
Mortgage loans held for sale, at fair value	143,434,684	100,223,953
Accounts receivable and advances	1,020,842	733,905
Derivative assets	10,199,245	1,932,676
Prepaid expenses and other current assets	499,014	589,023
Loans eligible for repurchase from GNMA	2,338,905	—
Total current assets	175,843,251	111,021,103
OTHER ASSETS		
Property and equipment, net	921,652	784,371
Mortgage servicing rights, net	1,694,970	6,750
Mortgage loans held for investment, net	2,081,000	3,308,201
Real estate owned	32,900	122,900
Due from related parties	174,400	393,339
Deposits and other assets	159,986	172,645
Total other assets	5,064,908	4,788,206
TOTAL ASSETS	$ 180,908,159	$ 115,809,309
LIABILITIES AND MEMBERS' EQUITY		
LIABILITIES		
Accounts payable and accrued expenses	$ 7,395,761	$ 3,527,203
Customer deposits and loan escrows	1,148,034	4,743,419
Warehouse lines of credit	136,087,177	92,052,015
Operating line of credit, related party	—	3,734,308
Derivative liabilities	2,496,602	74,922
Note payable, current portion	2,051,145	—
Liability for loans eligible for repurchase from GNMA	2,338,905	—
Loan indemnification reserve	1,325,068	593,287
Total current liabilities	152,842,692	104,725,154
Note payable, net of current portion	1,647,243	—
Total liabilities	154,489,935	104,725,154
COMMITMENTS AND CONTINGENCIES (Note O)		
MEMBERS' EQUITY		
Preferred interests, $1 par value; 3,304,656 shares authorized, issued and outstanding	3,304,656	3,304,656
Common interests, $0.057 par value; 8,783,212 shares authorized, issued and outstanding	500,000	500,000
Additional paid-in capital	344,575	344,575
Retained earnings	22,268,993	6,934,924
Total members' equity	26,418,224	11,084,155
TOTAL LIABILITIES AND MEMBERS' EQUITY	$ 180,908,159	$ 115,809,309

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

SOUTHERN TRUST MORTGAGE, LLC
STATEMENTS OF OPERATIONS

	Years Ended December 31,		
REVENUE	**2020**	**2019**	**2018**
Gain on sale of mortgage loans held for sale, net of direct costs of $6,528,911, $4,918,604 and $2,873,463, respectively	$ 107,063,928	$ 45,726,642	$ 27,166,592
Loan origination fees	9,341,728	4,871,817	2,693,451
Interest income	4,184,292	3,989,638	2,597,127
Interest expense	(5,045,267)	(5,215,135)	(2,992,447)
Loan servicing fees, net of direct costs of $315,922,$133,809 and $182,345, respectively	382,754	32,235	119,041
Gain on sale of mortgage servicing rights	—	337,865	—
Other income	139,317	53,595	92,000
Total revenue	116,066,752	49,796,657	29,675,764
EXPENSES			
Salaries, commissions and benefits	84,080,099	39,032,347	24,557,526
Occupancy, equipment and communication	3,519,608	3,353,159	2,914,415
General and administrative	4,866,432	3,895,578	3,227,331
Provision for loan losses	897,309	551,322	131,557
Depreciation and amortization	275,692	224,550	194,005
Loss on sale of real estate owned	31,607	3,600	—
Amortization and deletions of mortgage servicing rights	167,947	51,590	230,995
Total expenses	93,838,694	47,112,146	31,255,829
NET INCOME (LOSS)	$ 22,228,058	$ 2,684,511	$ (1,580,065)

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

SOUTHERN TRUST MORTGAGE, LLC
STATEMENTS OF CHANGES IN MEMBERS' EQUITY
FOR THE YEARS ENDED DECEMBER 31, 2020, 2019 AND 2018

	Preferred Interests		Common Interests		Additional Paid-In	Retained	
	Shares	Amount	Shares	Amount	Capital	Earnings	Totals
Balance, December 31, 2017	3,304,656	$3,304,656	8,783,212	$500,000	$ 344,575	$ 6,540,436	$ 10,689,667
Preferred dividends	—	—	—	—	—	(248,892)	(248,892)
Member distributions	—	—	—	—	—	(67,554)	(67,554)
Net loss	—	—	—	—	—	(1,580,065)	(1,580,065)
Balance, December 31, 2018	3,304,656	3,304,656	8,783,212	500,000	344,575	4,643,925	8,793,156
Preferred dividends	—	—	—	—	—	(249,312)	(249,312)
Member distributions	—	—	—	—	—	(144,200)	(144,200)
Net income	—	—	—	—	—	2,684,511	2,684,511
Balance, December 31, 2019	3,304,656	3,304,656	8,783,212	500,000	344,575	6,934,924	11,084,155
Preferred dividends	—	—	—	—	—	(247,039)	(247,039)
Member distributions	—	—	—	—	—	(6,646,950)	(6,646,950)
Net income	—	—	—	—	—	22,228,058	22,228,058
Balance, December 31, 2020	3,304,656	$3,304,656	8,783,212	$500,000	$ 344,575	$ 22,268,993	$ 26,418,224

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

SOUTHERN TRUST MORTGAGE, LLC

STATEMENTS OF CASH FLOWS

	Years Ended December 31,		
	2020	2019	2018
CASH FLOWS FROM OPERATING ACTIVITIES			
Net income (loss)	$ 22,228,058	$ 2,684,511	$ (1,580,065)
Non-cash items-			
Provision for loan losses	897,309	551,322	131,557
Depreciation and amortization	275,692	224,550	194,005
Amortization and deletions of mortgage servicing rights	167,947	51,590	230,995
Gain on sale of mortgage loans held for sale, net of direct costs	(107,063,928)	(45,726,642)	(27,166,592)
Gain on sale of mortgage servicing rights	—	(337,865)	—
Loss on sale of real estate owned	31,607	3,600	—
Loss on sale of mortgage loans held for investment	7,809	116,867	13,536
(Increase) decrease in-			
Escrow cash	(355,961)	(72,972)	(33,149)
Proceeds from sale and principal payments on mortgage loans held for sale	2,454,696,861	1,419,984,689	898,918,782
Originations and purchases of mortgage loans held for sale	(2,392,699,831)	(1,410,062,230)	(871,675,334)
Mortgage loans held for investment, net	(698,356)	(1,456,528)	(423,636)
Accounts receivable and advances	(286,937)	(196,024)	103,964
Derivative assets	(8,266,569)	(475,733)	(320,392)
Prepaid expenses and other current assets	90,009	(208,221)	156,922
Deposits and other assets	12,659	(8,232)	(13,732)
Due from related parties	218,939	46,019	(439,358)
Increase (decrease) in-			
Accounts payable and accrued expenses	3,906,866	1,465,591	(167)
Customer deposits and loan escrows	(3,595,385)	1,438,541	2,409,450
Derivative liabilities	2,421,680	(478,516)	477,657
Loan indemnification reserve	(183,882)	(465,205)	(244,619)
Net cash provided by (used in) operating activities	(28,195,413)	(32,920,888)	739,824
CASH FLOWS FROM INVESTING ACTIVITIES			
Purchases of property and equipment	(412,973)	(204,349)	(161,158)
Proceeds from sale of mortgage servicing rights	—	566,157	—
Proceeds from sale of real estate owned	58,393	—	—
Proceeds from sale of mortgage loans held for investment	1,836,102	1,765,519	375,519
Net cash provided by investing activities	1,481,522	2,127,327	214,361
CASH FLOWS FROM FINANCING ACTIVITIES			
Net borrowings (repayments) under warehouse lines of credit	44,035,162	32,588,987	(3,165,139)
Net borrowings (repayments) under operating line of credit, related party	(3,734,308)	68,204	372,242
Borrowings under note payable	3,698,388	—	—
Preferred dividends	(185,347)	(187,037)	(248,892)
Member distributions	(6,646,950)	(144,200)	(67,554)
Net cash provided by (used in) financing activities	37,166,945	32,325,954	(3,109,343)

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

	Years Ended December 31,		
	2020	2019	2018
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS AND RESTRICTED CASH	10,453,054	1,532,393	(2,155,158)
CASH AND CASH EQUIVALENTS AND RESTRICTED CASH, BEGINNING OF YEAR	7,228,363	5,695,970	7,851,128
CASH AND CASH EQUIVALENTS AND RESTRICTED CASH, END OF YEAR	$ 17,681,417	$ 7,228,363	$ 5,695,970
SUPPLEMENTAL INFORMATION			
Cash paid for interest	$ 4,996,763	$ 5,165,733	$ 2,966,787
Preferred dividends payable	$ 61,692	$ 62,275	$ 62,066
NON-CASH OPERATING AND INVESTING ACTIVITIES			
The Company increased retained mortgage servicing rights in connection with loan sales.	$ 1,856,167	$ 15,094	$ 32,218
The Company recognized loans eligible for repurchase from GNMA and the related liability.	$ 2,338,905	$ —	$ —

The Company made a reclassification between loan indemnification reserve and accounts payable and accrued expenses totaling $100,000 during the year ended December 31, 2020.

The Company sold certain mortgage servicing rights for a sales price of $629,063, which was comprised of cash proceeds of $566,157 and a receivable of $62,906 during the year ended December 31, 2019.

A. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization
Southern Trust Mortgage, LLC (the Company) was incorporated in the Commonwealth of Virginia. The Company is primarily engaged in the business of originating, selling and servicing residential mortgage loans through its retail origination channel. The Company maintains its corporate office in Virginia Beach, Virginia, with branch offices in multiple states. The Company is approved as a Title II, non-supervised direct endorsement mortgagee with the United States Department of Housing and Urban Development (HUD). In addition, the Company is an approved issuer with the Government National Mortgage Association (GNMA), as well as an approved seller and servicer with the Federal National Mortgage Association (FNMA) and Federal Home Loan Mortgage Corporation (FHLMC).

Basis of Accounting
The financial statements of the Company are prepared on the accrual basis of accounting.

Basis of Presentation
The accompanying financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) as codified in the Financial Accounting Standards Board's (FASB) *Accounting Standards Codification* (ASC).

Use of Estimates
The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Consolidation, Variable Interest Entities
The Company sells mortgage loans to FNMA and FHLMC, which are government-sponsored enterprises. The Company may also issue GNMA securities by pooling eligible mortgage loans through a custodian and assigning rights to the mortgage loans to GNMA. FNMA, FHLMC and GNMA (the Agencies) provide credit enhancements for mortgage loans through certain guarantee provisions. These securitizations involve variable interest entities (VIEs) as the trusts or similar vehicles, by design, that either (1) lack sufficient equity to permit the entity to finance its activities without additional subordinated financial support from other parties, or (2) have equity investors that do not have the ability to make significant decisions relating to the entity's operations through voting rights, or do not have the obligation to absorb the expected losses, or do not have the right to receive the residual returns of the entity.

A. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Consolidation, Variable Interest Entities (Continued)

The primary beneficiary of a VIE (i.e., the party that has a controlling financial interest) is required to consolidate the assets and liabilities of the VIE. The primary beneficiary is the party that has both (1) the power to direct the activities of an entity that most significantly impact the VIE's economic performance; and (2) through its interests in the VIE, the obligation to absorb losses or the right to receive benefits from the VIE that could potentially be significant to the VIE. The Company may retain the right to service mortgage loans sold or securitized by the Agencies. Due to the significant influence of the Agencies over the VIEs that hold the assets from mortgage loan securitizations, principally through their rights and responsibilities as master servicer, the Company is not the primary beneficiary of the VIEs and therefore the VIEs are not consolidated.

The Company performs on-going reassessments of (1) whether entities previously evaluated under the majority voting-interest framework have become VIEs, based on certain events, and therefore become subject to the VIE consolidation framework; and (2) whether changes in the facts and circumstances regarding the Company's involvement with a VIE cause the Company's consolidation determination to change.

Cash and Cash Equivalents

For cash flow purposes, the Company considers cash and temporary investments with original maturities of three months or less, to be cash and cash equivalents. The Company has diversified its credit risk for cash by maintaining deposits in several financial institutions, which may at times exceed amounts covered by insurance from the Federal Deposit Insurance Corporation. The Company evaluates the creditworthiness of these financial institutions in determining the risk associated with these balances. The Company has not experienced any losses in such accounts and believes it is not exposed to any significant credit risk related to cash and cash equivalents.

Restricted Cash

The Company maintains certain cash balances that are restricted under warehouse agreements and broker margin accounts associated with its derivative instruments.

Mortgage Loans Held for Sale and Revenue Recognition

Mortgage loans held for sale are carried at fair value under the fair value option with changes in fair value recorded in gain on sale of mortgage loans held for sale on the statements of operations. The fair value of mortgage loans held for sale committed to investors is calculated using observable market information such as the investor purchase commitment, assignment of trade or other mandatory delivery commitment prices. The Company bases loans committed to Agency investors based on the Agency's quoted mortgage backed security (MBS) prices. The fair value of mortgage loans held for sale not committed to investors is based on quoted best execution secondary market prices. If no such quoted price exists, the fair value is determined using quoted prices for a similar asset or assets, such as MBS prices, adjusted for the specific attributes of that loan, which would be used by other market participants.

A. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Mortgage Loans Held for Sale and Revenue Recognition (Continued)

Gains and losses from the sale of mortgage loans held for sale are recognized based upon the difference between the sales proceeds and carrying value of the related loans upon sale and are recorded in gain on sale of mortgage loans held for sale on the statements of operations. Sales proceeds reflect the cash received from investors through the sale of the loan and servicing release premium. If the related mortgage servicing right (MSR) is sold servicing retained, the MSR addition is recorded in gain on sale of mortgage loans held for sale on the statements of operations. Gain on sale of mortgage loans held for sale also includes the unrealized gains and losses associated with the changes in the fair value of mortgage loans held for sale and the realized and unrealized gains and losses from derivative instruments.

Mortgage loans held for sale are considered sold when the Company surrenders control over the financial assets. Control is considered to have been surrendered when the transferred assets have been isolated from the Company, beyond the reach of the Company and its creditors; the purchaser obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets; and the Company does not maintain effective control over the transferred assets through either an agreement that both entitles and obligates the Company to repurchase or redeem the transferred assets before their maturity or the ability to unilaterally cause the holder to return specific assets. The Company typically considers the above criteria to have been met upon acceptance and receipt of sales proceeds from the purchaser.

Mortgage Loans Held for Investment, Net

Mortgage loans held for investment for which management has the intent and ability to hold for the foreseeable future or to maturity are carried at amortized cost reduced by a valuation allowance for estimated credit losses. Mortgage loans transferred from the held for sale category are transferred at the lower of cost or fair value, which becomes the new cost basis in the loans.

Loan Origination Fees

Loan origination fees represent revenue earned from originating mortgage loans. Loan origination fees generally represent a flat per-loan fee amount based on a percentage of the original principal loan balance and are recognized as revenue at the time the mortgage loans are funded. Loan origination expenses are charged to operations as incurred.

Interest Income

Interest income on mortgage loans held for sale is recognized for the period from loan funding to sale based upon the principal balance outstanding and contractual interest rates. Revenue recognition is discontinued when loans become 90 days delinquent, or when, in management's opinion, the recovery of principal and interest becomes doubtful and the mortgage loans held for sale are put on nonaccrual status.

A. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Revenue Recognition

FASB ASC 606, *Revenue from Contracts with Customers* (ASC 606), establishes principles for reporting information about the nature, amount, timing and uncertainty of revenue and cash flows arising from the entity's contracts to provide goods or services to customers. The core principle requires an entity to recognize revenue to depict the transfer of goods or services to customers in an amount that reflects the consideration that it expects to be entitled to receive in exchange for those goods or services recognized as performance obligations are satisfied. The majority of the Company's revenue generating transactions are not subject to ASC 606, including revenue generated from financial instruments, such as the Company's mortgage loans and derivatives, as well as revenue related to the Company's mortgage servicing activities.

Loan Servicing Fees and Expenses

Loan servicing fees represent revenue earned for servicing loans for various investors. Loan servicing fees are based on a contractual percentage of the outstanding unpaid principal balance and are recognized into revenue as the related mortgage payments are received. Loan servicing expenses are charged to operations as incurred.

Servicing Advances

Servicing advances represent escrows advanced by the Company on behalf of borrowers and investors to cover delinquent balances for property taxes, insurance premiums and other out-of- pocket costs. Servicing advances are made in accordance with the servicing agreements and are recoverable upon collection of future borrower payments, sale of loan collateral, reimbursement by investor, or mortgage insurance claims. The Company periodically reviews servicing advances for collectability and establishes a valuation allowance for estimated uncollectible amounts. No allowance has been recorded as of December 31, 2020 and 2019, as management has determined that all amounts are fully collectible.

A. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Property and Equipment, Net

Property and equipment is recorded at cost and depreciated or amortized using the straight line method over the estimated useful lives of the assets. The following is a summary of property and equipment at December 31:

	Useful lives (years)	2020	2019
Property and equipment, at cost			
Equipment	3-7	$ 1,234,632	$ 1,010,207
Furniture and fixtures	3-7	878,603	715,241
Software	3-5	180,187	180,187
Leasehold improvements	(a)	105,065	79,879
Total property and equipment, at cost		2,398,487	1,985,514
Accumulated depreciation and amortization			
Equipment		(801,417)	(608,190)
Furniture and fixtures		(507,803)	(430,232)
Software		(122,075)	(121,747)
Leasehold improvements		(45,540)	(40,974)
Total accumulated depreciation and amortization		(1,476,835)	(1,201,143)
Total property and equipment, net		$ 921,652	$ 784,371

(a) Amortized over the shorter of the related lease term or the estimated useful life of the assets.

The Company periodically assesses property and equipment for impairment whenever events or circumstances indicate the carrying amount of an asset may exceed its fair value. If property and equipment is considered impaired, the impairment losses will be recorded on the statements of operations. The Company did not recognize any impairment losses during the years ended December 31, 2020, 2019 and 2018.

A. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Derivative Instruments

The Company holds and issues derivative financial instruments such as interest rate lock commitments (IRLCs) and forward sale commitments. IRLCs are subject to price risk primarily related to fluctuations in market interest rates. To hedge the interest rate risk on mandatory IRLCs, the Company uses forward sale commitments, such as to-be-announced securities or mandatory delivery commitments with investors. Management expects these forward sale commitments to experience changes in fair value opposite to the changes in fair value of the IRLCs, thereby reducing earnings volatility. Forward sale commitments are also used to hedge the interest rate risk on mortgage loans held for sale that are not committed to investors and still subject to price risk. If the mandatory delivery commitments are not fulfilled, the Company pays a pair-off fee. Best effort forward sale commitments are also executed with investors, whereby certain loans are locked with a borrower and simultaneously committed to an investor at a fixed price. If the best effort IRLC does not fund, the Company has no obligation to fulfill the investor commitment.

The Company considers various factors and strategies in determining what portion of the IRLCs and uncommitted mortgage loans held for sale to economically hedge. FASB ASC 815-25, *Derivatives and Hedging*, requires that all derivative instruments be recognized as assets or liabilities on the balance sheets at their fair value. Changes in the fair value of the derivative instruments and gains and losses resulting from pairing-out of forward sale commitments are recognized in gain on sale of mortgage loans held for sale on the statements of operations in the period in which they occur. The Company accounts for all derivative instruments as free-standing derivative instruments and does not designate any for hedge accounting.

Mortgage Servicing Rights and Revenue Recognition

FASB ASC 860-50, *Transfers and Servicing*, requires that MSRs be initially recorded at fair value at the time the underlying loans are sold. To determine the fair value of the MSR created, the Company uses a valuation model, along with currently available market information including rate sheets from aggregators, that calculates the net present value of future cash flows. The valuation model incorporates assumptions that market participants would use in estimating future net servicing revenue, including the estimated discount rate, estimated prepayment speeds, the cost of servicing, estimated delinquencies, contractual service fees, ancillary income and late fees, float value, the inflation rate, and default rates. The credit quality and stated interest rates of the forward loans underlying the MSRs affects the assumptions used in the cash flow models. MSRs are not actively traded in open markets; accordingly, considerable judgment is required to estimate their fair value, and changes in these estimates could materially change the estimated fair value. The Company receives a monthly fixed servicing fee based on the outstanding principal balances of the mortgage loans, which is collected from investors.

A. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Mortgage Servicing Rights and Revenue Recognition (Continued)

After initially recording the MSRs at fair value, the Company subsequently amortizes the MSRs over the estimated economic life of the related mortgage loans in proportion to the estimated future net servicing revenue. The net capitalized cost of MSRs is periodically evaluated to determine if the amortized cost of MSRs is in excess of their estimated fair value. For this purpose, the Company stratifies its MSRs based on loan term, interest rate and product type, with estimates of remaining loan lives and prepayment rates being incorporated into the model. When impairment is identified due to the MSR asset's amortized book value exceeding its fair value, management records a valuation allowance. Valuation allowances are recorded as a reduction to the MSRs on the balance sheets.

Any impairment of the amortized cost of MSRs is assessed based on their fair value at each reporting date using estimated prepayment speeds of the underlying mortgage loans serviced and stratification based on risk characteristics of the underlying loans (predominantly interest rates). As interest rates decrease, mortgage refinancing activity may increase, resulting in higher prepayment speeds of the loans underlying MSRs, which may result in a reduction of the MSRs' fair value. Such fair value adjustment may require an additional valuation allowance being charged to earnings, to the extent that the amortized cost of the MSR exceeds the estimated fair value from stratification. Conversely, as mortgage interest rates rise, prepayment speeds are usually slower and the value of the MSR asset generally increases, requiring less valuation allowance. If it is later determined that all or a portion of the temporary impairment no longer exists for a stratification, the valuation allowance is reduced through a recovery to earnings. An other-than-temporary impairment (i.e. recoverability is considered remote when considering interest rates and loan pay-off activity) is recognized as a write-down of the MSR asset and the related valuation allowance. A direct write-down permanently reduces the carrying value of the MSR asset and valuation allowance, precluding subsequent recoveries.

The key unobservable inputs used in determining the fair value of MSRs when they are initially recorded were as follows for the year ended December 31, 2020:

	Inputs
Discount rates	11.00% - 11.26%
Annual prepayment speeds	15.39% - 21.40%
Average cost of servicing	$85

The Company's MSR portfolio was de minimus at December 31, 2019, therefore, certain disclosures pertaining to 2019 were omitted from the notes to the financial statements.

A. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Sale of Mortgage Servicing Rights

A transfer of servicing rights related to loans previously sold qualifies as a sale at the date on which title passes, if substantially all risks and rewards of ownership have irrevocably passed to the transferee and any protection provisions retained by the transferor are minor and can be reasonably estimated. In addition, if a sale is recognized and only minor protection provisions exist, a liability should be accrued for the estimated obligation associated with those provisions.

Loans in Forbearance and Eligible for Repurchase from GNMA

When the Company has the unilateral right to repurchase GNMA pool loans it has previously sold (generally loans that are more than 90 days past due) and the Company has determined there is more than a trivial benefit to repurchase the loans, the Company records its right to the loan on its balance sheets as an asset and corresponding liability. The recognition of previously sold mortgage loans does not impact the accounting for the previously recognized MSRs. At December 31, 2020, delinquent or defaulted mortgage loans currently in GNMA pools that the Company has recognized on its balance sheets totaled $2,338,905. The Company had no delinquent or defaulted mortgage loans in GNMA pools at December 31, 2019. Loans with borrowers that have entered into a forbearance plan under the Coronavirus Aid, Relief, and Economic Security Act (CARES Act) have an unpaid principal balance of approximately $7,041,000 or 1.36% of the MSR portfolio at December 31, 2020, of which approximately $2,339,000 and 0.45% of the MSR portfolio is greater than 90 days delinquent. There were no actual repurchases of GNMA delinquent or defaulted mortgage loans during the year ended December 31, 2020. The Company repurchased $503,131 and $750,392 of GNMA delinquent or defaulted mortgage loans during the years ended December 31, 2019 and 2018, respectively, with the intention to modify their terms and include the loans in new GNMA pools.

Real Estate Owned

Real estate owned is initially recorded at the estimated fair value at the date of foreclosure of the underlying delinquent mortgage loan, which becomes the new cost basis in the real estate owned. The fair value of real estate owned is determined, when possible, using observable market data, including recent real estate appraisals and broker price opinions. Costs incurred in managing and maintaining foreclosed real estate and subsequent declines in fair value are charged to operations as incurred and are included in general and administrative on the statements of operations. The Company periodically assesses real estate owned for impairment whenever events or circumstances indicate the carrying amount of the assets may exceed their fair value. If real estate owned is considered impaired, the impairment losses will be recorded on the statements of operations.

A. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Loan Indemnification Reserve

Loans sold to investors by the Company and which met investor and Agency underwriting guidelines at the time of sale may be subject to repurchase in the event of specific default by the borrower or subsequent discovery that underwriting standards were not met. The Company may, upon mutual agreement, indemnify the investor against future losses on such loans. The Company has established a reserve for potential losses related to these representations and warranties. In assessing the adequacy of the reserve, management evaluates various factors including actual write-offs during the period, historical loss experience, known delinquent and other problem loans, and economic trends and conditions in the industry. Actual losses incurred are reflected as write-offs against the loan indemnification reserve.

The activity in the loan indemnification reserve for mortgage loans held for sale is as follows for the years ended December 31:

	2020	2019	2018
Balance, beginning of year	$ 593,287	$ 532,071	$ 645,761
Provision for loan losses	815,663	526,421	130,929
Reclassification of provision	100,000	—	—
Loans written-off, net of recoveries	(183,882)	(465,205)	(244,619)
Balance, end of year	$ 1,325,068	$ 593,287	$ 532,071

Because of the uncertainty in the various estimates underlying the loan indemnification reserve, there is a range of losses in excess of the recorded loan indemnification reserve that is reasonably possible. The estimate of the range of possible loss for representations and warranties does not represent a probable loss and is based on current available information, significant judgment, and a number of assumptions that are subject to change.

Valuation Allowance on Mortgage Loans Held for Investment, Net

The Company periodically evaluates the carrying value of mortgage loans held for investment in excess of fair value and establishes a valuation allowance for potential losses. In assessing the adequacy of the valuation allowance, management evaluates various factors on a loan level basis, including the probability of not being able to collect payments based on the contractual terms of the mortgage, the estimated fair value of the underlying collateral and probable losses inherent to the loan portfolio. Additions to and recovery of the valuation allowance are reflected in the provision for loan losses on the statements of operations.

A. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Valuation Allowance on Mortgage Loans Held for Investment, Net (Continued)

The activity in the valuation allowance for mortgage loans held for investment is as follows for the years ended December 31:

	2020	2019	2018
Balance, beginning of year	$ 59,184	$ 44,900	$ 48,845
Provision for loan losses	81,646	24,901	628
Loans written-off, net of recoveries	(51,395)	(10,617)	(4,573)
Balance, end of year	$ 89,435	$ 59,184	$ 44,900

Because of the uncertainty in the various estimates underlying the valuation allowance, there is a range of losses in excess of the recorded valuation allowance that is reasonably possible. The estimate of the range of possible loss does not represent a probable loss and is based on current available information, significant judgment and a number of assumptions that are subject to change.

Escrow and Fiduciary Funds

The Company maintains segregated bank accounts for escrow balances in trust for investors for mortgagors. The balances of these accounts amounted to $2,178,678 and $19,845 at December 31, 2020 and 2019, respectively, and are excluded from the balance sheets.

Advertising and Marketing

Advertising and marketing is expensed as incurred and amounted to $1,220,661, $1,221,637 and $905,831 for the years ended December 31, 2020, 2019 and 2018, respectively, and are included in general and administrative on the statements of operations.

Income Taxes

The Company has elected to be taxed as a partnership under the Internal Revenue Code. Accordingly, no federal income tax provision and state income taxes, to the extent possible, have been recorded in the financial statements, as all items of income and expense generated by the Company are reported on the members' income tax returns. The Company has no federal or state tax examinations in process as of December 31, 2020.

Risks and Uncertainties

In the normal course of business, companies in the mortgage banking industry encounter certain economic and regulatory risks. Economic risks include interest rate risk and credit risk. The Company is subject to interest rate risk to the extent that in a rising interest rate environment, the Company may experience a decrease in loan production, as well as decreases in the value of mortgage loans held for sale not committed to investors and commitments to originate loans, which may negatively impact the Company's operations. Credit risk is the risk of default that may result from the borrowers' inability or unwillingness to make contractually required payments during the period in which loans are being held for sale or serviced by the Company.

A. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Risks and Uncertainties (Continued)
The Company sells loans to investors without recourse. As such, the investors have assumed the risk of loss or default by the borrower. However, the Company is usually required by these investors to make certain standard representations and warranties relating to credit information, loan documentation and collateral. To the extent that the Company does not comply with such representations, or there are early payment defaults, the Company may be required to repurchase the loans or indemnify these investors for any losses from borrower defaults. In addition, if loans pay-off within a specified time frame, the Company may be required to refund a portion of the sales proceeds to the investors.

The Company's business requires substantial cash to support its operating activities. As a result, the Company is dependent on its warehouse lines of credit, and other financing facilities in order to finance its continued operations. If the Company's principal lenders decided to terminate or not to renew any of these financing facilities with the Company, the loss of borrowing capacity could have a material adverse impact on the Company's financial statements unless the Company found a suitable alternative source.

The recent global outbreak of COVID-19 has disrupted economic markets, and the prolonged economic impact is uncertain. The operational and financial performance of the Company depends on future developments, including the duration and spread of the outbreak, and such uncertainty may have an adverse impact on the Company's financial performance.

Recently Issued Accounting Pronouncements

Future Adoption of New Accounting Pronouncements
In February 2016, FASB issued *Accounting Standards Update (ASU)* No. 2016-02, *Leases* (ASU 2016- 02), which requires recognition of right-of-use assets and lease liabilities by lessees for all leases with a term greater than 12 months and to provide enhanced disclosures. ASU 2016-02 is effective for fiscal years beginning after December 15, 2021, with early adoption permitted.

Adoption of Recent Accounting Pronouncements
In May 2014, the FASB issued new revenue recognition guidance that supersedes most industry-specific guidance but does exclude financial instruments. The Company adopted the guidance beginning January 1, 2018 and concluded that its revenue streams are not within the scope of the standard because the standard does not apply to revenue on contracts accounted for under the transfers and servicing of financial assets or financial instrument standards. Therefore, the revenue recognition for these contracts remained unchanged.

In January 2016, the FASB issued an ASU that amends the guidance on the classification and measurement of financial instruments. Among other things, the ASU amends certain disclosure requirements associated with the fair value of financial instruments. This Company adopted the guidance beginning January 1, 2018. The adoption did not have a significant impact on the Company's financial statements.

A. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Recently Issued Accounting Pronouncements (Continued)

Adoption of Recent Accounting Pronouncements (Continued)
In June 2016, the FASB issued ASU 2016-13, *Financial Instruments – Credit Losses* (Topic 326): *Measurement of Credit Losses on Financial Instruments*, as amended, which amends the guidance for recognizing credit losses on financial instruments measured at amortized cost including receivables. The ASU requires measurement and recognition of expected versus incurred credit losses using a lifetime credit loss measurement approach. Significantly all of the Company's financial assets are measured at fair value and are therefore not subject to the guidance; however, the Company determined that receivables and GNMA early buyout loans are within the scope of the ASU. GNMA early buyout loans are insured by the FHA or guaranteed by the Department of Veterans Affairs (VA) which limits the Company's exposure to potential credit- related losses to an immaterial amount. Further, the estimated credit-related losses of the Company's receivables are also immaterial due to the short-term nature of the assets. Servicing advances are generally expected to be fully reimbursed under the terms of the servicing agreements. The Company adopted the guidance beginning January 1, 2020. The adoption did not have a significant impact on the Company's financial statements.

In August 2018, the FASB issued an ASU that further removes, modifies or adds certain disclosure requirements for fair value measurements. The Company adopted the guidance beginning January 1, 2020. The adoption did not have a significant impact on the Company's financial statements.

B. MORTGAGE LOANS HELD FOR SALE, AT FAIR VALUE

Mortgage loans held for sale are as follows at December 31:

	2020	2019
Mortgage loans held for sale	$136,912,023	$ 96,137,616
Mortgage loans held for sale (greater than 90 days outstanding)	—	669,026
Fair value adjustment	6,522,661	3,417,311
	$143,434,684	$100,223,953

C. MORTGAGE LOANS HELD FOR INVESTMENT, NET

The following summarizes mortgage loans held for investment, net at December 31:

	2020	2019
Mortgage loans held for investment	$2,170,435	$3,367,385
Valuation allowance	(89,435)	(59,184)
	$2,081,000	$3,308,201

D. ACCOUNTS RECEIVABLE AND ADVANCES

The following summarizes accounts receivable and advances at December 31:

	2020	2019
Loan sales receivable	$ 149,347	$364,407
Due from borrower	43,885	118,483
Servicing advances	99,570	54,888
MSR co-issue receivable	728,040	196,127
	$1,020,842	$733,905

The Company periodically evaluates the carrying value of accounts receivable and advance balances with delinquent balances written-off based on specific credit evaluations and circumstances of the debtor. No allowance for doubtful accounts has been established at December 31, 2020 and 2019, as management has determined that all amounts are fully collectible.

The Company issued two notes receivable to an employee totaling $218,000 during the year ended December 31, 2019. The notes receivable bear interest at 5.00% per annum with principal and unpaid interest payable on the fifth anniversary of each note receivable. The Company will forgive 20% of the principal and interest every 12 months after the effective date of each note receivable, provided the employee meets certain conditions related to continued employment and minimum annual loan origination. The notes receivable totaled $174,400 and $218,000 at December 31, 2020 and 2019, respectively, which are included in due from related parties on the balance sheets.

E. DERIVATIVE INSTRUMENTS

The Company enters into IRLCs to originate residential mortgage loans held for sale, at specified interest rates and within a specified period of time (generally between 30 and 90 days), with borrowers who have applied for a loan and have met certain credit and underwriting criteria. The IRLCs are adjusted for estimated costs to originate the loan as well as the probability that the mortgage loan will fund within the terms of the IRLC (the pullthrough rate). Estimated costs to originate include loan officer commissions and overrides. The pullthrough rate is estimated on changes in market conditions, loan stage, and actual borrower behavior using a historical analysis of IRLC closing rates. The Company obtains an analysis from an independent third party on a monthly basis to support the reasonableness of the pullthrough estimate.

E. DERIVATIVE INSTRUMENTS (Continued)

The key unobservable inputs used in determining the fair value of IRLCs are as follows for the years ended December 31:

	2020	2019	2018
Pullthrough rates	81.92% - 88.35%	86.60% - 88.98%	87.50% - 89.67%
Average cost to originate	1.20%	1.20%	1.15%

The following summarizes derivative instruments at December 31:

	2020		2019	
	Fair Value	Notional Amount	Fair Value	Notional Amount
IRLCs:				
Mandatory	$ 9,945,416	$254,186,000 (b)	$ 1,702,564	$ 60,814,000 (b)
Best efforts	253,829	$ 27,329,000 (b)	230,112	$ 25,413,000 (b)
MBSs	(2,496,602)	$326,000,000	(74,922)	$ 71,000,000
Total	$ 7,702,643		$ 1,857,754	

(b) Pullthrough rate adjusted

The notional amounts of mortgage loans held for sale not committed to investors amounted to approximately $105,819,000 and $17,514,000 at December 31, 2020 and 2019, respectively.

The Company has exposure to credit loss in the event of contractual non-performance by its trading counterparties in derivative instruments that the Company uses in its rate risk management activities. The Company manages this credit risk by selecting only counterparties that the Company believes to be financially strong, spreading the risk among multiple counterparties, by placing contractual limits on the amount of unsecured credit extended to any single counterparty and by entering into netting agreements with counterparties, as appropriate.

F. MORTGAGE SERVICING RIGHTS

The following summarizes the activity of MSRs for the years ended December 31:

	2020	2019	2018
Balance, beginning of year	$ 6,750	$ 303,194	$ 501,971
Additions due to loans sold servicing retained	1,856,167	15,094	32,218
Deletions due to sale of MSRs	—	(259,948)	—
Deletions due to loan payoffs	(17,151)	(19,787)	(33,061)
Amortization expense	(150,796)	(31,803)	(197,934)
Balance, end of year	$ 1,694,970	$ 6,750	$ 303,194

At December 31, 2020 and 2019, the unpaid principal balance of mortgage loans serviced approximated $517,842,000 and $4,476,000, respectively. Conforming conventional loans serviced by the Company are sold to FNMA and FHLMC on a non-recourse basis, whereby foreclosure losses are generally the responsibility of FNMA and FHLMC, and not the Company. The government loans serviced by the Company are secured through GNMA, whereby the Company is insured against loss by the Federal Housing Administration or partially guaranteed against loss by the VA.

The key unobservable inputs used in determining the fair value of the Company's MSRs are as follows at December 31, 2020:

	Inputs
Discount rates	11.00% - 11.24%
Annual prepayment speeds	15.52% - 21.40%
Average cost of servicing	$85

The hypothetical effect of an adverse change in these key unobservable inputs would result in a decrease in fair value as follows at December 31, 2020:

	Amounts
Discount rates:	
Effect on value - 1% adverse change	$ (139,594)
Effect on value - 2% adverse change	$ (270,488)
Prepayment speeds:	
Effect on value - 5% adverse change	$ (153,468)
Effect on value - 10% adverse change	$ (299,990)
Cost of servicing:	
Effect on value - 5% adverse change	$ (28,738)
Effect on value - 10% adverse change	$ (57,477)

F. MORTGAGE SERVICING RIGHTS (Continued)

These sensitivities are hypothetical and should be used with caution. As the table demonstrates, the Company's methodology for estimating the fair value of MSRs is highly sensitive to changes in key unobservable inputs. For example, actual prepayment experience may differ and any difference may have a material effect on MSR fair value. Changes in fair value resulting from changes in inputs generally cannot be extrapolated because the relationship of the change in input to the change in fair value may not be linear. Also, in this table, the effect of a variation in a particular input on the fair value of the MSRs is calculated without changing any other input; in reality, changes in one factor may be associated with changes in another (for example, decreases in market interest rates may indicate higher prepayments; however, this may be partially offset by lower prepayments due to other factors such as a borrower's diminished opportunity to refinance), which may magnify or counteract the sensitivities. Thus, any measurement of MSR fair value is limited by the conditions existing and inputs made as of a particular point in time. Those inputs may not be appropriate if they are applied to a different point in time.

Sale of Mortgage Servicing Rights

During the year ended December 31, 2019, the Company sold the majority of its MSR portfolio with an unpaid principal balance of approximately $75,280,000 for a net sales price of $597,813, which includes the gross sales prices of $629,063 less $31,250 for transactional expenses. The Company recognized a gain on sale of $337,865 which is recorded in gain on sale of mortgage servicing rights on the statements of operations. In addition, the Company recorded a receivable totaling $62,906, at December 31, 2019, related to the sale, which is due when all of the complete mortgage files have been received by the purchaser. The Company performed temporary sub-servicing activities with respect to the underlying loans through the established transfer date, for which the Company earned a fee and is also entitled to certain other ancillary income amounts.

G. WAREHOUSE LINES OF CREDIT AGREEMENTS

The Company has the following warehouse lines of credit (WHLOC) agreements with various financial institutions at December 31:

Facility Type	Maturity	Line Amount	Interest Rate	Restricted Cash	Outstanding Balance 2020	Outstanding Balance 2019
WHLOC	N/A	$ 10,000,000	LIBOR plus 2.75%, with a floor rate of 3.25%	$ 100,000	$ —	$ —
WHLOC*	January 2022	$ 40,000,000	LIBOR plus 2.25%, with a floor rate of 3.25%	—	30,757,899	23,007,825
WHLOC	N/A	$ 90,000,000	LIBOR plus 2.90%, with a floor rate of 3.25%	586,643	58,664,259	25,123,038
WHLOC	August 2021	$ 50,000,000	LIBOR plus 2.75% - 3.25%, with a LIBOR floor rate of 1.00%	—	25,009,964	14,776,973
WHLOC	June 2021	$ 75,000,000	LIBOR plus 2.65%, with a LIBOR floor rate of 0.50%	—	21,655,055	29,144,179
				$ 686,643	$ 136,087,177	$ 92,052,015

* The WHLOC is with a related party.

As of December 31, 2020 and 2019, the Company had mortgage loans held for sale pledged as collateral under the above WHLOC agreements, with the lines being personally guaranteed by the members. The above agreements also contain covenants which include certain financial requirements, including maintenance of minimum tangible net worth, minimum liquid assets, maximum debt to net worth ratio, positive net income, and minimum fidelity bond and errors and omissions coverage, as defined in the agreements. The Company was in compliance with all significant debt covenants at December 31, 2020. The Company intends to renew the WHLOCs when they mature.

H. OPERATING LINE OF CREDIT AGREEMENT, RELATED PARTY

The Company had a $7 million revolving line of credit agreement with a related party, which matured and was fully repaid in May 2020. The line of credit was payable on demand, bore interest at the Prime rate plus 0.50%, with a floor rate of 3.75%, and was personally guaranteed by a member of the Company. The outstanding balance under the operating line of credit totaled $3,734,308 at December 31, 2019.

I. NOTE PAYABLE

In April 2020, the Company was approved by the U.S. Small Business Administration (SBA) under the CARES Act for a Paycheck Protection Program (PPP) loan and received proceeds totaling

$3,698,388. Interest is at 1.00% per annum and matures in April 2022. The note has a deferral period of 15 months beginning on the date of the note, during which interest accrues but no payments are due. The outstanding balance under the note payable totaled $3,698,388 at December 31, 2020. The Company intends to use the entire PPP loan amount for qualifying expenses and to apply for forgiveness of the loan in accordance with the terms of the CARES Act.

Future minimum payments under the note payable are as follows at December 31, 2020:

Year Ending December 31,	Amounts
2021	$ 2,051,145
2022	1,647,243
	$ 3,698,388

J. RELATED PARTY TRANSACTIONS

A related party financial institution is a member of the Company with common membership shares and preferred membership shares.

During the years ended December 2020, 2019 and 2018, the Company sold 225, 287 and 304 loans, respectively, servicing released with unpaid principal balances of $58,916,783, $158,200,197 and

$131,718,723, respectively, to the related party financial institution. Premiums received on the loans amounted to $1,096,796, $2,633,141 and $2,306,708, during the years ended December 31, 2020, 2019 and 2018, respectively, and are included in gain on sale of mortgage loans held for sale on the statements of operations. The Company also paid origination expenses to the related party financial institution totaling $3,100, $9,603 and $7,402 during the years ended December 31, 2020, 2019 and 2018, respectively, which is included in gain on sale of mortgage loans held for sale, direct costs on the statements of operations.

The Company has a warehouse line of credit agreement and an operating line of credit agreement with the same related party financial institution (Notes G and H, respectively). Pursuant to which, the Company paid $996,728, $1,332,480 and $1,069,282 in interest expense and other fees during the years ended December 31, 2020, 2019 and 2018, respectively, which are included in interest expense on the statements of operations.

The Company paid $16,371, $27,154 and $36,224 in marketing expenses to the related party financial institution during the years ended December 31, 2020, 2019 and 2018, respectively, which is included in general and administrative on the statements of operations.

J. RELATED PARTY TRANSACTIONS (Continued)

The Company has receivables due from various employees totaling $174,400 and $393,339 at December 31, 2020 and 2019, respectively, which are included in due from related parties on the balance sheets.

K. COMMON INTERESTS

At December 31, 2020 and 2019, the Company has 8,783,212 common shares issued and outstanding with certain members. Common shares with voting rights are held by a member that is an officer of the Company and a financial institution member. On the fifteenth day of January, April, June and September, the members with common shares receive distributions in aggregate amounts equal to no less than 40% of the Company's available cash, as reasonably determined by the Board of Directors, for the fiscal year through the end of the immediately preceding full calendar month less any amounts previously distributed during such fiscal year, in proportion to their respective common shares. The Board of Directors is authorized to make additional distributions from time to time to the members in proportion to their respective common shares. Profits and losses of the Company shall be allocated first to the preferred members and second to the common members.

L. PREFERRED INTERESTS

At December 31, 2020 and 2019, the Company has 3,304,656 preferred shares issued and outstanding. Members with preferred shares are entitled to receive, if and when declared, cash payments at the rate of $0.075 per share per annum, made in equal quarterly installments on the fifteenth day of January, April, July and October. Such preferred dividend payments are cumulative and totaled $247,039, $249,312 and $248,892 during the years ended December 31, 2020, 2019 and 2018, respectively, with $61,692 and $62,275 recorded in accounts payable and accrued expenses on the balance sheets at December 31, 2020 and 2019, respectively. Holders of preferred membership shares are not entitled to voting rights.

M. PROFIT INTEREST UNITS

During the year ended December 31, 2020, members transferred 518,210 units to an officer of the Company as common profits interest membership shares (profit interest units). The transfer was based on loan production volume from the preceding year. The profit interest units entitle the officer to participate in future profits, losses, distributions and appreciation of the Company. The profit interest units do not require initial investment and do not have voting rights. During the year ended December 31, 2020, profit interest unit distributions totaled $308,615.

N. EMPLOYEE BENEFIT PLAN

The Company has a 401(k) qualified retirement plan covering substantially all employees. Employees may contribute amounts subject to certain Internal Revenue Service and plan limitations. The Company may make discretionary matching and non-elective contributions. The Company made no contributions to the plan for the years ended December 31, 2020, 2019 and 2018.

O. COMMITMENTS AND CONTINGENCIES

Commitments to Extend Credit

The Company enters into IRLCs with customers who have applied for residential mortgage loans and meet certain credit and underwriting criteria. These commitments expose the Company to market risk if interest rates change and the underlying loan is not economically hedged or committed to an investor. The Company is also exposed to credit loss if the loan is originated and not sold to an investor and the mortgagor does not perform. The collateral upon extension of credit typically consists of a first deed of trust in the mortgagor's residential property. Commitments to originate loans do not necessarily reflect future cash requirements as some commitments are expected to expire without being drawn upon. Total commitments to originate loans approximated $321,058,000 and $97,692,000 at December 31, 2020 and 2019, respectively.

Regulatory Contingencies

The Company is subject to periodic audits and examinations, both formal and informal in nature, from various federal and state agencies, including those made as part of regulatory oversight of mortgage origination, servicing and financing activities. Such audits and examinations could result in additional actions, penalties or fines by state or federal governmental bodies, regulators or the courts.

Operating Leases

The Company leases office space and equipment under various operating lease arrangements, which expire through May 2025. Total rent expense under all operating leases amounted to $2,477,219, $2,419,495 and $2,087,331 for the years ended December 31, 2020, 2019 and 2018, respectively, and are included in occupancy, equipment and communication on the statements of operations.

Future minimum rental payments under long-term operating leases are as follows at December 31, 2020:

Year Ending December 31,	Amounts
2021	$ 1,634,130
2022	941,993
2023	583,258
2024	408,689
2025	90,844
	$ 3,658,914

O. COMMITMENTS AND CONTINGENCIES (Continued)

Legal

The Company operates in a highly regulated industry and may be involved in various legal and regulatory proceedings, lawsuits and other claims arising in the ordinary course of its business. The amount, if any, of ultimate liability with respect to such matters cannot be determined, but despite the inherent uncertainties of litigation, management currently believes that the ultimate disposition of any such proceedings and exposure will not have, individually or taken together, a material adverse effect on the financial condition, results of operations, or cash flows of the Company. However, actual outcomes may differ from those expected and could have a material effect on the Company's financial position, results of its operations or cash flows in a future period. The Company accrues for losses when they are probable to occur, and such losses are reasonably estimable. Legal costs are expensed as incurred and are included in general and administrative on the statements of operations.

Regulatory Net Worth Requirements

In accordance with the regulatory requirements of HUD, governing non-supervised, direct endorsement mortgagees, the Company is required to maintain a minimum net worth (as defined by HUD) of $2,500,000. At December 31, 2020, the Company exceeded the regulatory net worth requirement.

In accordance with the regulatory requirements of GNMA, governing issuers of GNMA securities, the Company is required to maintain a minimum net worth (as defined by GNMA) of $4,808,820. At December 31, 2020, the Company exceeded the regulatory net worth requirement.

Self-Insurance Plan

The Company has engaged an insurance company to provided administrative services for the Company's self-funded insurance plan. The Company pays the qualifying medical claims expense for all participating individuals. The Company has a stop loss policy with the insurance company whereby they are reimbursed for all qualifying medical expenses incurred by individual employees above $1,665,736 in the aggregate. In addition, the Company is reimbursed for all aggregate medical expenses incurred by all participating individuals above $100,000 per the stop loss agreement. The Company has accrued for expenses related to incurred but not reported claims totaling $187,000 and $197,000 for the years ended December 31, 2020 and 2019.

P. FAIR VALUE MEASUREMENTS

FASB ASC 820, *Fair Value Measurements and Disclosures* (ASC 820), defines fair value as the price that would be received upon sale of an asset or paid upon transfer of a liability in an orderly transaction between market participants at the measurement date and in the principal or most advantageous market for that asset or liability. The fair value should be calculated based on assumptions that market participants would use in pricing the asset or liability, not assumptions specific to the entity.

P. FAIR VALUE MEASUREMENTS (Continued)

ASC 820 specifies a hierarchy of valuation techniques based upon whether the inputs to those valuation techniques reflect assumptions other market participants would use based upon the market data obtained from independent sources (observable inputs). In accordance with ASC 820, the following summarizes the fair value hierarchy:

Level 1 Inputs – Unadjusted quoted market prices for identical assets and liabilities in an active market that the Company has the ability to access.

Level 2 Inputs – Inputs other than the quoted market prices in active markets that are observable either directly or indirectly.

Level 3 Inputs – Inputs based on prices or valuation techniques that are both unobservable and significant to the overall fair value measurements.

ASC 820 requires the use of observable market data, when available, in making fair value measurements. When inputs used to measure fair value fall within different levels of the hierarchy, the level within which the fair value measurement is categorized is based on the lowest level input that is significant to the fair value measurements. Valuation techniques used need to maximize the use of observable inputs and minimize the use of unobservable inputs.

While the Company believes its valuation methods are appropriate and consistent with those used by other market participants, the use of different methods or assumptions to estimate the fair value of certain financial statement items could result in a different estimate of fair value at the reporting date. The significant unobservable inputs used in the fair value measurement may result in significantly different fair value measurements if any of those inputs were to change in isolation. Generally, a change in the assumptions used in the fair value measurement would be accompanied by a directionally opposite change in other assumptions. Those estimated values may differ significantly from the values that would have been used had a readily available market for such items existed, or had such items been liquidated, and those differences could be material to the financial statements.

The following is a description of the valuation methodologies used for assets and liabilities measured at fair value. There have been no changes in the methodologies used at December 31, 2020 and 2019.

Mortgage loans held for sale (MLHFS) – The fair value of mortgage loans held for sale based on Level 2 inputs is determined, when possible, using either quoted secondary-market prices or investor commitments. If no such quoted price exists, the fair value of a loan is determined using quoted prices for a similar asset or assets, adjusted for the specific attributes of that loan, which would be used by other market participants.

Mortgage loans held for investment – The fair value of mortgage loans held for investment is determined based on observable market information, including pricing from actual market transactions or broker quotations.

P. FAIR VALUE MEASUREMENTS (Continued)

Derivative instruments – The fair value of IRLCs is based on valuation models incorporating market pricing for instruments with similar characteristics, commonly referred to as best execution pricing, or investor commitment prices for best effort IRLCs. The valuation models used to value the IRLCs have unobservable inputs, such as an estimate of the fair value of the servicing rights expected to be recorded upon sale of the loans, estimated costs to originate the loans, and pullthrough, and are therefore classified as Level 3 within the fair value hierarchy.

The fair value of forward sale commitments is based on observable market pricing for similar instruments and are therefore classified as Level 2 within the fair value hierarchy.

Mortgage servicing rights – The fair value of MSRs is difficult to determine because MSRs are not actively traded in observable stand-alone markets. The Company uses a discounted cash flow approach to estimate the fair value of MSRs. This approach consists of projecting net servicing cash flows discounted at a rate that management believes market participants would use in their determinations of fair value. The key unobservable inputs used in the estimation of the fair value of MSRs include prepayment speeds, discount rates, default rates, cost to service, contractual servicing fees, escrow earnings and ancillary income.

Real estate owned – Real estate owned is initially recorded at the estimated fair value at the date of foreclosure on the delinquent mortgage loans, which becomes the new cost basis in the real estate owned. The fair value of real estate owned is determined, when possible, using observable market data, including recent real estate appraisals and broker price opinions. Subsequent declines in fair value are credited to a valuation allowance.

Assets and Liabilities Measured at Fair Value

The following are the major categories of assets and liabilities measured at fair value on a recurring basis as of December 31, 2020:

Description	Level 1	Level 2	Level 3	Total
MLHFS	$ —	$ 143,434,684	$ —	$ 143,434,684
Derivative instruments	—	(2,496,602)	10,199,245	7,702,643
Total	$ —	$ 140,938,082	$ 10,199,245	$ 151,137,327

The following are the major categories of assets and liabilities measured at fair value on a recurring basis as of December 31, 2019:

Description	Level 1	Level 2	Level 3	Total
MLHFS	$ —	$ 100,223,953	$ —	$ 100,223,953
Derivative instruments	—	(74,922)	1,932,676	1,857,754
Total	$ —	$ 100,149,031	$ 1,932,676	$ 102,081,707

The Company does not have any impaired assets or liabilities that are recorded at fair value on a non-recurring basis as of December 31, 2020 and 2019.

P. FAIR VALUE MEASUREMENTS (Continued)

Assets and Liabilities Measured at Fair Value (Continued)

The following are the changes in fair value of Level 1 and Level 2 assets and liabilities measured at fair value on a recurring basis for the years ended December 31:

Financial Instrument	2020	2019	2018
Mortgage loans held for sale	$ 3,105,350	$ 1,087,360	$ 262,785
Derivative liabilities	(2,421,680)	478,516	(477,657)
Total	$ 683,670	$ 1,565,876	$ (214,872)

Level 3 Purchases, Issuances and Transfers

The following is a summary of the Company's purchases, issuances, and transfers of assets, as applicable, which are measured at fair value on a recurring and non-recurring basis using Level 3 inputs during the year ended December 31, 2020:

	MSRs	IRLCs
Issuances (c)	$1,856,167	$ 68,946,475
Transfers out of Level 3 (d)	$ —	$112,297,249

(c) Issuances of Level 3 MSRs represent current year additions from mortgage loans sold servicing retained. Issuances of Level 3 IRLCs represent the lock-date fair value of IRLCs issued to borrowers during the year, net of the estimated pullthrough rate and costs to originate.

(d) IRLCs transferred out of Level 3 represent IRLCs that were funded and transferred to mortgage loans held for sale, at fair value.

Fair Value of Other Financial Instruments

Due to their short-term nature, the carrying value of cash and cash equivalents, restricted cash, escrow cash, short-term receivables, short-term payables, note payable, and warehouse and operating lines of credit approximate their fair value at December 31, 2020.

Q. SUBSEQUENT EVENTS

Management has evaluated subsequent events through March 12, 2021, the date on which the financial statements were available to be issued.