

provident
bancorp inc.



ANNUAL
report.
2021



financials at a glance.

Return on Assets



Return on Equity



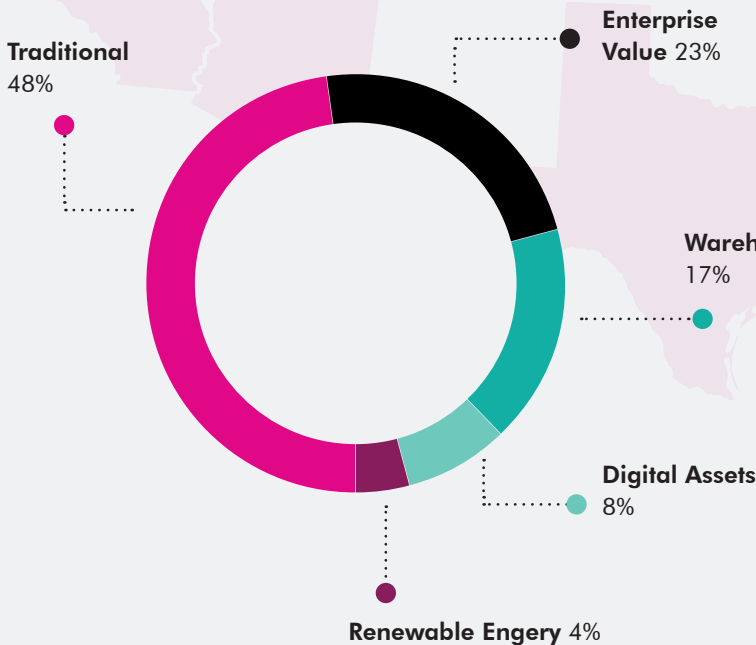
Efficiency Ratio



Non-interest Bearing Deposits to Total Deposits



Loan Composition



We firmly believe in our mission and belief that all businesses should be afforded the same access and rights to traditional financing tools.

provident
bancorp inc.

2021 Form 10-K

**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, 2021

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: 001-39090

PROVIDENT BANCORP, INC.

(Exact name of registrant as specified in its charter)

Maryland

(State or other jurisdiction of
incorporation or organization)

84-4132422

(I.R.S. Employer
Identification Number)

5 Market Street, Amesbury, Massachusetts

(Address of Principal Executive Offices)

01913

Zip Code

(978) 834-8555

(Registrant's telephone number, including area code)

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

<u>Title of each class</u>	<u>Trading Symbol</u>	<u>Name of each exchange on which registered</u>
Common Stock, \$0.01 par value	PVBC	The NASDAQ Stock Market LLC

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, smaller reporting company, or an emerging growth company. See the 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

Non-accelerated Filer

Accelerated Filer

Smaller Reporting Company

Emerging Growth Company

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 its 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 issued its audit report.

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

The aggregate market value of the voting and non-voting common stock held by non-affiliates of the registrant, computed by reference to the last sale price as of June 30, 2021, as reported by the Nasdaq Capital Market, was approximately \$256.4 million.

The number of shares outstanding of the registrant's common stock as of March 16, 2022 was 17,834,693.

DOCUMENTS INCORPORATED BY REFERENCE:

Portions of the Registrant's proxy statement for the 2021 Annual Meeting of Stockholders (Part III).

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PART I

ITEM 1. BUSINESS

FORWARD-LOOKING STATEMENTS

This Annual Report contains forward-looking statements, which can be identified by the use of words such as “estimate,” “project,” “believe,” “intend,” “anticipate,” “plan,” “seek,” “expect” and words of similar meaning. These forward-looking statements include, but are not limited to:

- statements of our goals, intentions and expectations;
- statements regarding our business plans, prospects, growth and operating strategies;
- statements regarding the quality of our loan and investment portfolios; and
- estimates of our risks and future costs and benefits.

These forward-looking statements are based on current beliefs and expectations of our management and are inherently subject to significant business, economic and competitive uncertainties and contingencies, many of which are beyond our control. In addition, these forward-looking statements are subject to assumptions with respect to future business strategies and decisions that are subject to change.

The following factors, among others, could cause actual results to differ materially from the anticipated results or other expectations expressed in the forward-looking statements:

- general economic conditions, either nationally or in our market areas, that are worse than expected, including as a result of the ongoing COVID-19 pandemic;
- changes in the level and direction of loan delinquencies and charge-offs and changes in estimates of the adequacy of the allowance for loan losses;
- our ability to access cost-effective funding;
- fluctuations in real estate values and both residential and commercial real estate market conditions;
- demand for loans and deposits in our market area;
- changes in monetary or fiscal policies of the U.S. Government, including policies of the U.S. Treasury and the Federal Reserve Board;
- cyber attacks, computer viruses and other technological risks that may breach the security of our websites or other systems, or those of third parties upon which we rely, to obtain unauthorized access to confidential information and destroy data or disable our systems;
- technological changes that may be more difficult or expensive than expected;
- the ability of third-party providers to perform their obligations to us;
- the ability of the U.S. Government to manage federal debt limits;
- our ability to continue to implement or change our business strategies;
- competition among depository and other financial institutions;
- inflation and changes in the interest rate environment that reduce our margins and yields, reduce the fair value of financial instruments or reduce the origination levels in our lending business, or increase the level of defaults, losses and prepayments on loans we have made and make whether held in portfolio or sold in the secondary markets;
- adverse changes in the securities markets;
- changes in and impacts of laws or government regulations or policies affecting financial institutions, including changes in regulatory fees, tax policy and rates, and capital requirements;
- our ability to manage market risk, credit risk and operational risk;
- our ability to enter new markets successfully and capitalize on growth opportunities;
- our ability to successfully integrate any assets, liabilities, customers, systems and management personnel we may acquire into our operations and our ability to realize related revenue synergies and cost savings within expected time frames and any goodwill charges related thereto;
- changes in consumer spending, borrowing and savings habits;
- changes in accounting policies and practices, as may be adopted by the bank regulatory agencies, the Financial Accounting Standards Board, the Securities and Exchange Commission or the Public Company Accounting Oversight Board;

- our ability to retain key employees;
- effects of natural disasters, terrorism and global pandemics;
- the effects of any U.S. government shutdown;
- the effects of climate change and societal, investor and governmental responses to climate change;
- the effects of social and governance change and societal and investor sentiment and governmental responses to social and governance matters;
- the effects of domestic and international hostilities, including terrorism;
- our compensation expense associated with equity allocated or awarded to our employees; and
- changes in the financial condition, results of operations or future prospects of issuers of securities that we own.

Further, given its ongoing and dynamic nature, it is difficult to predict the full impact of the COVID-19 pandemic on our business. The extent of such impact will depend on future developments, which are highly uncertain, including when the coronavirus can be fully controlled and abated. As the result of the COVID-19 pandemic and the related adverse local and national economic consequences, we could be subject to any of the following risks, any of which could have a material, adverse effect on our business, financial condition, liquidity, and results of operations: demand for our products and services may decline, making it difficult to grow assets and income; loan delinquencies, problem assets, and foreclosures may increase, resulting in increased charges and reduced income; collateral for loans, especially real estate, may decline in value, which could cause loan losses to increase; our allowance for loan losses may have to be increased if borrowers experience financial difficulties, which will adversely affect our net income; the net worth and liquidity of loan guarantors may decline, impairing their ability to honor commitments to us; a material decrease in net income or a net loss over several quarters could result in a decrease in the rate of our quarterly cash dividend; our cyber security risks are increased as the result of an increase in the number of employees working remotely; and Federal Deposit Insurance Corporation (“FDIC”) premiums may increase if the agency experiences additional resolution costs.

Because of these and other uncertainties, our actual future results may be materially different from the results indicated by these forward-looking statements.

Provident Bancorp, Inc.

Provident Bancorp, Inc. (the “Company”) is a Maryland corporation that was incorporated in June 2019 to be the successor corporation to Provident Bancorp, Inc. (“Old Provident”), a Massachusetts corporation, upon completion of the second-step mutual-to-stock conversion (the “Conversion”) of Provident Bancorp (the “MHC”), the top tier mutual holding company of Old Provident. Old Provident was the former mid-tier holding company for The Provident Bank (“BankProv” or the “Bank”). Prior to completion of the Conversion, approximately 52% of the shares of common stock of Old Provident were owned by the MHC. In conjunction with the Conversion, the MHC was merged into the Company (and ceased to exist) and the Company became its successor under the name Provident Bancorp, Inc. At December 31, 2021, Provident Bancorp, Inc. had total assets of \$1.73 billion, deposits of \$1.46 billion and shareholders’ equity of \$233.8 million on a consolidated basis.

The Company’s executive offices are located at 5 Market Street, Amesbury, Massachusetts 01913, and the telephone number is (978) 834-8555. The Company is subject to regulation and examination by the Board of Governors of the Federal Reserve System and the Massachusetts Commissioner of Banks.

On October 16, 2019, the Company completed the Conversion. The Company raised gross proceeds of \$102.1 million by selling a total of 10,212,397 shares of common stock at \$10.00 per share in the second-step stock offering. The Company utilized \$8.2 million of the proceeds to fund an addition to its Employee Stock Ownership Plan (“ESOP”) loan for the acquisition of an additional 816,992 shares at \$10.00 per share. Expenses incurred related to the offering were \$2.4 million, and have been recorded against offering proceeds. The Company invested \$45.8 million of the net proceeds it received from the sale into the Bank’s operations and has retained the remaining amount for general corporate purposes. Concurrent with the completion of the stock offering, each share of Old Provident common stock owned by public stockholders (stockholders other than the MHC) was exchanged for 2.0212 shares of Company common stock. A total of 19,484,343 shares of common stock were outstanding following the completion of the stock offering.

BankProv

BankProv, legally operating as The Provident Bank, is a future-ready commercial bank for corporate clients specializing in offering adaptive and technology-first banking solutions to niche markets including renewable energy, digital assets, fin-tech and search fund lending.

BankProv is a Massachusetts-chartered stock savings bank that operates from its main office and two branch offices in the Northeastern Massachusetts area, three branch offices in Southeastern New Hampshire and one branch located in Bedford, New Hampshire. We also have loan production offices in Boston, Massachusetts and Ponte Vedra, Florida. Our primary lending area encompasses Northeastern Massachusetts and Southern New Hampshire, with a focus on Essex County, Massachusetts, and Hillsborough and Rockingham

Counties, New Hampshire. However, we offer our enterprise value and mortgage warehouse loans nationwide. Our primary deposit-gathering area is currently concentrated in Essex County, Massachusetts, Rockingham County, New Hampshire, and Hillsborough County, New Hampshire, although we also receive deposits from our business customers who are located nationwide. We attract deposits from the general public and use those funds to originate primarily commercial real estate and commercial business loans, and to invest in securities. In recent years, we have been successful in growing both deposits and loans. From December 31, 2017 to December 31, 2021, deposits have increased \$709.8 million, or 94.6%, and net loans have increased \$691.7 million, or 93.2%.

BankProv is subject to regulation and examination by the Massachusetts Commissioner of Banks and the Federal Deposit Insurance Corporation.

Our website address is www.bankprov.com. Information on this website is not and should not be considered a part of this annual report.

Available Information

The Company is a public company and files interim, quarterly and annual reports with the Securities and Exchange Commission. These reports are on file and a matter of public record with the Securities and Exchange Commission. The Securities and Exchange Commission maintains an Internet site that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC (<http://www.sec.gov>). The Company's reports can also be obtained for free on our website, www.bankprov.com.

Market Area

Our primary lending area encompasses a broad market that includes Northeastern Massachusetts and Southern New Hampshire, with a focus on Essex County, Massachusetts, and Hillsborough and Rockingham Counties, New Hampshire, which are part of, and bedroom communities to, the technology corridor between Boston, Massachusetts and Concord, New Hampshire. Our enterprise value loan product is offered nationally, and as of December 31, 2021 we had relationships spanning 26 states. In 2020, the Bank purchased a warehouse lending business which is located in Ponte Vedra, Florida and targets national credit worthy, small to mid-cap non-bank mortgage origination companies for facility lines. Our primary deposit-gathering area is currently concentrated in Essex County, Massachusetts, and Rockingham County and Hillsborough County, New Hampshire, although we also receive deposits from our business customers who are located nationwide.

According to data from the FDIC as of June 30, 2021 (the latest date for which information is available), Essex County represents 5.6% of total deposits in the state of Massachusetts or approximately \$32.40 billion. The Bank holds a 2.31% market share of Essex County. Rockingham and Hillsborough County represent 22.7% and 34.6% of total deposits in the state of New Hampshire or approximately \$11.08 billion and \$16.89 billion, respectively. The Bank holds market share of 3.30% and 1.38% of Rockingham and Hillsborough Counties, respectively.

Competition

We face significant competition for deposits and loans. Our most direct competition for deposits has historically come from the many financial institutions operating in our market area. Several large holding companies operate banks in our market area. Many of these institutions, such as TD Bank, Bank of America and Citizens Bank, are significantly larger than us and, therefore, have greater resources. Additionally, some of our competitors offer products and services that we do not offer, such as insurance services, trust services, and wealth management. We also face competition for investors' funds from other financial service companies such as brokerage firms, fintech companies, money market funds, mutual funds and other corporate and government securities. Based on data from the FDIC as of June 30, 2021, BankProv had 2.31% of the deposit market share within Essex County, Massachusetts, giving us the 12th largest market share out of 35 financial institutions with offices in that county as of that date and had 3.30% of the deposit market share within Rockingham County, New Hampshire, giving us the 9th largest market share out of 26 financial institutions with offices in that county as of that date. This data excludes deposits held by credit unions.

Our competition for loans comes primarily from financial institutions in our market area. Our experience in recent years is that many financial institutions in our market area, especially community banks that are seeking to significantly expand their commercial loan portfolios and banks located in lower growth regions in New Hampshire and Maine, have been willing to price commercial loans aggressively in order to gain market share.

Lending Activities

Commercial Business Loans. We make commercial business loans primarily in our market area to a variety of small- and medium-sized businesses, including professional and nonprofit organizations, and, to a lesser extent, sole proprietorships. We also originate our enterprise value and digital asset loans nationwide, and we originate our renewable energy loans primarily in New England and New York. At December 31, 2021, commercial business loans were \$726.2 million, or 49.8% of our total loan portfolio, and we intend to

increase the amount of commercial business loans that we originate. As part of our relationship driven focus, we encourage our commercial business borrowers to maintain their primary deposit accounts with us, which enhances our interest rate spread and overall profitability.

Commercial lending products include term loans and revolving lines of credit. Commercial loans and lines of credit are made with either variable or fixed rates of interest. Variable rates and rates on Small Business Administration (“SBA”) loans (with the exception of SBA Payment Protection Program (“PPP”) loans, discussed below) are based on the prime rate as published in The Wall Street Journal, plus a margin. Initial rates on non-SBA fixed-rate business loans are generally based on a corresponding Federal Home Loan Bank rate, plus a margin. Commercial business loans typically have shorter maturity terms and higher interest rates than commercial real estate loans, but may involve more credit risk because of the type and nature of the collateral. We are focusing our efforts on originating such loans to experienced, growing small- to medium-sized, privately-held companies with local or regional businesses and non-profit entities that operate in our market area.

When making commercial loans, we consider the financial statements of the borrower, our lending history with the borrower, the debt service capabilities and global cash flows of the borrower and other guarantors, the projected cash flows of the business and the value of the collateral, accounts receivable, inventory and equipment. All of these loans are secured by assets of the respective borrowers.

As of December 31, 2021, enterprise value loans, which we also refer to as search fund lending, merger and acquisition, re-capitalization, and shareholder/partner buyout loans, totaled \$340.3 million, with relationships spanning 26 states. We originate these loans to small- and medium-size businesses in a senior secured position; relying largely on the enterprise value of the business and ongoing cash flow to support operational and debt service requirements. These are fully amortizing term loans (up to seven years) with material levels of equity and/or combination of seller financing behind our senior secured lending. At December 31, 2021, the largest loan was \$29.4 million and is secured by all business assets. At December 31, 2021, the loan was performing in accordance with its original repayment terms.

The following table provides information with respect to our enterprise value loans by type at December 31, 2021.

Type of Industry	Balance (In thousands)
Advertising	\$ 37,800
Consulting services	40,425
Industrial/manufacturing/warehouse	66,027
Information technology and software	19,442
Landscaping	13,421
Non-essential retail	61,391
Real estate services	38,612
Other	63,187
Total	\$ 340,305

The non-essential retail loans include the following sectors:

Type of Industry	Balance (In thousands)
Home & garden	\$ 1,393
Personal services	9,000
Professional services	25,982
Repairs and maintenance	8,870
Sporting goods and hobbies	3,429
Wholesale	12,717
Total	\$ 61,391

In late 2020, the Bank began offering lines of credit to enterprise businesses in the digital asset space. These lines of credit are utilized by digital asset businesses to further their offerings in crypto-backed lending, margin trading, crypto mining operations, or other growth initiatives in the rapidly expanding industry. These lines of credit are collateralized by the United States dollar (“USD”) value of the digital currency. The Bank uses a custodian to hold the digital currency and monitors the collateral coverage ratio on an ongoing basis. If warranted, the Bank will instruct the custodian to liquidate the collateral and provide us with the USD proceeds of the liquidation. In 2021 the Bank expanded its loan offerings in the digital asset space by offering term loans to purchase mining equipment. We lend based

on the loan to value of the equipment with a term generally ranging from 24 to 30 months. At December 31, 2021, credit lines to digital asset companies totaled \$120.5 million, with relationships spanning eight states. The largest loan was \$36.0 million and is secured by the USD value of the digital currency. At December 31, 2021, the loan was performing in accordance with its original payment terms.

In 2015, we started originating loans to developers of commercial-scale renewable energy facilities, primarily in New England and New York, and at December 31, 2021, we had a total of \$62.3 million in renewable energy loans. Our renewable energy loans primarily include loans secured by solar arrays and battery storage operations which work in conjunction with the solar arrays. The average term and amortization for these loans can extend to 15 years or more, given the asset life, and are generally underwritten to lesser term than the associated power purchase agreement (“PPA”) supporting the repayment of each loan. The term of the loan is also shorter than the life expectancy of the related equipment. Generally, the underwriting criteria includes: a report supporting the power generation capacity and ultimately the ability to generate sufficient cash flows, assignment of the associated PPA, analysis on the quality of the power off-taker, an overall business valuation, and appropriate loan covenants, which may include maximum loan-to-value and minimum debt service coverage requirements. At December 31, 2021, \$49.7 million, or 79.7%, of our renewable energy loans was secured by solar arrays. The largest loan was \$11.9 million and is secured by all business assets of the company, including the solar array and an assignment of the PPA. At December 31, 2021, the loan was performing in accordance with its original repayment terms.

A portion of our commercial business loans are guaranteed by the SBA through the SBA 7(a) loan program. The SBA 7(a) loan program supports, through a U.S. Government guarantee, some portion of the traditional commercial loan underwriting that might not be fully covered absent the guarantee. A typical example would be a business acquiring another business, where the value purchased is an enterprise value (as opposed to tangible assets), which results in a collateral shortfall under traditional loan underwriting requirements. In addition, SBA 7(a) loans, through term loans, can provide a good source of permanent working capital for growing companies. BankProv is a Preferred Lender under the SBA’s PLP Program, which allows expedited underwriting and approval of SBA 7(a) loans.

The Coronavirus Aid, Relief and Economic Security Act (the “CARES Act”) was signed into law on March 27, 2020 as a \$2 trillion legislative package. The goal of the CARES Act was 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 CARES Act also included extensive emergency funding for hospitals and providers. The Economic Aid Act amended the PPP by extending the authority of the SBA to guarantee loans and the ability of PPP lenders to disburse PPP loans until March 31, 2021. The PPP Extension Act of 2021, which was enacted on March 30, 2021, extended the PPP application deadline to May 31, 2021, and provided the SBA additional time to process applications through June 30, 2021. During the first round of the PPP, the Company originated \$78.0 million in PPP loans. During the second round of the PPP, the Company originated an additional \$46.0 million in PPP loans. The Company continues to work with customers who received PPP loans on applying for loan forgiveness, and as of December 31, 2021, of the \$124.0 million in PPP loans issued, only \$12.4 million remained outstanding with unaccrued fee income totaling \$503,000.

Our two largest commercial business loans at December 31, 2021 totaled \$36.0 million and \$35.0 million, were originated in 2021 and 2020, respectively, and are commercial lines to digital asset companies. The third largest commercial loan totaled \$29.4 million, was originated in 2021 and is an enterprise value loan. As of December 31, 2021, the loans were performing in accordance with the original repayment terms.

Commercial Real Estate Loans. At December 31, 2021, commercial real estate loans were \$432.3 million, or 29.7% of our total loan portfolio. This amount includes \$31.5 million of multi-family residential real estate loans, which we consider a subset of commercial real estate loans, and which are described below. Our commercial real estate loans are generally secured by properties used for business purposes such as office buildings, industrial facilities and retail facilities; however, we also originate loans secured by investment real estate in the form of residential rental units. At December 31, 2021, \$180.4 million of our commercial real estate portfolio was secured by owner occupied commercial real estate, and \$251.9 million was secured by income producing, or non-owner occupied commercial real estate. We currently target new commercial real estate loan originations to experienced, growing small- and mid-size owners and investors in our market area. The average outstanding loan in our commercial real estate portfolio was \$663,000 as of December 31, 2021, although we originate commercial real estate loans with balances significantly larger than this average. At December 31, 2021, our ten largest commercial real estate loans had an average balance of \$9.2 million.

We focus our commercial real estate lending on properties within our primary market areas, but we will originate commercial real estate loans on properties located outside the area based on an established relationship with a strong borrower. We intend to continue to grow our commercial real estate loan portfolio while maintaining prudent underwriting standards. In addition to originating these loans, we occasionally will participate in commercial real estate loans with other financial institutions. Such participations are underwritten in accordance with our policies before we will participate in such loans.

We originate a variety of fixed- and adjustable-rate commercial real estate loans with terms and amortization periods generally up to 20 years, although our Loan Policy permits longer terms and amortization periods depending on the risk profile, which may include balloon loans. Interest rates and payments on our adjustable-rate loans adjust every three, five or seven years and generally are indexed to the corresponding Federal Home Loan Bank borrowing rate plus a margin. Most of our adjustable-rate commercial real estate loans adjust

every five years and amortize over terms of 20 years. We generally include pre-payment penalties on commercial real estate loans we originate.

The following table provides information with respect to our commercial real estate loans by type at December 31, 2021. The table excludes multi-family residential real estate loans, discussed below.

Type of Loan	Number	Balance (In thousands)
Residential one-to-four family	135	\$ 38,108
Mixed use	84	59,160
Office	74	49,102
Retail	43	22,731
Industrial/manufacturing/warehouse	108	71,922
Hotel/motel/inn	16	25,392
Mobile home/park	9	31,906
Self-storage facility	15	29,940
Other commercial real estate	110	72,538
Total	594	\$ 400,799

If we foreclose on a commercial real estate loan, the marketing and liquidation period to convert the real estate asset to cash can be lengthy with substantial holding costs. In addition, vacancies, deferred maintenance, repairs and market stigma can result in prospective buyers expecting sale price concessions to offset their real or perceived economic losses for the time it takes them to return the property to profitability. Depending on the individual circumstances, initial charge-offs and subsequent losses on commercial real estate loans can be unpredictable and substantial.

Our largest single commercial real estate loan at December 31, 2021 totaled \$16.0 million, was originated in 2013 and is a commercial line of credit secured by non-owner occupied commercial use property. Our next largest commercial real estate loan at December 31, 2021 was for \$15.8 million, was originated in 2019 and is secured by non-owner occupied commercial use property. The third largest commercial real estate loan was for \$13.3 million, was originated in 2019 and is secured by non-owner occupied commercial use property. All of the collateral securing these loans is located in our primary lending area. At December 31, 2021, all of these loans were performing in accordance with their original repayment terms.

Multi-Family Residential Real Estate Loans. At December 31, 2021, multi-family real estate loans were \$31.5 million, or 2.2% of our total loan portfolio. We do not focus on the origination of multi-family real estate lending, but we will originate these loans to well-qualified borrowers when opportunities exist that meet our underwriting standards. We currently originate new individual multi-family real estate loans to experienced, growing small- and mid-size owners and investors in our market area. Our multi-family real estate loans are generally secured by properties consisting of five to 15 rental units. The average outstanding loan size in our multi-family real estate portfolio was \$525,000 as of December 31, 2021. We generally do not make multi-family real estate loans outside our primary market areas. In addition to originating these loans, we also participate in multi-family residential real estate loans with other financial institutions. Such participations are underwritten in accordance with our policies before we will participate in such loans.

We originate a variety of fixed- and adjustable-rate multi-family real estate loans for terms up to 30 years. Interest rates and payments on our adjustable-rate loans adjust every three, five or seven years and generally are indexed to the corresponding Federal Home Loan Bank borrowing rate plus a margin. Most of our adjustable-rate multi-family real estate loans adjust every five years and amortize over terms of 20 to 25 years. We also include pre-payment penalties on loans we originate.

If we foreclose on a multi-family real estate loan, the marketing and liquidation period to convert the real estate asset to cash can be lengthy with substantial holding costs. In addition, vacancies, deferred maintenance, repairs and market stigma can result in prospective buyers expecting sale price concessions to offset their real or perceived economic losses for the time it takes them to return the property to profitability. Depending on the individual circumstances, initial charge-offs and subsequent losses on commercial real estate loans can be unpredictable and substantial.

Our largest multi-family real estate loan at December 31, 2021 totaled \$3.3 million, was originated in 2017 and is secured by a multi-family property. At December 31, 2021, this loan was performing in accordance with its original repayment terms.

Construction and Land Development Loans. At December 31, 2021, construction and land development loans were \$42.8 million, or 2.9% of our total loan portfolio, consisting of \$6.5 million of one- to four-family residential and condominium construction loans and \$36.3 million of commercial and multi-family real estate construction loans. At December 31, 2021, \$34.8 million of our commercial and multi-family real estate construction loans are expected to convert to permanent loans upon completion of the construction phase. The majority of the balance of these loans is secured by properties located in our primary lending area.

We primarily make construction loans for commercial development projects, including hotels, condominiums and single family residences, small industrial buildings, retail and office buildings and apartment buildings. Most of our construction loans are interest-only loans that provide for the payment of interest during the construction phase, which is usually up to 12 to 24 months, although some construction loans are renewed, generally for one or two additional years. At the end of the construction phase, the loan may convert to a permanent mortgage loan or the loan may be paid in full.

We also originate construction and site development loans to contractors and builders to finance the construction of single-family homes and subdivisions. While we may originate these loans whether or not the collateral property underlying the loan is under contract for sale, we consider each project carefully in light of current residential real estate market conditions. We actively monitor the number of unsold homes in our construction loan portfolio and local housing markets to attempt to maintain an appropriate balance between home sales and new loan originations. We generally will limit the maximum number of speculative units (units that are not pre-sold) approved for each project to two units. We have attempted to diversify the risk associated with speculative construction lending by doing business with experienced small and mid-sized builders within our market area.

Residential real estate construction loans include single-family tract construction loans for the construction of entry level residential homes. While maturity dates for residential construction loans are largely a function of the estimated construction period of the project, and generally do not exceed one year, land development loans generally are for 18 to 24 months. Substantially all of our residential construction loans have adjustable rates of interest based on The Wall Street Journal prime rate plus a margin. Construction loan proceeds are disbursed periodically in increments as construction progresses and as inspection by our approved inspectors warrant.

Our largest construction and land development loan at December 31, 2021 totaled \$9.3 million, was originated in 2018 and is secured by commercial use property.

Mortgage Warehouse Loans. In 2020, the Bank completed an asset purchase of a mortgage warehouse line of business. Our mortgage warehouse lending business has a national platform with relationship managers across the United States that offers facility lines to independent non-bank mortgage origination companies, which allow them to fund the closing of residential mortgage loans. Each facility advance is fully collateralized by a security interest in one- to four-family residential mortgage loans and are further enhanced by deposit balances. The primary source of repayment of the facility lines is the sale of the underlying mortgage loans to outside investors, which typically occurs within 15 days. These investors can include Federal National Mortgage Association/Federal Home Loan Mortgage Corporation and Government National Mortgage Association, as well as other large financial institutions who aggregate pools of loans.

To approve facility lines to non-bank mortgage origination borrowers we conduct a thorough due diligence of the company and its ownership to assess the financial performance including assets and liquidity and regulatory profile. To underwrite the companies we use a proprietary risk based scoring model that correlates to our internal regulatory loan risk grading system. We continually monitor companies' performance through both internal and external financial management and quality reviews. At December 31, 2021, mortgage warehouse loans were \$253.8 million, or 17.4% of total loans.

Consumer Loans. At December 31, 2021, consumer loans were \$1.5 million, or 0.1% of total loans. In 2016, we entered into an agreement to purchase pools of unsecured consumer loans through the BancAlliance Lending Club Program. This program encompasses loans risk graded by Lending Club as A through C with a 680 minimum credit score, out of a possible risk grade of A through G. The Lending Club retains the servicing of these loans. As of December 31, 2021, we had \$1.4 million in outstanding consumer loans that were purchased through this program. Our last Lending Club investment purchase was in 2018 and as of May 2019, we stopped reinvesting any proceeds in new pools. At this time, we do not anticipate purchasing any new loans through this network.

The remaining loans in this portfolio are loans secured by certificate accounts and overdraft lines of credit. We discontinued lending for loans secured by certificate accounts in 2020 to focus on commercial loan originations. Accordingly, we expect our portfolio of certificate account secured loans to decrease over time due to normal amortization and repayments. We are continuing to offer overdraft lines of credit. Consumer loans generally do not have prepayment penalties. The procedures for underwriting consumer loans include an assessment of the applicant's payment history on other debts and ability to meet existing obligations and payments on the proposed loan.

Loan Underwriting Risks

Commercial Business Loans. Unlike residential mortgage loans, which generally are made on the basis of the borrower's ability to make repayment from his or her employment or other income, and which are secured by real property whose value tends to be more easily ascertainable, commercial business loans are of higher risk and typically are made on the basis of the borrower's ability to make repayment from the cash flow of the borrower's business and the collateral securing these loans may fluctuate in value. Our commercial business loans are originated primarily based on the identified cash flow of the borrower and secondarily on the underlying collateral provided by the borrower. Most often, this collateral consists of accounts receivable, inventory or equipment, the value of which may depreciate over time, may be more difficult to appraise and may be more susceptible to fluctuation in value. Credit support provided by

the borrower for most of these loans and the probability of repayment is based on the liquidation of the pledged collateral and enforcement of a personal guarantee, if any. As a result, the availability of funds for the repayment of commercial business loans may depend substantially on the success of the business itself. These types of loans are generally more sensitive to regional and local economic conditions, making loss levels more difficult to predict.

Enterprise value loans may expose us to a greater risk of non-payment and loss than our other business loans because: (1) repayment of such loans may be dependent upon the successful execution of the borrower's business plan, which may include new management and be based on projected cash flows that may include business synergies, cost savings, and revenue growth that have yet to be realized; (2) they may require additional financing from their private equity sponsors or others, a successful sale to a third party, a public offering, or some other form of liquidity event; or (3) in the event of default and liquidation, there may be reliance on the sale of intangible assets that may have insufficient value to repay the debt in full.

Commercial and Multi-Family Real Estate Loans. Loans secured by commercial and multi-family real estate generally have larger balances and involve a greater degree of risk than one- to four-family residential mortgage loans. In addition, many of our commercial borrowers have more than one loan outstanding with us. Consequently, an adverse development with respect to one loan or one credit relationship can expose us to a significantly greater risk of loss compared to an adverse development with respect to a one- to four-family residential mortgage loan. Of primary concern in commercial and multi-family real estate lending is the borrower's creditworthiness and the feasibility and cash flow potential of the project. Payments on loans secured by income producing properties often depend on successful operation and management of the properties. As a result, repayment of such loans may be subject to a greater extent than residential real estate loans to adverse conditions in the real estate market or the economy. To monitor cash flows on income producing properties, we require borrowers and loan guarantors, if any, to provide annual financial statements on commercial and multi-family real estate loans. In reaching a decision on whether to make a commercial or multi-family real estate loan, we consider and review a global cash flow analysis of the borrower and consider the net operating income of the property, the borrower's expertise, credit history and profitability and the value of the underlying property. We have generally required that the properties securing these real estate loans have debt service coverage ratios (the ratio of earnings before debt service to debt service) of at least 1.20x. In accordance with our loan policy, an environmental phase one report may be obtained when the possibility exists that hazardous materials may have existed on the site, or the site may have been impacted by adjoining properties that handled hazardous materials. These types of loans are generally more sensitive to regional and local economic conditions, making loss levels more difficult to predict. In addition, some of our commercial real estate loans are not fully amortizing and contain large balloon payments upon maturity. These balloon payments may require the borrower to either sell or refinance the underlying property in order to make the balloon payment, which may increase the risk of default or non-payment.

Further, if we foreclose on a commercial real estate or multi-family real estate loan, our holding period for the collateral may be longer than for one- to four-family residential mortgage loans because there are fewer potential purchasers of the collateral, which can result in substantial holding costs. In addition, vacancies, deferred maintenance, repairs and market stigma can result in prospective buyers expecting sale price concessions to offset their real or perceived economic losses for the time it takes them to return the property to profitability.

Construction and Land Development Loans. Our construction loans are based upon estimates of costs and values associated with the completed project. Underwriting is focused on the borrowers' financial strength, credit history and demonstrated ability to produce a quality product and effectively market and manage their operations. All construction loans for which the builder does not have a binding purchase agreement must be approved by senior loan officers.

Construction lending involves additional risks when compared with permanent residential lending because funds are advanced upon the security of the project, which is of uncertain value prior to its completion. Because of the uncertainties inherent in estimating construction costs, as well as the market value of the completed project and the effects of governmental regulation of real property, it is relatively difficult to evaluate accurately the total funds required to complete a project and the related loan-to-value ratio. This type of lending also typically involves higher loan principal amounts and is often concentrated with a small number of builders. In addition, generally during the term of a construction loan, interest may be funded by the borrower or disbursed from an interest reserve set aside from the construction loan budget. These loans often involve the disbursement of substantial funds with repayment substantially dependent on the success of the ultimate project and the ability of the borrower to sell or lease the property or obtain permanent take-out financing, rather than the ability of the borrower or guarantor to repay principal and interest. If the appraised value of a completed project proves to be overstated, we may have inadequate security for the repayment of the loan upon completion of construction of the project and may incur a loss. A discounted cash flow analysis is utilized for determining the value of any construction project of five or more units. Our ability to continue to originate a significant amount of construction loans is dependent on the strength of the housing market in our market areas.

Land loans secured by improved lots generally involve greater risks than residential mortgage lending because land loans are more difficult to evaluate. If the estimate of value proves to be inaccurate, in the event of default and foreclosure, we may be confronted with a property the value of which is insufficient to assure full payment. These types of loans are generally more sensitive to regional and local economic conditions, making loss levels more difficult to predict.

Mortgage Warehouse Loans. Mortgage warehouse loans are primarily facility lines to non-bank mortgage origination companies. The risk of fraud associated with this type of lending includes, but is not limited to, settlement process risks, the risk of financing nonexistent loans or fictitious mortgage loan transactions, or the risk that collateral delivered is fraudulent or non-existent, creating a risk of loss of the full amount financed on the underlying residential mortgage loan, or in the settlement processes. In addition to fraud risk, there is also the risk of the mortgage companies being unable to sell the loans.

Adjustable-Rate Loans. While we anticipate that adjustable-rate loans will better offset the adverse effects of an increase in interest rates as compared to fixed-rate loans, an increased monthly mortgage payment required of adjustable-rate loan borrowers in a rising interest rate environment could cause an increase in delinquencies and defaults. The marketability of the underlying property also may be adversely affected in a high interest rate environment. In addition, although adjustable-rate mortgage loans make our asset base more responsive to changes in interest rates, the extent of this interest sensitivity is limited by the annual and lifetime interest rate adjustment limits on residential loans.

Consumer Loans. Consumer loans may entail greater risk than residential mortgage loans, particularly in the case of consumer loans that are unsecured or secured by assets that depreciate rapidly. Repossessed collateral for a defaulted consumer loan may not provide an adequate source of repayment for the outstanding loan and a small remaining deficiency often does not warrant further substantial collection efforts against the borrower. Consumer loan collections depend on the borrower's continuing financial stability, and therefore are likely to be adversely affected by various factors, including job loss, divorce, illness or personal bankruptcy. Furthermore, the application of various federal and state laws, including federal and state bankruptcy and insolvency laws, may limit the amount that can be recovered on such loans.

Loan Originations, Purchases and Sales

We have grown our loan portfolio by developing expertise for customers who typically have not been supported by larger financial institutions but whose business needs are usually too complex for smaller institutions. Loan originations come from a variety of sources. The primary sources of loan originations are current customers, business development by our relationship managers, walk-in traffic, our website, networking events and referrals from customers as well as our directors, business owners, investors, entrepreneurs, builders, realtors, and other professional third parties, including brokers. Loan originations are further supported by lending services offered through cross-selling and employees' community service.

Historically, we generally originated loans for our portfolio. We occasionally sell participation interests in commercial real estate loans and commercial business loans to local financial institutions, primarily on the portion of loans exceeding our borrowing limits. At December 31, 2021, we were servicing \$25.6 million of commercial real estate and commercial business loans where we had sold an interest to local financial institutions. We sold loan participations of \$12.9 million and \$1.4 million for the years ended December 31, 2021 and 2020, respectively.

While we generally do not purchase whole loans, we will occasionally purchase loan participations from other financial institutions and have in previous years purchased through a shared national credit program. As of December 31, 2021, we had \$8.9 million of outstanding purchased loans. We do not expect to make any purchases through a shared national credit program going forward. We purchased loans totaling \$6.3 million for the year ended December 31, 2021. We did not have any loan participation purchases for the year ended December 31, 2020.

Loan Approval Procedures and Authority

Our lending activities follow written, non-discriminatory, underwriting standards and loan origination procedures established by BankProv's board of directors and management. BankProv's board of directors has granted loan approval authority to certain officers up to prescribed limits, depending on the officer's experience, the type of loan and whether the loan is secured or unsecured. All loans require the approval of a minimum of two lending officers, one of which must be a Senior Vice President or above (the exception is borrowing relationships of \$25,000 and below, which can be approved by one officer with sufficient authority for that loan type, as well as, loans of any amount which are 100% cash secured). For loan relationships below \$2.0 million, approval is required by designated individuals with delegated loan authority as identified within our loan policy. Our loan policy dictates that for loan relationships of between \$2.0 million and \$3.0 million approval is required by one of the following members of Credit Committee: Chief Executive Officer, Chief Financial Officer, Chief Lending Officer and/or Senior Credit Officer. Loan relationships exceeding \$3.0 million in exposure that involve exceptions to policy, including loans in excess of our internal loans-to-one borrower limitation, must be authorized by BankProv's Risk Committee of the board of directors. Exceptions are fully disclosed to the approving authority, either an individual officer or the appropriate management or board committee prior to commitment. Exceptions are reported to the board of directors quarterly.

When entering a new lending line, we typically seek to manage risks and costs by limiting initial activity. We then decide whether it would be profitable and consistent with our risk tolerance levels to expand the activity, and continually calibrate and adjust our actions to maintain appropriate risk limitations.

Loans-to-One Borrower Limit and Loan Category Concentration

The maximum amount that we may lend to one borrower and the borrower's related entities is generally limited, by statute, to 20% of our capital, which is defined under Massachusetts law as the sum of our capital stock, surplus account and undivided profits. At December 31, 2021, our regulatory limit on loans-to-one borrower was \$44.4 million. We generally establish our internal loans-to-one borrower limit as 90% of our regulatory limit. As of December 31, 2021, this amount was \$39.9 million, with loans greater than this amount requiring approval by BankProv's Risk Committee of the board of directors.

At December 31, 2021, our largest lending relationship consisted of 11 commercial business loans and one commercial real estate loan with an exposure of \$44.4 million, secured by all business assets and owner-occupied investment real estate. Within this relationship, at December 31, 2021, one enterprise value loan for \$1.5 million and one for \$59,000 were six and two days delinquent, respectively. The remaining loans in the relationship were performing in accordance with their original repayment terms at December 31, 2021. Our second largest lending relationship consisted of three commercial business loans with a total exposure of \$37.0 million, secured by all business assets. This relationship was performing in accordance with its original repayment terms at December 31, 2021. Our third largest lending relationship consisted of one commercial business line, with a total exposure of \$36.0 million, secured by the USD value of the business' digital currency. This relationship was performing in accordance with its original repayment terms at December 31, 2021. Our fourth largest lending relationship consisted of one commercial business line with a total exposure of \$35.0 million, secured by the USD value of the business' digital currency. Our fifth largest lending relationship consisted of two commercial business loans, with a total exposure of \$34.4 million, secured by all business assets. The relationship was performing in accordance with its original repayment terms at December 31, 2021.

Investment Activities

We have legal authority to invest in various types of investment securities and liquid assets, including U.S. Treasury obligations, securities of various government-sponsored enterprises, residential mortgage-backed securities and municipal government bonds, deposits at the Federal Home Loan Bank of Boston, certificates of deposit of federally insured institutions, investment grade corporate bonds and investment grade marketable equity securities, including common stock and money market mutual funds. We also are required to maintain an investment in Federal Home Loan Bank of Boston stock, which investment is based on the level of our Federal Home Loan Bank borrowings. While we have the authority under applicable law to invest in derivative securities, we had no investments in derivative securities at December 31, 2021.

At December 31, 2021, our investment portfolio had a fair value of \$36.8 million, and consisted of U.S. Government Agency mortgage-backed securities, and state and municipal bonds.

Our investment objectives are to provide and maintain liquidity, to establish an acceptable level of interest rate and credit risk, to provide a use of funds when demand for loans is weak and to generate a favorable return. Our board of directors has the overall responsibility for the investment portfolio, including approval of our investment policy. The Risk Committee of the board of directors and management are responsible for implementation of the investment policy and monitoring our investment performance. Our Risk Committee reviews the status of our investment portfolio quarterly.

Each reporting period, we evaluate all debt securities with a decline in fair value below the amortized cost of the investment to determine whether or not the impairment is deemed to be other-than-temporarily impaired ("OTTI"). OTTI is required to be recognized if (1) we intend to sell the security; (2) it is more likely than not that we will be required to sell the security before recovery of its amortized cost basis; or (3) for debt securities, the present value of expected cash flows is not sufficient to recover the entire amortized cost basis. For all impaired debt securities that we intend to sell, or more likely than not will be required to sell, the full amount of the depreciation is recognized as OTTI resulting in a realized loss that is a charged to earnings through a reduction in our noninterest income. For all other impaired debt securities, credit-related OTTI is recognized through earnings and non-credit related OTTI is recognized in other comprehensive income/loss, net of applicable taxes. We did not recognize any OTTI during the years ended December 31, 2021 or 2020.

Sources of Funds

General. Deposits have traditionally been our primary source of funds for use in lending and investment activities. We also use borrowings, primarily Federal Home Loan Bank of Boston advances, brokered deposits and certificates of deposit obtained from a national exchange, to supplement cash flow needs, lengthen the maturities of liabilities for interest rate risk purposes and to manage the cost of funds. In addition, funds are derived from scheduled loan payments, investment securities maturities and sales, loan prepayments, retained earnings and income on earning assets. While scheduled loan payments and income on earning assets are relatively stable

sources of funds, deposit inflows and outflows can vary widely and are influenced by prevailing interest rates, market conditions and levels of competition.

Deposit Accounts. The majority of our deposits (other than certificates of deposit) are from depositors who reside in our primary market areas. However, a significant portion of our brokered certificates of deposits and QwickRate deposits, described below, are from depositors located outside our primary market areas. We also receive deposits from our nationwide business customers. Deposits are attracted through the offering of a broad selection of deposit instruments, including noninterest-bearing demand deposits (such as checking accounts), interest-bearing demand accounts (such as NOW and money market accounts), savings accounts and certificates of deposit. In addition to accounts for individuals, we also offer several commercial checking accounts designed for the businesses operating in our market area, and we encourage our commercial borrowing customers to maintain their deposit relationships with us.

We have grown our core deposits (which we define as all deposits except for certificates of deposit) through a variety of strategies, including investing in technology and hiring additional employees, as well as proactive interaction with our customers. Our investment in technology has enabled us to better serve commercial customers who demand faster processing times and simplified online interaction. For example, we provide deposit and cash management services for 1031 qualified intermediaries, digital currency customers, payroll providers and community association management companies. Funds we receive from digital currency customers are denominated in U.S. dollars; we do not have any digital assets or liabilities on our balance sheet and we do not take any digital currency exchange rate risk. In addition, we believe that our specialized commercial activities have provided opportunities to generate business deposits from those customers, including from customers outside of our branch network, that may not be available to traditional community banks.

At December 31, 2021, our deposits totaled \$1.46 billion. As of that date, our certificates of deposit included \$20.2 million of brokered certificates of deposit and \$16.8 million of QwickRate certificates of deposit, where we gather certificates of deposit nationwide by posting rates we will pay on these deposits. At December 31, 2021, all of our QwickRate certificates of deposit were in amounts of \$100,000 or greater.

Deposit account terms vary according to the minimum balance required, the time period that funds must remain on deposit, and the interest rate, among other factors. In determining the terms of our deposit accounts, we consider the rates offered by our competition, our liquidity needs, profitability, and customer preferences and concerns. We generally review our deposit mix and pricing on a weekly basis. Our deposit pricing strategy has generally been to offer competitive rates and services and to periodically offer special rates in order to attract deposits of a specific type or term, although we have not done so in recent periods. We do not price our deposit products to be among the highest rate paying institution in our market area, but instead focus on services to gather deposits.

Borrowings. We primarily utilize advances from the Federal Home Loan Bank of Boston to supplement our supply of investable funds. The Federal Home Loan Bank functions as a central reserve bank providing credit for its member financial institutions. As a member, we are required to own capital stock in the Federal Home Loan Bank and are authorized to apply for advances on the security of such stock and certain of our whole first mortgage loans and other assets (principally securities which are obligations of, or guaranteed by, the United States), provided certain standards related to creditworthiness have been met. Advances are made under several different programs, each having its own interest rate and range of maturities. Depending on the program, limitations on the amount of advances are based either on a fixed percentage of an institution's net worth or on the Federal Home Loan Bank's assessment of the institution's creditworthiness. As of December 31, 2021, we had a borrowing capacity of \$141.3 million with the Federal Home Loan Bank of Boston, including an available line of credit of \$2.0 million at an interest rate that adjusts daily. On that date, we had \$13.5 million in advances outstanding from the Federal Home Loan Bank of Boston. All of our borrowings from the Federal Home Loan Bank are secured by investment securities and qualified collateral, including one- to four-family loans and multi-family and commercial real estate loans held in our portfolio.

From time to time and dependent on rates, we may utilize the FRB Borrower In Custody ("BIC") program as a source of overnight borrowings. Borrowings from the FRB BIC program are secured by a Uniform Commercial Code ("UCC") financing statement on qualified collateral, consisting of certain commercial loans and qualified mortgage-backed government securities. We did not have any outstanding FRB borrowings at December 31, 2021 or 2020.

Personnel

As of December 31, 2021, we had 170 full-time and ten part-time employees, none of whom is represented by a collective bargaining unit. We believe we have a good working relationship with our employees.

Subsidiaries

The Provident Bank's subsidiaries include Provident Security Corporation and 5 Market Street Security Corporation, which were established to buy, sell, and hold investments for their own account.

SUPERVISION AND REGULATION

General

The Provident Bank is a Massachusetts-chartered stock savings bank. The Bank's deposits are insured up to applicable limits by the Federal Deposit Insurance Corporation and by the Depositors Insurance Fund for amounts in excess of the Federal Deposit Insurance Corporation insurance limits. The Provident Bank is subject to extensive regulation by the Massachusetts Commissioner of Banks, as its chartering agency, and by the Federal Deposit Insurance Corporation, as its primary federal regulatory and primary deposit insurer. The Provident Bank is required to file reports with, and is periodically examined by, the Federal Deposit Insurance Corporation and the Massachusetts Commissioner of Banks concerning its activities and financial condition and must obtain regulatory approvals prior to entering into certain transactions, including, but not limited to, mergers with or acquisitions of other financial institutions. The Provident Bank is a member of the Federal Home Loan Bank of Boston.

The regulation and supervision of The Provident Bank establish a comprehensive framework of activities in which an institution can engage and is intended primarily for the protection of depositors and borrowers and, for purposes of the Federal Deposit Insurance Corporation, the protection of the insurance fund. The regulatory structure also gives the regulatory authorities extensive discretion in connection with their supervisory and enforcement activities and examination policies, including policies with respect to the classification of assets and the establishment of adequate loan loss reserves for regulatory purposes.

As a bank holding company, Provident Bancorp, Inc. is required to comply with the rules and regulations of the Federal Reserve Board. It is required to file certain reports with the Federal Reserve Board and is subject to examination by and the enforcement authority of the Federal Reserve Board. Provident Bancorp, Inc. is also subject to the rules and regulations of the Securities and Exchange Commission under the federal securities laws.

Any change in applicable laws or regulations, whether by the Massachusetts Commissioner of Banks, the Federal Deposit Insurance Corporation, the Federal Reserve Board, the Commonwealth of Massachusetts or Congress, could have a material adverse impact on the operations and financial performance of Provident Bancorp, Inc. and The Provident Bank. In addition, Provident Bancorp, Inc. and The Provident Bank are affected by the monetary and fiscal policies of various agencies of the United States Government, including the Federal Reserve Board. In view of changing conditions in the national economy and in the money markets, it is impossible for management to accurately predict future changes in monetary policy or the effect of such changes on the business or financial condition of Provident Bancorp, Inc. and The Provident Bank.

Set forth below is a brief description of material regulatory requirements that are or will be applicable to The Provident Bank and Provident Bancorp, Inc. The description is limited to certain material aspects of the statutes and regulations addressed, and is not intended to be a complete description of such statutes and regulations and their effects on The Provident Bank and Provident Bancorp, Inc.

Massachusetts Banking Laws and Supervision

The Provident Bank, as a Massachusetts-chartered stock savings bank, is regulated and supervised by the Massachusetts Commissioner of Banks. The Massachusetts Commissioner of Banks is required to regularly examine each state-chartered bank. The approval of the Massachusetts Commissioner of Banks is required to establish or close branches, to merge with another bank, to issue stock and to undertake many other activities. Any Massachusetts savings bank that does not operate in accordance with the regulations, policies and directives of the Massachusetts Commissioner of Banks may be sanctioned. The Massachusetts Commissioner of Banks may suspend or remove directors or officers of a savings bank who have violated the law, conducted a bank's business in a manner that is unsafe, unsound or contrary to the depositors' interests, or been negligent in the performance of their duties. In addition, the Massachusetts Commissioner of Banks has the authority to appoint a receiver or conservator if it is determined that the bank is conducting its business in an unsafe or unauthorized manner, and under certain other circumstances.

The powers that Massachusetts-chartered savings banks can exercise under these laws include, but are not limited to, the following.

Lending Activities. A Massachusetts-chartered savings bank may make a wide variety of mortgage loans including fixed-rate loans, adjustable-rate loans, variable-rate loans, participation loans, graduated payment loans, construction and development loans, condominium and co-operative loans, second mortgage loans and other types of loans that may be made in accordance with applicable regulations. Commercial loans may be made to corporations and other commercial enterprises with or without security. Consumer and personal loans may also be made with or without security.

Insurance Sales. Massachusetts savings banks may engage in insurance sales activities if the Massachusetts Commissioner of Banks has approved a plan of operation for insurance activities and the bank obtains a license from the Massachusetts Division of Insurance. A savings bank may be licensed directly or indirectly through an affiliate or a subsidiary corporation established for this purpose. Although The Provident Bank has received approval for insurance sales activities, it does not offer insurance products.

Investment Activities. In general, Massachusetts-chartered savings banks may invest in preferred and common stock of any corporation organized under the laws of the United States or any state provided such investments do not involve control of any corporation and do not, in the aggregate, exceed 4.0% of the bank's deposits. Massachusetts-chartered savings banks may in addition invest an amount equal to 1.0% of their deposits in stocks of Massachusetts corporations or companies with substantial employment in the Commonwealth which have pledged to the Massachusetts Commissioner of Banks that such monies will be used for further development within the Commonwealth. At the present time, The Provident Bank has the authority to invest in equity securities. However, such investment authority is constrained by federal law. See “—Federal Bank Regulation—Investment Activities” for such federal restrictions.

Dividends. A Massachusetts stock bank may declare from net profits cash dividends not more frequently than quarterly and non-cash dividends at any time. No dividends may be declared, credited or paid if the bank's capital stock is impaired. A Massachusetts savings bank with outstanding preferred stock may not, without the prior approval of the Commissioner of Banks, declare dividends to the common stock without also declaring dividends to the preferred stock. The approval of the Massachusetts Commissioner of Banks is required if the total of all dividends declared in any calendar year exceeds the total of its net profits for that year combined with its retained net profits of the preceding two years, less any required transfer to surplus or a fund for the retirement of any preferred stock. For this purpose, net profits mean the remainder of all earnings from current operations plus actual recoveries on loans and investments and other assets after deducting current operating expenses, actual losses, accrued dividends on preferred stock, if any, and all federal and state taxes.

Protection of Personal Information. Massachusetts has adopted regulatory requirements intended to protect personal information. The requirements are similar to existing federal laws such as the Gramm-Leach-Bliley Act, discussed below under “—Federal Bank Regulation—Privacy Regulations.” They require organizations to establish written information security programs to prevent identity theft. The Massachusetts regulation also contains technology system requirements, especially for the encryption of personal information sent over wireless or public networks or stored on portable devices.

Parity Approval. A Massachusetts bank may, in accordance with Massachusetts law, exercise any power and engage in any activity that has been authorized for national banks, federal thrifts or state banks in a state other than Massachusetts, provided that the activity is permissible under applicable federal law and not specifically prohibited by Massachusetts law. Such powers and activities must be subject to the same limitations and restrictions imposed on the national bank, federal thrift or out-of-state bank that exercised the power or activity. A Massachusetts bank may exercise such power and engage in such activities by providing 30 days' advanced written notice to the Massachusetts Commissioner of Banks.

Loans to One Borrower Limitations. Massachusetts banking law grants broad lending authority. However, with certain limited exceptions, total obligations of one borrower to a bank may not exceed 20.0% of the total of the bank's capital, which is defined under Massachusetts law as the sum of the bank's capital stock, surplus account and undivided profits.

Loans to a Bank's Insiders. Massachusetts law provides that a Massachusetts financial institution shall comply with Regulation O of the Federal Reserve Board, which generally requires that extensions of credit to insiders:

- be made on terms that are substantially the same as, and follow credit underwriting procedures that are not less stringent than, those prevailing for comparable transactions with unaffiliated persons and that do not involve more than the normal risk of repayment or present other unfavorable features; and
- not exceed certain limitations on the amount of credit extended to such persons, individually and in the aggregate, which limits are based, in part, on the amount of the Massachusetts financial institution's capital.

Regulatory Enforcement Authority. Any Massachusetts bank that does not operate in accordance with the regulations, policies and directives of the Massachusetts Commissioner of Banks may be subject to sanctions for non-compliance, including seizure of the property and business of the bank and suspension or revocation of its charter. The Massachusetts Commissioner of Banks may, under certain circumstances, suspend or remove officers or directors who have violated the law, conducted the bank's business in a manner which is unsafe, unsound or contrary to the depositors' interests or been negligent in the performance of their duties. In addition, upon finding that a bank has engaged in an unfair or deceptive act or practice, the Massachusetts Commissioner of Banks may issue an order to cease and desist and impose a fine on the bank concerned. Massachusetts consumer protection and civil rights statutes applicable to The Provident Bank permit private individual and class action lawsuits and provide for the rescission of consumer transactions, including loans, and the recovery of statutory and punitive damage and attorney's fees in the case of certain violations of those statutes.

Depositors Insurance Fund. The Provident Bank is a member of the Depositors Insurance Fund, a corporation that insures savings bank deposits in excess of federal deposit insurance coverage. The Depositors Insurance Fund is authorized to charge savings banks a risk-based assessment on deposit balances in excess of the amounts insured by the Federal Deposit Insurance Corporation.

Massachusetts has other statutes and regulations that are similar to the federal provisions discussed below.

Federal Bank Regulation

Interagency Statement on Loan Modifications. On March 22, 2020, the federal banking agencies issued an interagency statement to provide additional guidance to financial institutions who are working with borrowers affected by the coronavirus (“COVID-19”). The statement provided that agencies will not criticize institutions for working with borrowers and will not direct supervised institutions to automatically categorize all COVID-19 related loan modifications as troubled debt restructurings (“TDRs”). The agencies have confirmed with staff of the Financial Accounting Standards Board that short-term modifications made on a good faith basis in response to COVID-19 to borrowers who were current prior to any relief, are not TDRs. This includes short-term (e.g., six months) modifications such as payment deferrals, fee waivers, extensions of repayment terms, or other delays in payment that are insignificant. Borrowers considered current are those that are less than 30 days past due on their contractual payments at the time a modification program is implemented.

The statement further provided that working with borrowers that are current on existing loans, either individually or as part of a program for creditworthy borrowers who are experiencing short-term financial or operational problems as a result of COVID-19, generally would not be considered TDRs. For modification programs designed to provide temporary relief for current borrowers affected by COVID-19, financial institutions may presume that borrowers that are current on payments are not experiencing financial difficulties at the time of the modification for purposes of determining TDR status, and thus no further TDR analysis is required for each loan modification in the program.

The statement indicated that the agencies’ examiners will exercise judgment in reviewing loan modifications, including TDRs, and will not automatically adversely risk rate credits that are affected by COVID-19, including those considered TDRs.

In addition, the statement noted that efforts to work with borrowers of one- to-four family residential mortgages, where the loans are prudently underwritten, and not past due or carried on non-accrual status, will not result in the loans being considered restructured or modified for the purposes of their risk-based capital rules. With regard to loans not otherwise reportable as past due, financial institutions are not expected to designate loans with deferrals granted due to COVID-19 as past due because of the deferral.

The CARES Act. The CARES Act, which became law on March 27, 2020, provided over \$2 trillion to combat COVID-19 and stimulate the economy. The law had several provisions relevant to financial institutions, including:

- Allowing institutions not to characterize loan modifications relating to the COVID-19 pandemic as TDRs and also allowing them to suspend the corresponding impairment determination for accounting purposes.
- An option to delay the implementation of the accounting standard for current expected credit losses (“CECL”) until the earlier of December 31, 2020 or when the President declares that the coronavirus emergency is terminated. The effective date has subsequently been extended by the Financial Accounting Standards Board to fiscal years beginning after December 15, 2022, including interim periods within those fiscal years, for all institutions, except U.S. Securities and Exchange Commission filers that are not eligible to be smaller reporting companies.
- The ability of a borrower of a federally backed mortgage loan (VA, FHA, USDA, Freddie Mac and Fannie Mae) experiencing financial hardship due, directly or indirectly, to the COVID-19 pandemic to request forbearance from paying their mortgage by submitting a request to the borrower’s servicer affirming their financial hardship during the COVID-19 emergency. Such a forbearance could be granted for up to 180 days, with an extension for an additional 180-day period upon the request of the borrower. During that time, no fees, penalties or interest beyond the amounts scheduled or calculated as if the borrower made all contractual payments on time and in full under the mortgage contract will accrue on the borrower’s account. Except for vacant or abandoned property, the servicer of a federally backed mortgage is prohibited from taking any foreclosure action, including any eviction or sale action, for not less than the 60-day period beginning March 18, 2020, which was subsequently extended until September 30, 2021.
- The ability of a borrower of a multi-family federally backed mortgage loan that was current as of February 1, 2020, to submit a request for forbearance to the borrower’s servicer affirming that the borrower is experiencing financial hardship during the COVID-19 emergency. A forbearance could be granted for up to 30 days, with an extension for up to two additional 30-day periods upon the request of the borrower. During the time of the forbearance, the multi-family borrower cannot evict or initiate the eviction of a tenant or charge any late fees, penalties or other charges to a tenant for late payment of rent. Additionally, a multi-family borrower that receives a forbearance may not require a tenant to vacate a dwelling unit before a date that is 30 days after the date on which the borrower provides the tenant notice to vacate and may not issue a notice to vacate until after the expiration of the forbearance.

The Paycheck Protection Program. The Paycheck Protection Program (“PPP”), established as part of the CARES Act provided 100% federally guaranteed loans to eligible small businesses through the Small Business Administration’s (“SBA”) 7(a) loan guaranty program for amounts up to 2.5 times the average monthly “payroll costs” of the business. The entire principal amount of the borrower’s PPP

loan, including any accrued interest, is eligible for PPP loan forgiveness so long as employee and compensation levels of the business are maintained and 60% of the loan proceeds are used for payroll expenses, with the remaining 40% of the loan proceeds used for other qualifying expenses, including, but not limited to, mortgage interest, rent and utilities. In May 2021, the SBA announced that PPP funding has been exhausted and the SBA stopped accepting new PPP loan applications.

Coronavirus Response and Relief Supplemental Appropriations Act of 2021. On December 27, 2020, the Coronavirus Response and Relief Supplemental Appropriations Act of 2021 was signed into law, which also contains provisions that could directly impact financial institutions, including extending the time that insured depository institutions and depository institution holding companies have to comply with the CECL accounting standard and extending the authority granted to banks under the CARES Act to elect to temporarily suspend the requirements under U.S. GAAP applicable to troubled debt restructurings for loan modifications related to the COVID-19 pandemic for any loan that was not more than 30 days past due as of December 31, 2019.

Capital Requirements. Federal regulations require Federal Deposit Insurance Corporation-insured depository institutions to meet several minimum capital standards: a common equity Tier 1 capital to risk-based assets ratio of 4.5%, a Tier 1 capital to risk-based assets ratio of 6.0%, a total capital to risk-based assets ratio of 8%, and a Tier 1 capital to average assets leverage ratio of 4%.

For purposes of the regulatory capital requirements, common equity Tier 1 capital is generally defined as common stockholders' equity and retained earnings. Tier 1 capital is generally defined as common equity Tier 1 and additional Tier 1 capital. Additional Tier 1 capital includes certain noncumulative perpetual preferred stock and related surplus and minority interests in equity accounts of consolidated subsidiaries. Total capital includes Tier 1 capital (common equity Tier 1 capital plus additional Tier 1 capital) and Tier 2 capital. Tier 2 capital is comprised of capital instruments and related surplus, meeting specified requirements, and may include cumulative preferred stock and long-term perpetual preferred stock, mandatory convertible securities, intermediate preferred stock and subordinated debt. Also included in Tier 2 capital is the allowance for loan and lease losses limited to a maximum of 1.25% of risk-weighted assets and, for institutions that made such an election regarding the treatment of Accumulated Other Comprehensive Income ("AOCI"), up to 45% of net unrealized gains on available-for-sale equity securities with readily determinable fair market values. Institutions that have not exercised the AOCI opt-out have AOCI incorporated into common equity Tier 1 capital (including unrealized gains and losses on available-for-sale securities). The Provident Bank has exercised the opt-out and therefore does not include AOCI in its regulatory capital determinations. Calculation of all types of regulatory capital is subject to deductions and adjustments specified in the regulations.

In determining the amount of risk-weighted assets for purposes of calculating risk-based capital ratios, all assets, including certain off-balance sheet assets (e.g., recourse obligations, direct credit substitutes, residual interests) are multiplied by a risk weight factor assigned by the regulations based on the risks believed inherent in the type of asset. Higher levels of capital are required for asset categories believed to present greater risk. For example, a risk weight of 0% is assigned to cash and U.S. government securities, a risk weight of 50% is generally assigned to prudently underwritten first lien one to four-family residential mortgages, a risk weight of 100% is assigned to commercial and consumer loans, a risk weight of 150% is assigned to certain past due loans and a risk weight of between 0% to 600% is assigned to permissible equity interests, depending on certain specified factors.

In addition to establishing the minimum regulatory capital requirements, the regulations limit capital distributions and certain discretionary bonus payments to management if the institution does not hold a "capital conservation buffer" consisting of 2.5% of common equity Tier 1 capital to risk-weighted asset above the amount necessary to meet its minimum risk-based capital requirements. The capital conservation buffer requirement was fully implemented at 2.5% on January 1, 2019. At December 31, 2021, The Provident Bank exceeded the fully phased in regulatory requirement for the capital conservation buffer.

Legislation enacted in 2018 required the federal banking agencies, including the Federal Deposit Insurance Corporation, to establish a "community bank leverage ratio" of between 8 to 10% of average total consolidated assets for qualifying institutions with assets of less than \$10 billion. Institutions with capital meeting the specified requirements and electing to follow the alternative framework are deemed to comply with the applicable regulatory capital requirements, including the risk-based requirements. A qualifying institution may opt in and out of the community bank leverage ratio on its quarterly call report.

The federal regulators issued a final rule that set the optional community bank leverage ratio at 9%, effective the first quarter of 2020.

Section 4012 of the CARES Act of 2020 required that the community bank leverage ratio be temporarily lowered to 8%. The federal regulators issued a rule implementing the lower ratio, effective April 23, 2020. Another rule was issued to transition back to the 9% community bank leverage ratio by increasing the ratio to 8.5% for calendar year 2021 and 9% thereafter. The CBLR framework includes a two-quarter grace period for an institution that ceases to meet any qualifying criteria provided that the bank's leverage ratio falls no more than one percentage point below the applicable CBLR requirement. As of December 31, 2021, the Bank has not opted into the CBLR framework.

The Federal Deposit Insurance Corporation Improvement Act required each federal banking agency to revise its risk-based capital standards for insured institutions to ensure that those standards take adequate account of interest-rate risk, concentration of credit risk, and the risk of nontraditional activities, as well as to reflect the actual performance and expected risk of loss on multi-family residential

loans. The Federal Deposit Insurance Corporation, along with the other federal banking agencies, adopted a regulation providing that the agencies will take into account the exposure of a bank's capital and economic value to changes in interest rate risk in assessing a bank's capital adequacy. The Federal Deposit Insurance Corporation also has authority to establish individual minimum capital requirements in appropriate cases upon determination that an institution's capital level is, or is likely to become, inadequate in light of the particular circumstances.

Standards for Safety and Soundness. As required by statute, the federal banking agencies have adopted final regulations and Interagency Guidelines Establishing Standards for Safety and Soundness to implement safety and soundness standards. The guidelines set forth the safety and soundness standards that the federal banking agencies use to identify and address problems at insured depository institutions before capital becomes impaired. The guidelines address internal controls and information systems, internal audit system, credit underwriting, loan documentation, interest rate exposure, asset growth, asset quality, earnings and compensation, fees and benefits. The agencies have also established standards for safeguarding customer information. If the appropriate federal banking agency determines that an institution fails to meet any standard prescribed by the guidelines, the agency may require the institution to submit to the agency an acceptable plan to achieve compliance with the standard.

Investment Activities. All state-chartered Federal Deposit Insurance Corporation insured banks, including savings banks, are generally limited in their activities as principal and equity investments to activities and equity investments of the type and in the amount authorized for national banks, notwithstanding state law, subject to certain exceptions. For example, state-chartered banks may, with Federal Deposit Insurance Corporation approval, continue to exercise state authority to invest in common or preferred stocks listed on a national securities exchange and in the shares of an investment company registered under the Investment Company Act of 1940, as amended. The maximum permissible investment is 100% of Tier 1 Capital, as specified by the Federal Deposit Insurance Corporation's regulations, or the maximum amount permitted by Massachusetts law, whichever is less.

In addition, the Federal Deposit Insurance Corporation is authorized to permit such a state bank to engage in state-authorized activities or investments not permissible for national banks (other than non-subsidiary equity investments) if it meets all applicable capital requirements and it is determined that such activities or investments do not pose a significant risk to the Deposit Insurance Fund. The Federal Deposit Insurance Corporation has adopted procedures for institutions seeking approval to engage in such activities or investments. In addition, a nonmember bank may control a subsidiary that engages in activities as principal that would only be permitted for a national bank to conduct in a "financial subsidiary" if a bank meets specified conditions and deducts its investment in the subsidiary for regulatory capital purposes.

Interstate Banking and Branching. Federal law permits well capitalized and well managed bank holding companies to acquire banks in any state, subject to Federal Reserve Board approval, certain concentration limits and other specified conditions. Interstate mergers of banks are also authorized, subject to regulatory approval and other specified conditions. In addition, amendments made by the Dodd-Frank Act permit banks to establish de novo branches on an interstate basis to the extent that branching is authorized by the law of the host state for the banks chartered by that state.

Prompt Corrective Regulatory Action. Federal law requires, among other things, that federal bank regulatory authorities take "prompt corrective action" with respect to banks that do not meet minimum capital requirements. For these purposes, the law establishes five capital categories: well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized and critically undercapitalized.

The Federal Deposit Insurance Corporation has adopted regulations to implement the prompt corrective action legislation. An institution is deemed to be "well capitalized" if it has a CBLR leverage ratio of 9.0% or greater, or a total risk-based capital ratio of 10.0% or greater, a Tier 1 risk-based capital ratio of 8.0% or greater, a leverage ratio of 5.0% or greater and a common equity Tier 1 ratio of 6.5% or greater. An institution is "adequately capitalized" if it has a total risk-based capital ratio of 8.0% or greater, a Tier 1 risk-based capital ratio of 6.0% or greater, a leverage ratio of 4.0% or greater and a common equity Tier 1 ratio of 4.5% or greater. An institution is "undercapitalized" if it has a total risk-based capital ratio of less than 8.0%, a Tier 1 risk-based capital ratio of less than 6.0%, a leverage ratio of less than 4.0% or a common equity Tier 1 ratio of less than 4.5%. An institution is deemed to be "significantly undercapitalized" if it has a total risk-based capital ratio of less than 6.0%, a Tier 1 risk-based capital ratio of less than 4.0%, a leverage ratio of less than 3.0% or a common equity Tier 1 ratio of less than 3.0%. An institution is considered to be "critically undercapitalized" if it has a ratio of tangible equity (as defined in the regulations) to total assets that is equal to or less than 2.0%. As of December 31, 2021, The Provident Bank was a "well capitalized" institution under the Federal Deposit Insurance Corporation regulations.

At each successive lower capital category, an insured depository institution is subject to more restrictions and prohibitions, including restrictions on growth, restrictions on interest rates paid on deposits, restrictions or prohibitions on payment of dividends, and restrictions on the acceptance of brokered deposits. Furthermore, if an insured depository institution is classified in one of the undercapitalized categories, it is required to submit a capital restoration plan to the appropriate federal banking agency, and the holding company must guarantee the performance of that plan in an amount equal to the lesser of 5.0% of the institution's total assets when deemed undercapitalized or the amount necessary to achieve the status of adequately capitalized. Based upon its capital levels, a bank that is classified as well-capitalized, adequately capitalized, or undercapitalized may be treated as though it were in the next lower capital

category if the appropriate federal banking agency, after notice and opportunity for hearing, determines that an unsafe or unsound condition, or an unsafe or unsound practice, warrants such treatment. If an “undercapitalized” bank fails to submit an acceptable plan, it is treated as if it is “significantly undercapitalized.” “Significantly undercapitalized” banks must comply with one or more of a number of additional restrictions, including but not limited to an order by the Federal Deposit Insurance Corporation to sell sufficient voting stock to become adequately capitalized, requirements to reduce total assets, cease receipt of deposits from correspondent banks or dismiss directors or officers, and restrictions on interest rates paid on deposits, compensation of executive officers and capital distributions by the parent holding company. “Critically undercapitalized” institutions are subject to additional measures including, subject to a narrow exception, the appointment of a receiver or conservator within 270 days after it obtains such status.

The previously referenced rulemaking to establish a “community bank leverage ratio” adjusted the referenced categories for qualifying institutions that opt into the alternative framework for regulatory capital requirements. Institutions that exceed the community bank leverage ratio would be considered to have met the capital ratio requirements to be “well capitalized” for the agencies’ prompt corrective rules.

Transaction with Affiliates and Regulation W of the Federal Reserve Regulations. Transactions between banks and their affiliates are governed by federal law. An affiliate of a bank is any company or entity that controls, is controlled by or is under common control with the bank. In a holding company context, the parent bank holding company and any companies which are controlled by such parent holding company are affiliates of the bank (although subsidiaries of the bank itself, except financial subsidiaries, are generally not considered affiliates). Generally, Section 23A of the Federal Reserve Act and the Federal Reserve Board’s Regulation W limit the extent to which the bank or its subsidiaries may engage in “covered transactions” with any one affiliate to an amount equal to 10.0% of such institution’s capital stock and surplus, and with all such transactions with all affiliates to an amount equal to 20.0% of such institution’s capital stock and surplus. Section 23B applies to “covered transactions” as well as to certain other transactions and requires that all such transactions be on terms substantially the same, or at least as favorable, to the institution or subsidiary as those provided to a non-affiliate. The term “covered transaction” includes the making of loans to, purchase of assets from, and issuance of a guarantee to an affiliate, and other similar transactions. Section 23B transactions also include the provision of services and the sale of assets by a bank to an affiliate. In addition, loans or other extensions of credit by the financial institution to the affiliate are required to be collateralized in accordance with the requirements set forth in Section 23A of the Federal Reserve Act.

Sections 22(h) and (g) of the Federal Reserve Act place restrictions on loans to a bank’s insiders, i.e., executive officers, directors and principal shareholders. Under Section 22(h) of the Federal Reserve Act, loans to a director, an executive officer and to a greater than 10.0% shareholder of a financial institution, and certain affiliated interests of these, together with all other outstanding loans to such person and affiliated interests, may not exceed specified limits. Section 22(h) of the Federal Reserve Act also requires that loans to directors, executive officers and principal shareholders be made on terms and conditions substantially the same as offered in comparable transactions to persons who are not insiders and also requires prior board approval for certain loans. In addition, the aggregate amount of extensions of credit by a financial institution to insiders cannot exceed the institution’s unimpaired capital and surplus. Section 22(g) of the Federal Reserve Act places additional restrictions on loans to executive officers.

Enforcement. The Federal Deposit Insurance Corporation has extensive enforcement authority over insured state savings banks, including The Provident Bank. The enforcement authority includes, among other things, the ability to assess civil money penalties, issue cease and desist orders and remove directors and officers. In general, these enforcement actions may be initiated in response to violations of laws and regulations, breaches of fiduciary duty and unsafe or unsound practices. The Federal Deposit Insurance Corporation is required, with certain exceptions, to appoint a receiver or conservator for an insured state non-member bank if that bank was “critically undercapitalized” on average during the calendar quarter beginning 270 days after the date on which the institution became “critically undercapitalized.” The Federal Deposit Insurance Corporation may also appoint itself as conservator or receiver for an insured state non-member bank under specified circumstances, including: (1) insolvency; (2) substantial dissipation of assets or earnings through violations of law or unsafe or unsound practices; (3) existence of an unsafe or unsound condition to transact business; (4) insufficient capital; or (5) the incurrence of losses that will deplete substantially all of the institution’s capital with no reasonable prospect of replenishment without federal assistance.

Federal Insurance of Deposit Accounts. The Provident Bank is a member of the Deposit Insurance Fund, which is administered by the Federal Deposit Insurance Corporation. Deposit accounts in The Provident Bank are insured up to a maximum of \$250,000 for each separately insured depositor.

The Federal Deposit Insurance Corporation imposes an assessment for deposit insurance on all depository institutions. Under the Federal Deposit Insurance Corporation’s risk-based assessment system, insured institutions deemed less risky of failure pay lower assessments. Assessment rates (inclusive of possible adjustments) for most banks with less than \$10 billion of assets are based on a formula using financial data and supervisory ratings, and currently range from 1.5 to 30 basis points of each institution’s total assets less tangible capital.

The Federal Deposit Insurance Corporation has authority to increase insurance assessments. A significant increase in insurance premiums would likely have an adverse effect on the operating expenses and results of operations of The Provident Bank. Future insurance assessment rates cannot be predicted.

Insurance of deposits may be terminated by the Federal Deposit Insurance Corporation upon a finding that the 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 regulatory condition imposed in writing. We do not know of any practice, condition or violation that might lead to termination of deposit insurance.

Privacy Regulations. Federal Deposit Insurance Corporation regulations generally require that The Provident Bank disclose its privacy policy, including identifying with whom it shares a customer's "non-public personal information," to customers at the time of establishing the customer relationship and annually thereafter. In addition, The Provident Bank is required to provide its customers with the ability to "opt-out" of having their personal information shared with unaffiliated third parties and not to disclose account numbers or access codes to non-affiliated third parties for marketing purposes. The Provident Bank currently has a privacy protection policy in place and believes that such policy is in compliance with the regulations.

Community Reinvestment Act. Under the Community Reinvestment Act, or CRA, as implemented by Federal Deposit Insurance Corporation regulations, a non-member bank has a continuing and affirmative obligation, consistent with its safe and sound operation, to help meet the credit needs of its entire community, including low- and moderate-income neighborhoods. The CRA does not establish specific lending requirements or programs for financial institutions nor does it limit an institution's discretion to develop the types of products and services that it believes are best suited to its particular community, consistent with the CRA. The CRA does require the Federal Deposit Insurance Corporation, in connection with its examination of a non-member bank, to assess the institution's record of meeting the credit needs of its community and to take such record into account in its evaluation of certain applications by such institution, including applications to acquire branches and other financial institutions. The CRA requires the Federal Deposit Insurance Corporation to provide a written evaluation of an institution's CRA performance utilizing a four-tiered descriptive rating system. The Provident Bank's latest Federal Deposit Insurance Corporation CRA rating was "Satisfactory."

Massachusetts has its own statutory counterpart to the CRA which is also applicable to The Provident Bank. The Massachusetts version is generally similar to the CRA but utilizes a five-tiered descriptive rating system. Massachusetts law requires the Massachusetts Commissioner of Banks to consider, but not be limited to, a bank's record of performance under Massachusetts law in considering any application by the bank to establish a branch or other deposit-taking facility, to relocate an office or to merge or consolidate with or acquire the assets and assume the liabilities of any other banking institution. The Provident Bank's most recent rating under Massachusetts law was "Satisfactory."

Consumer Protection and Fair Lending Regulations. Massachusetts savings banks are subject to a variety of federal and Massachusetts statutes and regulations that are intended to protect consumers and prohibit discrimination in the granting of credit. These statutes and regulations provide for a range of sanctions for non-compliance with their terms, including imposition of administrative fines and remedial orders, and referral to the Attorney General for prosecution of a civil action for actual and punitive damages and injunctive relief. Certain of these statutes authorize private individual and class action lawsuits and the award of actual, statutory and punitive damages and attorneys' fees for certain types of violations.

USA PATRIOT Act. The Provident Bank is subject to the USA PATRIOT Act, which gave federal agencies additional powers to address terrorist threats through enhanced domestic security measures, expanded surveillance powers, increased information sharing, and broadened anti-money laundering requirements. By way of amendments to the Bank Secrecy Act, Title III of the USA PATRIOT Act provided measures intended to encourage information sharing among bank regulatory agencies and law enforcement bodies. Further, certain provisions of Title III impose affirmative obligations on a broad range of financial institutions, including banks, thrifts, brokers, dealers, credit unions, money transfer agents, and parties registered under the Commodity Exchange Act.

Other Regulations

Interest and other charges collected or contracted for by The Provident Bank are subject to state usury laws and federal laws concerning interest rates. Loan operations are also subject to state and federal laws applicable to credit transactions, such as the:

- Home Mortgage Disclosure Act of 1975, requiring financial institutions to provide information to enable the public and public officials to determine whether a financial institution is fulfilling its obligation to help meet the housing needs of the community it serves;
- Equal Credit Opportunity Act, prohibiting discrimination on the basis of race, creed or other prohibited factors in extending credit;
- Fair Credit Reporting Act of 1978, governing the use and provision of information to credit reporting agencies;
- Massachusetts Debt Collection Regulations, establishing standards, by defining unfair or deceptive acts or practices, for the collection of debts from persons within the Commonwealth of Massachusetts and the General Laws of Massachusetts, Chapter 167E, which governs The Provident Bank's lending powers; and

- Rules and regulations of the various federal and state agencies charged with the responsibility of implementing such federal and state laws.

The deposit operations of The Provident Bank also are subject to, among others, the:

- Right to Financial Privacy Act, which imposes a duty to maintain confidentiality of consumer financial records and prescribes procedures for complying with administrative subpoenas of financial records;
- Check Clearing for the 21st Century Act (also known as “Check 21”), which gives “substitute checks,” such as digital check images and copies made from that image, the same legal standing as the original paper check;
- Electronic Funds Transfer Act and Regulation E promulgated thereunder, which govern automatic deposits to and withdrawals from deposit accounts and customers’ rights and liabilities arising from the use of automated teller machines and other electronic banking services; and
- General Laws of Massachusetts, Chapter 167D, which governs deposit powers.

Federal Home Loan Bank System

The Provident Bank is a member of the Federal Home Loan Bank System, which consists of 11 regional Federal Home Loan Banks. The Federal Home Loan Bank provides a central credit facility primarily for member institutions. Members of the Federal Home Loan Bank are required to acquire and hold shares of capital stock in the Federal Home Loan Bank. The Provident Bank was in compliance with this requirement at December 31, 2021. Based on redemption provisions of the Federal Home Loan Bank of Boston, the stock has no quoted market value and is carried at cost. The Provident Bank reviews for impairment based on the ultimate recoverability of the cost basis of the Federal Home Loan Bank of Boston stock. As of December 31, 2021, no impairment has been recognized.

At its discretion, the Federal Home Loan Bank of Boston may declare dividends on their stock. The Federal Home Loan Banks are required to provide funds for certain purposes including, for example, contributing funds for affordable housing programs. These requirements could reduce the amount of dividends that the Federal Home Loan Banks pay to their members and result in the Federal Home Loan Banks imposing a higher rate of interest on advances to their members. In 2021, the Federal Home Loan Bank of Boston paid dividends equal to an annual yield of 1.69%. There can be no assurance that such dividends will continue in the future.

Holding Company Regulation

Provident Bancorp, Inc. is subject to examination, regulation, and periodic reporting under the Bank Holding Company Act of 1956, as amended, as administered by the Federal Reserve Board. Provident Bancorp, Inc. is required to obtain the prior approval of the Federal Reserve Board to acquire all, or substantially all, of the assets of any bank or bank holding company. Prior Federal Reserve Board approval would be required for Provident Bancorp, Inc. to acquire direct or indirect ownership or control of any voting securities of any bank or bank holding company if, after such acquisition, it would, directly or indirectly, own or control more than 5% of any class of voting shares of the bank or bank holding company. In addition to the approval of the Federal Reserve Board, prior approval may also be necessary from other agencies having supervisory jurisdiction over the bank to be acquired before any bank acquisition can be completed.

A bank holding company is generally prohibited from engaging in non-banking activities, or acquiring direct or indirect control of more than 5% of the voting securities of any company engaged in non-banking activities. One of the principal exceptions to this prohibition is for activities found by the Federal Reserve Board to be so closely related to banking or managing or controlling banks as to be a proper incident thereto. Some of the principal activities that the Federal Reserve Board has determined by regulation to be so closely related to banking are: (i) making or servicing loans; (ii) performing certain data processing services; (iii) providing discount brokerage services; (iv) acting as fiduciary, investment or financial advisor; (v) leasing personal or real property; (vi) making investments in corporations or projects designed primarily to promote community welfare; and (vii) acquiring a savings and loan association whose direct and indirect activities are limited to those permitted for bank holding companies.

The Gramm-Leach-Bliley Act of 1999 authorized a bank holding company that meets specified conditions, including being “well capitalized” and “well managed,” to opt to become a “financial holding company” and thereby engage in a broader array of financial activities than previously permitted. Such activities can include insurance underwriting and investment banking. We have not opted into financial holding company status.

A bank holding company is generally required to give the Federal Reserve Board prior written notice of any purchase or redemption of then outstanding equity securities if the gross consideration for the purchase or redemption, when combined with the net consideration paid for all such purchases or redemptions during the preceding 12 months, is equal to 10% or more of the company’s consolidated net worth. The Federal Reserve Board may disapprove such a purchase or redemption if it determines that the proposal would constitute an unsafe and unsound practice, or would violate any law, regulation, Federal Reserve Board order or directive, or any condition imposed by, or written agreement with, the Federal Reserve Board. There is an exception to this approval requirement for well-capitalized bank holding companies that meet certain other conditions.

The Federal Reserve Board has issued a policy statement regarding capital distributions, including dividends, by bank holding companies. In general, the Federal Reserve Board's policies provide that dividends should be paid only out of current earnings and only if the prospective rate of earnings retention by the bank holding company appears consistent with the organization's capital needs, asset quality and overall financial condition. The Federal Reserve Board's policies also require that a bank holding company serve as a source of financial strength to its subsidiary banks by standing ready to use available resources to provide adequate capital funds to those banks during periods of financial stress or adversity and by maintaining the financial flexibility and capital-raising capacity to obtain additional resources for assisting its subsidiary banks where necessary. The Dodd-Frank Act codified the source of strength doctrine. Under the prompt corrective action laws, the ability of a bank holding company to pay dividends may be restricted if a subsidiary bank becomes undercapitalized. In addition, the Federal Reserve Board has issued guidance that requires consultation with the agency prior to a bank holding company's payment of dividends or repurchase of stock under certain circumstances. These regulatory policies could affect the ability of Provident Bancorp, Inc. to pay dividends, repurchase its stock or otherwise engage in capital distributions.

Under the Federal Deposit Insurance Act, depository institutions are liable to the Federal Deposit Insurance Corporation for losses suffered or anticipated by the Federal Deposit Insurance Corporation in connection with the default of a commonly controlled depository institution or any assistance provided by the Federal Deposit Insurance Corporation to such an institution in danger of default.

The status of Provident Bancorp, Inc. as a registered bank holding company under the Bank Holding Company Act will not exempt it from certain federal and state laws and regulations applicable to corporations generally, including, without limitation, certain provisions of the federal securities laws.

Massachusetts Holding Company Regulation. Under the Massachusetts banking laws, a company owning or controlling two or more banking institutions, including a savings bank, is regulated as a bank holding company. The term "company" is defined by the Massachusetts banking laws similarly to the definition of "company" under the Bank Holding Company Act. Each Massachusetts bank holding company: (i) must obtain the approval of the Massachusetts Board of Bank Incorporation before engaging in certain transactions, such as the acquisition of more than 5% of the voting stock of another banking institution; (ii) must register, and file reports, with the Massachusetts Commissioner of Banks; and (iii) is subject to examination by the Massachusetts Commissioner of Banks. Provident Bancorp, Inc. is not a "bank holding company" under the Massachusetts banking laws.

Federal Securities Laws

Provident Bancorp, Inc.'s common stock is registered with the Securities and Exchange Commission. Provident Bancorp, Inc. is subject to the information, proxy solicitation, insider trading restrictions and other requirements under the Securities Exchange Act of 1934.

Acquisition of the Company

Under the Change in Bank Control Act, no person, or group of persons acting in concert, may acquire control of a bank holding company such as New Provident unless the Federal Reserve Board has been given 60 days' prior written notice and not disapproved the proposed acquisition. The Federal Reserve Board considers several factors in evaluating a notice, including the financial and managerial resources of the acquirer and competitive effects. Control, as defined under the Change in Bank Control Act and applicable regulations, means the power, directly or indirectly, to direct the management or policies of the company or to vote 25% or more of any class of voting securities of the company. Acquisition of more than 10% of any class of a bank holding company's voting securities constitutes a rebuttable presumption of control under certain circumstances, including where, as will be the case with Provident Bancorp, Inc., the issuer has registered securities under Section 12 of the Securities Exchange Act of 1934.

In addition, federal regulations provide that no company may acquire control of a bank holding-company without the prior approval of the Federal Reserve Board. Control, as defined under the Bank Holding Company Act and Federal Reserve Board regulations, means ownership, control or power to vote 25% or more of any class of voting stock, control in any manner over the election of a majority of the company's directors, or a determination by the regulator that the acquiror has the power to exercise, directly or indirectly, a controlling influence over the management or policies of the company. Any company that acquires such control becomes a "bank holding company" subject to registration, examination and regulation by the Federal Reserve Board. Effective September 30, 2020, the Federal Reserve Board amended its regulations concerning when a company exercises a controlling influence over a bank or bank holding company for purposes of the Bank Holding Company Act. Relevant factors include the company's voting and nonvoting equity investment in the bank or bank holding company, director, officer and employee overlap and the scope of business relationships between the company and bank or bank holding company.

ITEM 1A. RISK FACTORS

Not required for a smaller reporting company.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

At December 31, 2021, we conducted business through our main office and six branch offices located in Amesbury and Newburyport, Massachusetts and Bedford, Exeter, Portsmouth and Seabrook, New Hampshire, as well as two loan production offices located in Boston, Massachusetts and Ponte Vedra, Florida. We own five of our offices, including our main office, and lease two of our branch offices as well as two loan production offices. At December 31, 2021, the total net book value of our land, buildings, furniture, fixtures, equipment and lease right-of-use assets was \$18.4 million.

ITEM 3. LEGAL PROCEEDINGS

None.

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

(a) Market, Holder and Dividend Information. Our common stock is traded on the NASDAQ Capital Market under the symbol "PVBC." The approximate number of holders of record of Provident Bancorp Inc.'s common stock as of March 16, 2022 was 734. Certain shares of Provident Bancorp Inc. are held in "nominee" or "street" name and, accordingly, the number of beneficial owners of such shares is not known or included in the foregoing number.

(b) Sales of Unregistered Securities. Not applicable.

(c) Use of Proceeds. Not applicable.

(e) Stock Repurchases. On March 12, 2021, the Company announced that its Board of Directors had adopted a stock repurchase program under which it would repurchase up to 1,400,000 shares of its common stock, or approximately 7.5% of the then-outstanding shares. The repurchase program has no expiration date. The Company's repurchases of common stock for the fourth quarter of 2021, under the repurchase program is as follows:

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs
October 1, 2021 - October 31, 2021	13,328	\$ 16.20	13,328	434,955
November 1, 2021 - November 30, 2021	15,468	\$ 19.90	—	434,955
December 1, 2021 - December 31, 2021	16,633	\$ 18.30	—	434,955
Total	<u>45,429</u>	\$ 18.23	<u>13,328</u>	

ITEM 6. RESERVED

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

This discussion and analysis reflects our consolidated financial statements and other relevant statistical data, and is intended to enhance your understanding of our financial condition and results of operations. You should read the information in this section in conjunction with the business and financial information regarding Provident Bancorp, Inc., including the financial statements, provided in this Annual Report.

COVID-19

Since the distribution of COVID-19 vaccinations began in December 2020, significant progress has been made to combat the spread of the virus and as a result, there has been an uptick in economic activity, particularly those industries that had been most heavily impacted by the economic downturn caused by the COVID-19 pandemic. Despite the progress, COVID-19 has caused significant disruption in the U.S. economy and has adversely impacted a broad range of industries in which the Company's customers operate, which could impair their ability to fulfill their financial obligations. While it is not possible to know the full extent of these impacts as of the date of this filing, detailed below are potentially material items of which we are aware.

Congress, the President, and the Board of Governors of the Federal Reserve System (the "Federal Reserve") have taken several actions designed to cushion the economic fallout. Most notably, the Coronavirus Aid, Relief and Economic Security Act (the "CARES Act"), a \$2 trillion legislative package, was signed into law at the end of March 2020. The goal of the CARES Act was to prevent a severe economic downturn through various measures, including direct financial aid to American families and economic stimulus to significantly impacted industry sectors. Section 4013 of the CARES Act, "Temporary Relief from Troubled Debt Restructurings," provides banks the option to temporarily suspend certain requirements under U.S. GAAP related to troubled debt restructurings ("TDR") for a limited period of time to account for the effects of COVID-19. Additionally, the Economic Aid to Hard-Hit Small Businesses, Nonprofits, and Venues Act (the "Economic Aid Act") was enacted on December 27, 2020, providing for a second round of Paycheck Protection Program ("PPP") loans. Also on December 27, 2020, the Consolidated Appropriations Act ("CAA") was signed into law. Section 541 of the CAA extends the provision in Section 4013 of the CARES Act, "Temporary Relief from Troubled Debt Restructurings", to

January 1, 2022. The Federal Reserve also took actions to mitigate the economic impact of the COVID-19 pandemic, including cutting the federal funds rate 150 basis points and targeting a 0 to 25 basis point rate. However, in response to inflationary pressures, the Federal Reserve has announced that it will begin to taper its purchase of mortgage and other bonds and has signaled it will look to begin raising the federal funds rate in 2022. In addition to the general impact of the COVID-19 pandemic, certain provisions of the CARES Act as well as other legislative and regulatory relief efforts are expected to have a material impact on the Company's operations.

The Economic Aid Act amended the PPP by extending the authority of the Small Business Administration ("SBA") to guarantee loans and the ability of PPP lenders to disburse PPP loans until March 31, 2021. The PPP Extension Act of 2021, which was enacted on March 30, 2021, extended the PPP application deadline to May 31, 2021, and provided the SBA additional time to process applications through June 30, 2021.

Financial position and results of operations

In keeping with the guidance from regulators, during the height of the pandemic, the Company worked with COVID-19 affected customers to waive fees from a variety of sources and worked with affected borrowers to defer payments, interest and fees. The Company continues to monitor and measure the impact and potential future impact on operations.

Allowance for loan losses

Continued uncertainty regarding the severity and duration of the COVID-19 pandemic and related economic effects will continue to affect the accounting for credit losses, which could cause the provision for loan losses to increase. It also is possible that asset quality could worsen and expenses associated with collection efforts and loan charge-offs could increase. The Company participated in both rounds of the PPP, providing loans to small businesses negatively impacted by the COVID-19 pandemic. PPP loans are fully guaranteed by the U.S. government; if that should change, the Company could be required to increase its allowance for loan losses through an additional provision for loan losses charged to earnings.

In accordance with guidance issued by federal banking agencies, the Company worked with borrowers that were unable to meet contractual obligations due to the effects of COVID-19 by providing modifications to allow for deferral of interest or principal and interest payments on a case-by-case basis. In order to mitigate the risk associated with these modifications the Company incorporated covenants that require borrowers to submit quarterly financial statements, prohibit them from distributing funds to any owner or stockholder (with the exception of payroll) and also prohibit them from making any payments on debt owed to subordinated debt holders for the duration of their modification. If borrowers are unable to return to their normal payment plan following their modification period, the Company could be required to increase its allowance for loan losses through an additional provision for loan losses charged to earnings.

Valuation

Valuation and fair value measurement challenges may occur. For example, COVID-19 could cause further and sustained decline in the financial markets or the occurrence of what management would deem a valuation triggering event that could result in an impairment charge to earnings, such as our investment securities.

Critical Accounting Policies

A summary of our accounting policies is described in Note 2 to the Consolidated Financial Statements included in this annual report. Critical accounting estimates are necessary in the application of certain accounting policies and procedures and are particularly susceptible to significant change. Critical accounting policies are defined as those involving significant judgments and assumptions by management that are inherently uncertain and that could have a material impact on the carrying value of certain assets or on income under different assumptions or conditions. Management believes that the most critical accounting policies, which involve the most complex or subjective decisions or assessments, are as follows:

Allowance for Loan Losses.

The allowance for loan losses is a valuation allowance for probable incurred credit losses. Loan losses are charged against the allowance when management believes the un-collectability of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance. Management estimates the allowance balance required using past loan loss experience, the size and composition of the portfolio, information about specific borrower situations and estimated collateral values, economic conditions, and other factors. Allocations of the allowance may be made for specific loans, but the entire allowance is available for any loan that, in management's judgment, should be charged off.

The allowance consists of specific and general components. The specific component relates to loans that are individually classified as impaired when, based on current information and events, it is probable that the Company will be unable to collect all amounts due

according to the contractual terms of the loan agreement. Loans for which the terms have been modified resulting in a concession, and for which the borrower is experiencing financial difficulties, are considered troubled debt restructurings (“TDRs”) and are classified as impaired.

The Company classifies a loan as impaired when, based on current information and events, it is probable that it will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower’s prior payment record, and the amount of the shortfall in relation to the principal and interest owed.

Large groups of smaller balance homogeneous loans are collectively evaluated for impairment. Accordingly, we do not separately identify individual consumer and residential loans for impairment disclosures.

The allocated component relates to loans that are classified as impaired. Impairment is measured on a loan by loan basis for commercial, commercial real estate and construction loans by either the present value of expected future cash flows discounted at the loan’s effective interest rate or the fair value of the collateral if the loan is collateral dependent. An allowance is established when the discounted cash flows (or collateral value) of the impaired loan is lower than the carrying value of that loan.

Troubled debt restructurings are individually evaluated for impairment and included in the separately identified impairment disclosures. TDRs are measured at the present value of estimated future cash flows using the loan’s effective rate at inception. If a TDR is considered to be a collateral dependent loan, the loan is reported, net, at the fair value of the collateral. For TDRs that subsequently default, the Company determines the amount of the allowance on that loan in accordance with the accounting policy for the allowance for loan losses on loans individually identified as impaired.

Mortgage warehouse loans are facility lines to non-bank mortgage origination companies for sale into secondary markets, which is typically within 15 days of loan closure. Due to their short-term nature, these loans are assessed at a lower credit risk and do not carry the same allocation as traditional loans.

The general component of the allowance for loan losses is based on historical loss experience adjusted for qualitative factors stratified by all loan segments. Management uses a rolling average of historical losses based on a time frame appropriate to capture relevant loss data for each loan segment. The historical loss factors are adjusted for the following qualitative factors: levels/trends in delinquencies and non-accruals, economic conditions, portfolio trends, portfolio concentrations, loan grading and management’s discretion. The determination of qualitative factors involves significant judgment. There were no changes in our policies or methodology pertaining to the general component of the allowance for loan losses during 2021.

The qualitative factors are determined based on the various risk characteristics of each loan segment. Risk characteristics relevant to each portfolio segment are as follows:

Residential real estate: We generally do not originate loans with a loan-to-value ratio greater than 80% and do not grant subprime loans. Loans with loan to value ratios greater than 80% require the purchase of private mortgage insurance. All loans in this segment are collateralized by owner-occupied residential real estate and repayment is dependent on the credit quality of the individual borrower. The overall health of the economy, including unemployment rates and housing prices, will have an effect on the credit quality in this segment.

Commercial real estate: Loans in this segment are primarily income-producing properties throughout Massachusetts and New Hampshire. The underlying cash flows generated by the properties are adversely impacted by a downturn in the economy as evidenced by increased vacancy rates, which in turn, will have an effect on the credit quality in this segment. Management periodically obtains rent rolls and continually monitors the cash flows of these loans.

Construction and land development: Loans in this segment primarily include speculative and pre-sold real estate development loans for which payment is derived from sale of the property and a conversion of the construction loans to permanent loans for which payment is then derived from cash flows of the property. Credit risk is affected by cost overruns, time to sell at an adequate price, and market conditions.

Mortgage warehouse: Loans in this segment are primarily facility lines to non-bank mortgage origination companies. The underlying collateral of these loans are residential real estate loans. Loans are originated by the mortgage companies for sale into secondary markets, which is typically within 15 days of the loan closure. The primary source of repayment is the cash flow upon the sale of the loans. The credit risk associated with this type of lending is the risk that the mortgage companies are unable to sell the loans.

Commercial: Loans in this segment are made to businesses and are generally secured by assets of the business. Repayment is expected from the cash flows of the business. A weakened economy, and resultant decreased consumer spending, will have an effect on the credit quality in this segment.

Consumer: Loans in this segment are generally unsecured and repayment is dependent on the credit quality of the individual borrower.

An unallocated component can be maintained to cover uncertainties that could affect management's estimate of probable losses. The unallocated component of the allowance reflects the margin of imprecision and uncertainty inherent in the underlying assumptions used in the methodologies for estimating allocated and general reserves in the portfolio.

Income Taxes. The Company recognizes income taxes under the asset and liability method. Under this method, deferred tax assets and liabilities are established for the temporary differences between the accounting basis and the tax basis of the Company's assets and liabilities at enacted tax rates expected to be in effect when the amounts related to such temporary differences are realized or settled. A tax valuation allowance is established, as needed, to reduce net 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. The Company recognizes interest and/or penalties related to income tax matters in income tax expense.

The following tables set forth selected consolidated historical financial and other data of Provident Bancorp, Inc. for the years ended and at the dates indicated. The following is only a summary and you should read it in conjunction with the business and financial information regarding Provident Bancorp, Inc. contained elsewhere in this Annual Report. The information at December 31, 2021 and 2020, and for the years ended December 31, 2021 and 2020, is derived in part from the audited consolidated financial statements that appear in this Annual Report.

	At December 31,				
	2021	2020	2019	2018	2017
Financial Condition Data:			(In thousands)		
Total assets	\$ 1,729,283	\$ 1,505,781	\$ 1,121,788	\$ 974,079	\$ 902,265
Cash and cash equivalents	153,115	83,819	59,658	28,613	47,689
Debt securities available-for-sale (at fair value)	36,837	32,215	41,790	51,403	61,429
Federal Home Loan Bank stock, at cost	785	895	1,416	2,650	1,854
Loans held for sale	22,846	—	—	—	—
Loans receivable, net (1)	1,433,803	1,314,810	959,286	835,528	742,138
Bank-owned life insurance	42,569	36,684	26,925	26,226	25,540
Deposits	1,459,895	1,237,428	849,905	768,096	750,057
Borrowings	13,500	13,500	24,998	68,022	26,841
Total shareholders' equity (2)	233,782	235,856	230,933	125,584	115,777

	For the Year Ended December 31,				
	2021	2020	2019	2018	2017
Operating Data:	(In thousands, except per share data)				
Interest and dividend income	\$ 64,803	\$ 60,403	\$ 51,538	\$ 42,340	\$ 35,782
Interest expense	3,370	5,931	8,148	5,213	3,726
Net interest and dividend income	61,433	54,472	43,390	37,127	32,056
Provision for loan losses	3,887	5,597	5,326	3,329	2,929
Net interest and dividend income after provision for loan losses	57,546	48,875	38,064	33,798	29,127
Gains on sales of securities, net	—	—	113	—	5,912
Other noninterest income	5,166	3,543	3,998	4,178	4,043
Write down of other assets and receivables	225	2,207	—	—	—
Noninterest expense	40,394	33,601	27,556	25,414	23,749
Income before income taxes	22,093	16,610	14,619	12,562	15,333
Income tax expense (3)	5,954	4,625	3,811	3,237	7,418
Net income	<u>\$ 16,139</u>	<u>\$ 11,985</u>	<u>\$ 10,808</u>	<u>\$ 9,325</u>	<u>\$ 7,915</u>
Earnings per common share: (4)					
Basic	\$ 0.96	\$ 0.66	\$ 0.60	\$ 0.50	0.43
Diluted	\$ 0.93	\$ 0.66	\$ 0.60	\$ 0.50	0.43

(1) Excludes loans held-for-sale.

(2) Includes retained earnings and accumulated other comprehensive income/loss.

(3) Includes the expense related to the Tax Cuts and Jobs Act in 2017 of \$2.0 million

(4) Share amounts related to periods prior to the date of the Conversion (October 16, 2019) have been restated to give the retroactive recognition to the exchange ratio applied in the Conversion (2.0212-to-one)

	At or For the Year Ended December 31,				
	2021	2020	2019	2018	2017
Performance Ratios:					
Return on average assets	1.02%	0.89%	1.04%	1.03%	0.91%
Return on average equity	6.86%	5.05%	7.38%	7.75%	6.84%
Interest rate spread (1)	3.89%	3.93%	4.05%	4.05%	3.71%
Net interest margin (2)	4.06%	4.23%	4.44%	4.33%	3.90%
Efficiency ratio (3)	60.99%	61.72%	58.15%	61.53%	65.79%
Dividend payout ratio	15.86%	13.65%	—%	—%	—%
Average interest-earning assets to average interest-bearing liabilities	176.80%	165.71%	146.87%	146.01%	142.10%
Average equity to average assets	14.82%	17.58%	14.08%	13.26%	13.32%
Regulatory Capital Ratios:					
Total capital to risk weighted assets (bank only)	14.18%	14.60%	17.62%	14.55%	14.96%
Tier 1 capital to risk weighted assets (bank only)	12.93%	13.35%	16.37%	13.30%	13.71%
Tier 1 capital to average assets (bank only)	12.07%	12.37%	15.18%	12.69%	11.80%
Common equity tier 1 capital (bank only)	12.93%	13.35%	16.37%	13.30%	13.71%
Total capital to total assets (company)	13.52%	15.66%	20.59%	12.89%	12.83%
Asset Quality Ratios:					
Allowance for loan losses as a percentage of total loans (4)	1.34%	1.39%	1.42%	1.38%	1.30%
Allowance for loan losses as a percentage of non-performing loans	674.14%	341.72%	237.58%	186.55%	108.02%
Net charge-offs to average outstanding loans during the year	0.22%	0.08%	0.35%	0.18%	0.25%
Non-performing loans as a percentage of total loans (4)	0.20%	0.41%	0.60%	0.74%	1.20%
Non-performing loans as a percentage of total assets	0.17%	0.36%	0.52%	0.64%	1.00%
Total non-performing assets as a percentage of total assets	0.17%	0.36%	0.52%	0.81%	1.00%
Other:					
Number of offices	7	7	7	8	8
Number of full-time equivalent employees	175	158	139	123	126

(1) Represents the difference between the weighted average yield on average interest-earning assets and the weighted average cost of interest-bearing liabilities.

(2) Represents net interest income as a percent of average interest-earning assets.

(3) Represents noninterest expense divided by the sum of net interest income and noninterest income, excluding gains on securities available-for-sale, net.

(4) Loans are presented before the allowance but include deferred costs/fees.

Comparison of Financial Condition at December 31, 2021 and December 31, 2020

Assets. Our total assets increased \$223.5 million, or 14.8%, to \$1.73 billion at December 31, 2021 from \$1.51 billion at December 31, 2020. The primary reasons for the increase were increases in net loans, cash and cash equivalents, debt securities available-for-sale, and bank owned life insurance.

Cash and Cash Equivalents. Cash and cash equivalents increased \$69.3 million, or 82.7%, to \$153.1 million at December 31, 2021 from \$83.8 million at December 31, 2020. The increase was primarily related to an increase in short-term investments of \$58.7 million, or 81.5%. Short-term investments were increased as a result of an increase in deposits that exceeded loan growth.

Debt Securities Available-for-Sale. Investments in debt securities available-for-sale increased \$4.6 million or 14.3% to \$36.8 million at December 31, 2021 from \$32.2 million at December 31, 2020. The increase resulted primarily from purchases of debt securities, partially offset by principal pay downs on government mortgage-backed securities.

Bank Owned Life Insurance. Bank owned life insurance increased \$5.9 million, or 16.0%, to \$42.6 million at December 31, 2021 from \$36.7 million at December 31, 2020. The increase was primarily due to the purchase of additional insurance policies.

Loan Portfolio Analysis. At December 31, 2021, net loans were \$1.43 billion, or 82.9% of total assets, compared to \$1.31 billion, or 87.3% of total assets, at December 31, 2020. Increases in commercial loans of \$160.3 million, or 28.3%, and an increase in construction and land development loans of \$13.9 million, or 48.0% were partially offset by decreases in commercial real estate loans of \$6.7 million, or 1.5%, residential real estate loans of \$32.0 million, or 97.5%, consumer loans of \$4.0 million, or 72.6%, and mortgage warehouse of \$11.6 million, or 4.4%. Our commercial loan growth was primarily due to an increase in our loans to digital asset companies of \$105.4 million, or 703.1% to \$120.4 million compared to \$15.0 million at December 31, 2020, an increase in enterprise value loans of \$54.2 million, or 18.9%, to \$340.3 million compared to \$286.1 million at December 31, 2020, and an increase in renewable energy loans of \$25.1 million, or 67.7%, to \$62.3 million compared to \$37.2 million at December 31, 2020. The increase was partially offset by a decrease in PPP loans of \$29.4 million, or 70.2%, to \$12.4 million compared to \$41.8 million as of December 31, 2020. Residential real estate loans decreased primarily due to the transfer of the portfolio to loans held for sale. As of December 31, 2021, the Company determined they will no longer originate or service residential real estate loans. As such, the Company valued the portfolio at the lower of cost or market and transferred them to loans held for sale.

The following table sets forth the composition of our loan portfolio by type of loan at the dates indicated, excluding loans held for sale.

(Dollars in thousands)	At December 31,									
	2021		2020		2019		2018		2017	
	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percent
Real estate:										
Residential (1)	\$ 812	0.06 %	\$ 32,785	2.46 %	\$ 45,695	4.69 %	\$ 57,361	6.76 %	\$ 67,724	9.00 %
Commercial (2)	432,275	29.66	438,949	32.82	418,356	42.89	364,867	43.00	371,510	49.35
Construction and land development	42,800	2.94	28,927	2.16	46,763	4.79	44,606	5.26	55,828	7.42
Commercial (3)	726,241	49.83	565,976	42.31	451,791	46.32	361,782	42.64	240,223	31.91
Consumer	1,519	0.10	5,547	0.41	12,737	1.31	19,815	2.34	17,455	2.32
Mortgage warehouse	253,764	17.41	265,379	19.84	—	—	—	—	—	—
Total loans	1,457,411	100.00 %	1,337,563	%	975,342	100.00 %	848,431	100.00 %	752,740	100.00 %
Deferred loan fees, net	(4,112)		(4,235)		(2,212)		(1,223)		(845)	
Allowance for loan losses	(19,496)		(18,518)		(13,844)		(11,680)		(9,757)	
Loans, net	<u>\$1,433,803</u>		<u>\$1,314,810</u>		<u>\$959,286</u>		<u>\$835,528</u>		<u>\$742,138</u>	

- (1) Includes home equity loans and lines of credit
- (2) Includes multi-family real estate loans
- (3) Includes PPP and digital asset loans

Loan Maturity. The following table sets forth certain information at December 31, 2021 regarding the contractual maturity of our loan portfolio. Demand loans, loans having no stated repayment schedule or maturity, and overdraft loans are reported as being due in one year or less. The table does not include any estimate of prepayments that could significantly shorten the average life of all loans and may cause our actual repayment experience to differ from that shown below.

<i>(In thousands)</i>	Residential Real Estate	Commercial Real Estate	Construction and Land Development	Commercial	Consumer	Mortgage Warehouse	Total Loans
Amounts due in:							
One year or less	\$ —	\$ 30,004	\$ 6,364	\$ 95,897	\$ 515	\$ 253,764	\$ 386,544
More than one year to five years	—	27,698	1,595	275,472	1,004	—	305,769
More than five years through 15 years	647	123,169	3,447	331,200	—	—	458,463
More than 15 years	165	251,404	31,394	23,672	—	—	306,635
Total	<u>\$ 812</u>	<u>\$ 432,275</u>	<u>\$ 42,800</u>	<u>\$ 726,241</u>	<u>\$ 1,519</u>	<u>\$ 253,764</u>	<u>\$ 1,457,411</u>

The following table sets forth our fixed and adjustable-rate loans at December 31, 2021 that are contractually due after December 31, 2022.

<i>(In thousands)</i>	Fixed Rates	Floating or Adjustable Rates	Total Due After December 31, 2022
Real estate:			
Residential	\$ 411	\$ 401	\$ 812
Commercial	41,307	360,964	402,271
Construction and land development	5,082	31,354	36,436
Commercial	456,529	173,815	630,344
Consumer	1,004	—	1,004
Mortgage warehouse	—	—	—
Total loans	<u>\$ 504,333</u>	<u>\$ 566,534</u>	<u>\$ 1,070,867</u>

Asset Quality

Credit Risk Management. Our strategy for credit risk management focuses on having well-defined credit policies and uniform underwriting criteria and providing prompt attention to potential problem loans. Management of asset quality is accomplished by internal controls, monitoring and reporting of key risk indicators, and both internal and independent third-party loan reviews. The primary objective of our loan review process is to measure borrower performance and assess risk for the purpose of identifying loan weakness in order to minimize loan loss exposure. From the time of loan origination through final repayment, commercial real estate, construction and land development and commercial business loans are assigned a risk rating based on pre-determined criteria and levels of risk. The risk rating is monitored annually for most loans; however, it may change during the life of the loan as appropriate.

When entering a new lending line, we typically seek to manage risks and costs by limiting initial activity. We then decide whether it would be profitable and consistent with our risk tolerance levels to expand the activity, and continually calibrate and adjust our actions to maintain appropriate risk limitations. We typically enter a new lending line based upon the experience of our existing employees, or we may hire an experienced individual or group of individuals to manage new activities.

Internal and independent third-party loan reviews vary by loan type. Depending on the size and complexity of the loan, some loans may warrant detailed individual review, while other loans may have less risk based upon size, or be of a homogeneous nature reducing the need for detailed individual analysis. Assets with these characteristics, such as consumer loans and loans secured by residential real estate, may be reviewed on the basis of risk indicators such as delinquency or credit rating. In cases of significant concern, a total re-evaluation of the loan and associated risks are documented by completing a loan risk assessment and action plan. Some loans may be re-evaluated in terms of their fair market value or net realizable value in order to determine the likelihood of potential loss exposure and, consequently, the adequacy of specific and general loan loss reserves.

When a borrower fails to make a required loan payment, we take a number of steps to have the borrower cure the delinquency and restore the loan to current status, including contacting the borrower by letter and phone at regular intervals. When the borrower is in default, we may commence collection proceedings. If a foreclosure action is instituted and the loan is not brought current, paid in full, or refinanced before the foreclosure sale, the real property securing the loan generally is sold at foreclosure. Management informs the board of directors monthly of the amount of loans delinquent more than 30 days. Management provides detailed information to the board of directors quarterly on loans 60 or more days past due and all loans in foreclosure and repossessed property that we own.

Delinquent Loans. The following tables set forth our loan delinquencies by type and amount at the dates indicated.

	At December 31,								
	2021			2020			2019		
	30-59 Days Past Due	60-89 Days Past Due	90 Days or more Past Due	30-59 Days Past Due	60-89 Days Past Due	90 Days or more Past Due	30-59 Days Past Due	60-89 Days Past Due	90 Days or more Past Due
	(In thousands)								
Real Estate:									
Residential	\$ —	\$ —	\$ 555	\$ 255	\$ 346	\$ 1,030	\$ 715	\$ 154	\$ 832
Commercial	—	—	—	—	—	—	473	18,256	1,368
Construction and land development	—	—	—	—	—	—	—	—	165
Commercial	13	111	1,860	4,358	—	291	529	85	484
Consumer	15	11	—	61	21	64	111	58	38
Mortgage warehouse	—	—	—	—	—	—	—	—	—
Total	\$ 28	\$ 122	\$ 2,415	\$ 4,674	\$ 367	\$ 1,385	\$ 1,828	\$ 18,553	\$ 2,887

	At December 31,					
	2018			2017		
	30-59 Days Past Due	60-89 Days Past Due	90 Days or more Past Due	30-59 Days Past Due	60-89 Days Past Due	90 Days or more Past Due
	(In thousands)					
Real Estate:						
Residential	\$ 321	\$ 223	\$ 30	\$ 699	\$ 178	\$ 81
Commercial	742	—	519	—	3,669	—
Construction and land development	—	—	—	—	—	—
Commercial	40	—	3,167	12	—	—
Consumer	62	46	59	63	45	60
Mortgage warehouse	—	—	—	—	—	—
Total	\$ 1,165	\$ 269	\$ 3,775	\$ 774	\$ 3,892	\$ 141

Non-performing Assets. Non-performing assets include loans that are 90 or more days past due or on non-accrual status, including troubled debt restructurings on non-accrual status, and real estate and other loan collateral acquired through foreclosure and repossession. Troubled debt restructurings include loans for which either a portion of interest or principal has been forgiven, loans modified at interest rates materially less than current market rates, or the borrower is experiencing financial difficulty. Loans 90 days or greater past due may remain on an accrual basis if adequately collateralized and in the process of collection. At December 31, 2021, we did not have any accruing loans past due 90 days or greater. For non-accrual loans, interest previously accrued but not collected is reversed and charged against income at the time a loan is placed on non-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.

Real estate that we acquire as a result of foreclosure or by deed-in-lieu of foreclosure is classified as foreclosed real estate until it is sold. When property is acquired, it is initially recorded at the lower of cost or fair value less costs to sell at the date of foreclosure. Holding costs and declines in fair value after acquisition of the property result in charges against income.

The following table sets forth information regarding our non-performing assets at the dates indicated.

<i>(Dollars in thousands)</i>	At December 31,				
	2021	2020	2019	2018	2017
Non-accrual loans:					
Real estate:					
Residential	\$ 812	\$ 1,156	\$ 969	\$ 850	\$ 364
Commercial	—	—	1,701	519	7,102
Construction and land development	—	—	165	—	—
Commercial	2,080	4,198	2,955	4,830	1,505
Consumer	—	65	37	62	62
Mortgage warehouse	—	—	—	—	—
Total non-accrual loans	<u>2,892</u>	<u>5,419</u>	<u>5,827</u>	<u>6,261</u>	<u>9,033</u>
Accruing loans past due 90 days or more	—	—	—	—	—
Other real estate owned	—	—	—	1,676	—
Total non-performing assets	<u>\$ 2,892</u>	<u>\$ 5,419</u>	<u>\$ 5,827</u>	<u>\$ 7,937</u>	<u>\$ 9,033</u>
Total loans ⁽¹⁾	\$ 1,453,299	\$ 1,333,328	\$ 973,130	\$ 847,208	\$ 751,895
Total assets	\$ 1,729,283	\$ 1,505,781	\$ 1,121,788	\$ 974,079	\$ 902,265
Total non-performing loans to total loans ⁽¹⁾	0.20%	0.41%	0.60%	0.74%	1.20%
Total non-performing assets to total assets	0.17%	0.36%	0.52%	0.81%	1.00%

(1) Loans are presented before allowance for loan losses, but include deferred loan costs/fees.

The decrease in commercial non-accrual loans at December 31, 2021 as compared to the prior year was primarily due to workouts of loans in our portfolio.

We have cooperative relationships with the vast majority of our non-performing loan customers. Substantially all non-performing loans are collateralized by business assets or real estate and the repayment is largely dependent on the return of such loans to performing status or the liquidation of the underlying collateral. We pursue the resolution of all non-performing loans through collections, restructures, voluntary liquidation of collateral by the borrower and, where necessary, legal action. When attempts to work with a customer to return a loan to performing status, including restructuring the loan, are unsuccessful, we will initiate appropriate legal action seeking to acquire property by deed in lieu of foreclosure or through foreclosure, or to liquidate business assets.

The following table sets forth the accruing and non-accruing status of troubled debt restructurings at the dates indicated.

<i>(In thousands)</i>	At December 31,					
	2021		2020		2019	
	Non-Accruing	Accruing	Non-Accruing	Accruing	Non-Accruing	Accruing
Troubled Debt Restructurings:						
Real estate:						
Residential	\$ —	\$ —	\$ —	\$ 162	\$ —	\$ 182
Commercial	—	20,188	—	21,042	—	1,243
Construction and land development	—	—	—	—	—	—
Commercial	616	1,849	1,805	257	2,436	371
Consumer	—	—	—	—	—	—
Mortgage warehouse	—	—	—	—	—	—
Total	<u>\$ 616</u>	<u>\$ 22,037</u>	<u>\$ 1,805</u>	<u>\$ 21,461</u>	<u>\$ 2,436</u>	<u>\$ 1,796</u>

	At December 31,			
	2018		2017	
	Non-Accruing	Accruing	Non-Accruing	Accruing
<i>(In thousands)</i>				
Troubled Debt Restructurings:				
Real estate:				
Residential	\$ —	\$ 388	\$ —	\$ 404
Commercial	—	1,334	—	1,521
Construction and land development	—	—	—	—
Commercial	1,089	462	67	1,698
Consumer	—	—	—	—
Mortgage warehouse	—	—	—	—
Total	<u>\$ 1,089</u>	<u>\$ 2,184</u>	<u>\$ 67</u>	<u>\$ 3,623</u>

Potential Problem Loans. We classify certain commercial real estate, construction and land development, and commercial loans as “special mention”, “substandard”, or “doubtful”, based on criteria consistent with guidelines provided by our banking regulators. Certain potential problem loans represent loans that are currently performing, but for which known information about possible credit problems of the related borrowers causes management to have doubts as to the ability of such borrowers to comply with the present loan repayment terms and which may result in such loans becoming non-performing at some time in the future. Potential problem loans also include non-accrual or restructured loans presented above. We expect the levels of non-performing assets and potential problem loans to fluctuate in response to changing economic and market conditions, and the relative sizes of the respective loan portfolios, along with our degree of success in resolving problem assets.

Other potential problem loans are those loans that are currently performing, but where known information about possible credit problems of the borrowers causes us to have concerns as to the ability of such borrowers to comply with contractual loan repayment terms. At December 31, 2021, other potential problem loans totaled \$22.0 million, consisting of 15 troubled debt restructured loans that were accruing interest in accordance with their modified terms.

The Company is working with customers affected by COVID-19. As a result of the current economic crisis caused by the COVID-19 virus, the Company is engaging in more frequent communication with borrowers to better understand their situation and challenges faced.

The Company established a modification program in accordance with applicable regulations to provide economic relief. In working with our borrowers, the Company provided up to six-month payment deferrals. At the completion of the payment deferral, the Company allowed for deferral extensions on an as-needed and case-by-case basis. Under agency guidance and Section 4013 of the CARES Act, these modifications were not classified as troubled debt restructurings and were not considered delinquent. Throughout 2020, there were 287 outstanding loans, totaling \$265.6 million, or 19.9% of total loans at December 31, 2020, that had been modified under agency guidance and Section 4013 of the CARES Act. As of December 31, 2021, all loans that were modified under the CARES Act have resumed repayment or have been paid off.

Allowance for Loan Losses. The allowance for loan losses is maintained at levels considered adequate by management to provide for probable loan losses inherent in the loan portfolio as of the consolidated balance sheet reporting dates. The allowance for loan losses is based on management’s assessment of various factors affecting the loan portfolio, including portfolio composition, delinquent and non-accrual loans, national and local business conditions and loss experience and an overall evaluation of the quality of the underlying collateral.

The following table sets forth activity in our allowance for loan losses for the years indicated.

<i>(Dollars in thousands)</i>	Year Ended December 31,				
	2021	2020	2019	2018	2017
Allowance at beginning of year	\$ 18,518	\$ 13,844	\$ 11,680	\$ 9,757	\$ 8,590
Provision for loan losses	3,887	5,597	5,326	3,329	2,929
Charge offs:					
Real estate:					
Residential	—	—	—	—	—
Commercial	150	117	—	670	1,522
Construction and land development	—	24	—	—	—
Commercial	2,980	176	1,950	190	107
Consumer	315	772	1,355	699	190
Mortgage warehouse	—	—	—	—	—
Total charge-offs	3,445	1,089	3,305	1,559	1,819
Recoveries:					
Real estate:					
Residential	2	4	7	2	—
Commercial	92	—	—	—	45
Construction and land development	—	—	—	—	—
Commercial	368	7	35	87	—
Consumer	74	155	101	64	12
Mortgage warehouse	—	—	—	—	—
Total recoveries	536	166	143	153	57
Net charge-offs	2,909	923	3,162	1,406	1,762
Allowance at end of year	\$ 19,496	\$ 18,518	\$ 13,844	\$ 11,680	\$ 9,757
Non-performing loans at end of year	\$ 2,892	\$ 5,419	\$ 5,827	\$ 6,261	\$ 9,033
Total loans outstanding at end of year ⁽¹⁾	\$ 1,453,299	\$ 1,333,328	\$ 973,130	\$ 847,208	\$ 751,895
Average loans outstanding during the year ⁽¹⁾	\$ 1,320,160	\$ 1,209,736	\$ 906,909	\$ 783,570	\$ 698,859
Allowance to non-performing loans	674.14%	341.72%	237.58%	186.55%	108.02%
Allowance to total loans outstanding at end of the year ⁽²⁾	1.34%	1.39%	1.42%	1.38%	1.30%
Net charge-offs to average loans outstanding during the year	0.22%	0.08%	0.35%	0.18%	0.25%

(1) Loans are presented before the allowance for loan losses but include deferred fees/costs

(2) Allowance to total loans outstanding at end of the year, excluding \$12.4 million and \$41.8 million in PPP loans, was 1.35% and 1.43% at December 31, 2021 and 2020, respectively. There were no outstanding PPP loans at December 31, 2019, 2018 or 2017.

The following tables set forth net (recoveries)/charge-offs to average loans outstanding during the year based on loan categories.

	For the Year Ended December 31,								
	2021			2020			2019		
	Average Balance	% of Net (Recoveries) / Charge-offs to		Average Balance	% of Net (Recoveries) / Charge-offs to		Average Balance	% of Net (Recoveries) / Charge-offs to	
		Net (Recoveries) / Charge-offs	Average Balance		Net (Recoveries) / Charge-offs	Average Balance		Net (Recoveries) / Charge-offs	Average Balance
<i>(Dollars in thousands)</i>									
Real estate:									
Residential	\$ 27,310	\$ (2)	(0.01)%	\$ 39,584	\$ (4)	(0.01)%	\$ 52,068	\$ (7)	(0.01)%
Commercial	419,859	58	0.01	415,055	117	0.03	389,729	—	—
Construction and land development	35,420	—	—	45,444	24	0.05	41,810	—	—
Commercial	612,473	2,612	0.43	554,705	169	0.03	407,285	1,915	0.47
Consumer	3,399	241	7.09	9,077	617	6.80	17,755	1,254	7.06
Mortgage warehouse	226,636	—	—	149,755	—	—	—	—	—
Total gross	1,325,097	\$ 2,909	0.22	1,213,620	\$ 923	0.08	908,647	\$ 3,162	0.35
Deferred loan fees, net	(4,937)			(3,884)			(1,738)		
Total loans outstanding at end of year (1)	<u>\$1,320,160</u>		0.22 %	<u>\$1,209,736</u>		0.08 %	<u>\$906,909</u>		0.35 %

	For the Year Ended December 31,					
	2018			2017		
	Average Balance	Net (Recoveries) / Charge-offs to Average Balance		Average Balance	Net (Recoveries) / Charge-offs to Average Balance	
		Net (Recoveries) / Charge-offs	% of Net (Recoveries) / Charge-offs		Net (Recoveries) / Charge-offs	% of Net (Recoveries) / Charge-offs
<i>(Dollars in thousands)</i>						
Real estate:						
Residential	\$ 62,698	\$ (2)	— %	\$ 72,477	\$ —	— %
Commercial	363,903	670	0.18	367,144	1,477	0.40
Construction and land development	52,285	—	—	38,091	—	—
Commercial	286,142	103	0.04	210,316	107	0.05
Consumer	19,474	635	3.26	11,419	178	1.56
Mortgage warehouse	—	—	—	—	—	—
Total gross loans	784,502	\$ 1,406	0.18	699,447	\$ 1,762	0.25
Deferred loan fees, net	(932)			(587)		
Total loans outstanding at end of year (1)	<u>\$ 783,570</u>		0.18 %	<u>\$ 698,860</u>		0.25 %

(1) Loans are presented before the allowance for loan losses but include deferred fees/costs

Allocation of Allowance for Loan Losses. The following tables set forth the allowance for loan losses allocated by loan category. The allowance for loan losses allocated to each category is not necessarily indicative of future losses in any particular category and does not restrict the use of the allowance to absorb losses in other categories.

	At December 31,					
	2021		2020		2019	
	Allowance for Loan Losses	% of Loans in Category to Total Loans	Allowance for Loan Losses	% of Loans in Category to Total Loans	Allowance for Loan Losses	% of Loans in Category to Total Loans
<i>(Dollars in thousands)</i>						
Real estate:						
Residential	\$ 38	0.06 %	\$ 184	2.46 %	\$ 254	4.69 %
Commercial	4,935	29.66	6,095	32.82	6,104	42.89
Construction and land development	479	2.94	447	2.16	749	4.79
Commercial	13,495	49.83	10,543	42.31	6,086	46.32
Consumer	168	0.10	586	0.41	650	1.31
Mortgage warehouse	381	17.41	663	19.84	—	—
Total allocated allowance for loan losses	19,496	100.00 %	18,518	100.01 %	13,843	100.00 %
Unallocated	—		—		1	
Total	\$ 19,496		\$ 18,518		\$ 13,844	

	At December 31,			
	2018		2017	
	Allowance for Loan Losses	% of Loans in Category to Total Loans	Allowance for Loan Losses	% of Loans in Category to Total Loans
<i>(Dollars in thousands)</i>				
Real estate:				
Residential	\$ 251	6.76 %	\$ 300	9.00 %
Commercial	4,152	43.00	4,483	49.35
Construction and land development	738	5.26	965	7.42
Commercial	5,742	42.64	3,280	31.91
Consumer	710	2.34	649	2.32
Mortgage warehouse	—	—	—	—
Total allocated allowance for loan losses	11,593	100.00 %	9,677	100.00 %
Unallocated	87		80	
Total	\$ 11,680		\$ 9,757	

The allowance consists of general, specific, and unallocated components. The general component relates to pools of non-impaired loans and is based on historical loss experience adjusted for qualitative factors. The allocated component relates to loans that are classified as impaired, whereby an allowance is established when the discounted cash flows, collateral value, less estimated selling costs, or observable market price of the impaired loan is lower than the carrying value of that loan.

An unallocated component may be maintained to cover uncertainties that could affect management's estimate of probable losses. The unallocated component of the allowance reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating allocated and general reserves in the portfolio.

We had impaired loans totaling \$24.1 million and \$25.7 million as of December 31, 2021 and 2020, respectively. Impaired loans totaling \$1.9 million and \$4.0 million had a valuation allowance of \$1.6 million and \$2.0 million at December 31, 2021 and 2020, respectively. Our average investment in impaired loans was \$24.9 million and \$26.2 million for the years ended December 31, 2021 and 2020, respectively.

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

Large groups of smaller balance homogeneous loans are collectively evaluated for impairment based on payment status. Accordingly, we do not separately identify individual one- to four-family residential and consumer loans for impairment disclosures, unless such loans are subject to a troubled debt restructuring. We periodically agree to modify the contractual terms of loans. When a loan is modified and a concession is made to a borrower experiencing financial difficulty, the modification is considered a troubled debt restructuring. All troubled debt restructurings are initially classified as impaired.

Mortgage warehouse loans are facility lines to non-bank mortgage origination companies for sale into secondary markets, which is typically within 15 days of loan closure. Due to their short-term nature, these loans are assessed at a lower credit risk and do not carry the same allocation as traditional loans.

We review residential and commercial loans for impairment based on the fair value of collateral, if collateral-dependent, or the present value of expected cash flows. Management has reviewed the collateral value for all impaired and non-accrual loans that were collateral dependent as of December 31, 2021 and considered any probable loss in determining the allowance for loan losses.

Loans that are partially charged off generally remain on non-accrual status until foreclosure or such time that they are performing in accordance with the terms of the loan and have a sustained payment history of at least six months. The accrual of interest is generally discontinued when the contractual payment of principal or interest has become 90 days past due or management has serious doubts about further collectability of principal or interest, even though the loan is currently performing. Loan losses are charged against the allowance when we believe the uncollectability of a loan balance is confirmed; for collateral-dependent loans, generally when appraised values (as adjusted values, if applicable) less estimated costs to sell, are less than our carrying values.

Although we believe that we use the best information available to establish the allowance for loan losses, future adjustments to the allowance for loan losses may be necessary and our results of operations could be adversely affected if circumstances differ substantially from the assumptions used in making the determinations. Furthermore, while we believe we have established our allowance for loan losses in conformity with generally accepted accounting principles in the United States of America, our regulators, in reviewing our loan portfolio, may require us to increase our allowance for loan losses. In addition, because future events affecting borrowers and collateral cannot be predicted with certainty, the existing allowance for loan losses may not be adequate or increases may be necessary should the quality of any loans deteriorate as a result of the factors discussed above. Any material increase in the allowance for loan losses may adversely affect our financial condition and results of operations.

Securities Portfolio

The following table sets forth the composition of our securities portfolio at the dates indicated,

	At December 31,					
	2021		2020		2019	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value	Amortized Cost	Fair Value
<i>(In thousands)</i>						
Securities available- for-sale:						
State and municipal	\$ 12,002	\$ 12,591	\$ 10,211	\$ 10,894	\$ 10,808	\$ 11,206
Asset-backed securities	8,141	8,255	4,432	4,710	5,433	5,500
Government mortgage-backed securities	15,842	15,991	16,172	16,611	24,954	25,084
Total	<u>\$ 35,985</u>	<u>\$ 36,837</u>	<u>\$ 30,815</u>	<u>\$ 32,215</u>	<u>\$ 41,195</u>	<u>\$ 41,790</u>

At December 31, 2021, we had no investments in a single company or entity, other than government and government agency securities, that had an aggregate book value in excess of 10% of our equity.

Portfolio Maturities and Yields. The composition and maturities of the investment securities portfolio at December 31, 2021 are summarized in the following table. Certain mortgage-backed securities have adjustable interest rates and will reprice annually within the various maturity ranges. These repricing schedules are not reflected in the table below. Weighted average yields are calculated based on amortized cost and no tax-equivalent yield adjustments have been made, as the amount of tax-free interest-earning assets is immaterial.

	More than One Year to Five		More than Five Years to Ten		More than Ten Years		Total		
	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield	Amortized Cost	Fair Value	Weighted Average Yield
<i>(Dollars in thousands)</i>									
Securities available-for-sale:									
State and municipal	\$ 582	3.00%	\$ 598	4.32%	\$ 10,822	2.63%	\$ 12,002	\$ 12,591	2.73%
Asset-backed securities	136	1.97%	4,802	1.55%	3,203	2.76%	8,141	8,255	2.03%
Government mortgage-backed securities	213	1.51%	3,893	1.98%	11,736	1.29%	15,842	15,991	1.46%
Total	<u>\$ 931</u>		<u>\$ 9,293</u>		<u>\$ 25,761</u>		<u>\$ 35,985</u>	<u>\$ 36,837</u>	

Each reporting period, we evaluate all securities with a decline in fair value below the amortized cost of the investment to determine whether or not the impairment is deemed to be other-than-temporary. Other-than-temporary impairment (“OTTI”) is required to be recognized if (1) we intend to sell the security; (2) it is more likely than not that we will be required to sell the security before recovery of its amortized cost basis; or (3) for debt securities, the present value of expected cash flows is not sufficient to recover the entire amortized cost basis. For impaired debt securities that we intend to sell, or more likely than not will be required to sell, the full amount of the depreciation is recognized as OTTI, resulting in a realized loss that is a charged to earnings through a reduction in our non-interest income. For all other impaired debt securities, credit-related OTTI is recognized through earnings and non-credit related OTTI is recognized in other comprehensive income/loss, net of applicable taxes. We did not recognize any OTTI during the years ended December 31, 2021 or 2020.

Deposits

Total deposits increased \$222.5 million, or 18.0%, to \$1.46 billion at December 31, 2021 from \$1.24 billion at December 31, 2020. Our continuing focus on the acquisition and expansion of core deposit relationships, which we define as all deposits except for certificates of deposit, resulted in net growth in these deposits of \$340.1 million, or 32.1%, to \$1.40 billion at December 31, 2021, or 95.9% of total deposits at that date. Included in the growth of our core deposit relationships is an increase in NOW and demand deposits of \$270.4 million, or 48.8%, an increase of \$65.8 million, or 18.6%, in money market accounts and an increase of \$3.9 million, or 2.6%, in savings accounts. NOW and demand deposits and money market deposits increased primarily due to new and expanded relationships with traditional, digital asset, and banking as a service (“BaaS”) customers. As of December 31, 2021, deposit relationships with digital asset customers increased \$68.7 million, or 222.3%, to \$99.7 million compared to \$30.9 million at December 31, 2020. In 2021, the Company began offering deposit services to BaaS customers. BaaS is an end-to-end solution that allows financial technology companies (“FinTechs”) or other third parties to connect to banks’ systems directly via application programming interfaces so they can build banking offerings on top of the providers’ regulated infrastructure. As of December 31, 2021, deposits with BaaS customers totaled \$59.9 million. The increase in savings accounts is primarily caused by increased consumer savings. Certificates of deposit decreased \$117.7 million, or 66.0% primarily due to roll-off of brokered certificates of deposit. In addition, the Bank has increased its focus on growing noninterest-bearing deposit balances and as of December 31, 2021 noninterest-bearing deposits represented 42.9% of total deposits compared to 31.0% at December 31, 2020.

The following tables set forth the distribution of total deposits by account type at the dates indicated.

	At December 31,					
	2021		2020		2019	
	Amount	Percent	Amount	Percent	Amount	Percent
	(Dollars in thousands)					
Noninterest bearing	\$ 626,587	42.92%	\$ 383,079	30.96%	\$ 222,088	26.13%
Negotiable order of withdrawal (NOW)	197,884	13.55%	171,016	13.82%	147,335	17.34%
Savings accounts	155,267	10.64%	151,341	12.23%	115,593	13.60%
Money market deposit accounts	419,625	28.74%	353,793	28.59%	270,471	31.82%
Certificates of deposit	60,532	4.15%	178,199	14.40%	94,418	11.11%
Total	<u>\$ 1,459,895</u>	<u>100.00%</u>	<u>\$ 1,237,428</u>	<u>100.00%</u>	<u>\$ 849,905</u>	<u>100.00%</u>

As of December 31, 2021, our certificates of deposit included \$20.2 million of brokered certificates of deposit and \$16.8 million of QwickRate certificates of deposit. As of December 31, 2021 and 2020, all deposits were insured in full through our participation in the Massachusetts Depositors Insurance Fund (“DIF”).

As of December 31, 2021, the aggregate amount of all our certificates of deposit in amounts greater than or equal to \$250,000, which excludes all brokered certificates, was approximately \$5.1 million. The following table sets forth the maturity of these certificates as of December 31, 2021.

Maturity Period	At December 31, 2021 (In thousands)
Three months or less	\$ 574
Over three through six months	324
Over six through twelve months	1,203
Over twelve months	2,977
Total	<u>\$ 5,078</u>

Borrowings

Borrowings were \$13.5 million at December 31, 2021 and 2020. All of the borrowings at December 31, 2021 and 2020 were Federal Home Loan Bank long-term advances with an original maturity of more than one year. The weighted average interest rate was 2.11% and 2.12% at December 31, 2021 and 2020 respectively.

We had no securities sold under agreements to repurchase during the years ended December 31, 2021 and 2020.

Shareholders' Equity

Total shareholders' equity decreased \$2.1 million, or 0.9%, to \$233.8 million at December 31, 2021, from \$235.9 million at December 31, 2020. The decrease was primarily due to the repurchase of 1,272,607 shares of common stock for \$19.0 million, \$2.6 million from dividends paid, and a decrease in other comprehensive income of \$409,000, partially offset by net income of \$16.1 million, stock-based compensation expense of \$2.5 million and employee stock ownership plan shares earned of \$1.4 million.

Average Balance Sheets and Related Yields and Rates

The following tables set forth average balance sheets, average yields and costs, and certain other information for the years indicated. No tax-equivalent yield adjustments have been made, as we consider the amount of tax free interest-earning assets is immaterial. All average balances are daily average balances. Non-accrual loans were included in the computation of average balances. The yields set forth below include the effect of deferred fees, discounts, and premiums that are amortized or accreted to interest income or interest expense.

	For the Year Ended December 31,								
	2021			2020			2019		
	Average Balance	Interest Earned/ Paid	Yield/ Rate	Average Balance	Interest Earned/ Paid	Yield/ Rate	Average Balance	Interest Earned/ Paid	Yield/ Rate
<i>(Dollars in thousands)</i>									
Assets:									
Interest-earning assets:									
Loans ⁽¹⁾	\$1,320,160	\$ 63,873	4.84%	\$1,209,736	\$ 59,391	4.91%	\$ 906,909	\$ 49,693	5.48%
Short-term investments	159,656	208	0.13%	38,048	99	0.26%	19,106	296	1.55%
Investment securities	34,022	708	2.08%	37,320	830	2.22%	47,793	1,344	2.81%
Federal Home Loan Bank stock	827	14	1.69%	1,582	83	5.25%	3,281	205	6.25%
Total interest-earning assets	1,514,665	64,803	4.28%	1,286,686	60,403	4.69%	977,089	51,538	5.27%
Non-interest earning assets	73,057			62,741			62,522		
Total assets	\$1,587,722			\$1,349,427			\$1,039,611		
Interest-bearing liabilities:									
Savings accounts	\$ 151,586	196	0.13%	\$ 137,679	314	0.23%	\$ 128,438	419	0.33%
Money market accounts	406,392	1,680	0.41%	295,483	2,159	0.73%	238,708	2,857	1.20%
Now accounts	162,618	416	0.26%	136,613	518	0.38%	108,658	423	0.39%
Certificates of deposit	122,619	793	0.65%	163,032	2,212	1.36%	117,126	2,559	2.18%
Total interest-bearing deposits	843,215	3,085	0.37%	732,807	5,203	0.71%	592,930	6,258	1.06%
Borrowings	13,503	285	2.11%	43,682	728	1.67%	72,361	1,890	2.61%
Total interest-bearing liabilities	856,718	3,370	0.39%	776,489	5,931	0.76%	665,291	8,148	1.22%
Noninterest-bearing liabilities:									
Noninterest-bearing deposits	476,743			319,451			212,753		
Other noninterest-bearing liabilities	18,895			16,293			15,178		
Total liabilities							893,222		
Total equity	235,366			237,194			146,389		
Total liabilities and equity	\$1,587,722			\$1,349,427			\$1,039,611		
Net interest income		\$ 61,433			\$ 54,472			43,390	
Interest rate spread ⁽²⁾			3.89%			3.93%			4.05%
Net interest-earning assets ⁽³⁾	\$ 657,947			\$ 510,197			\$ 311,798		
Net interest margin ⁽⁴⁾			4.06%			4.23%			4.44%
Average interest-earning assets to interest-bearing liabilities		176.80%			165.71%			146.87%	

(1) Interest earned/paid on loans includes fee income related to SBA loan forgiveness of \$2.4 million and \$1.8 million for the years ended December 31, 2021 and 2020, respectively, and mortgage warehouse loan origination fee income of \$1.4 million and \$759,000 for the years ended December 31, 2021 and 2020, respectively. There was no fee income related to SBA loan forgiveness or mortgage warehouse loan originations for the year ended December 31, 2019.

(2) Net interest rate spread represents the difference between the weighted average yield on interest-bearing assets and the weighted average rate of interest-bearing liabilities.

(3) Net interest-earning assets represent total interest-earning assets less total interest-bearing liabilities.

(4) Net interest margin represents net interest income divided by average total interest-earning assets.

Rate/Volume Analysis

The following table sets forth the effects of changing rates and volumes on our net interest income. The rate column shows the effects attributable to changes in rate (changes in rate multiplied by prior volume). The volume column shows the effects attributable to changes in volume (changes in volume multiplied by prior rate). The net column represents the sum of the prior columns. For purposes of this table, changes attributable to changes in both rate and volume that cannot be segregated have been allocated proportionally based on the changes due to rate and the changes due to volume. There are no out-of-period adjustments excluded from the table below.

(In thousands)	Year Ended December 31, 2021 vs. 2020			Year Ended December 31, 2020 vs. 2019		
	Increase (Decrease) Due to		Total Increase (Decrease)	Increase (Decrease) Due to		Total Increase (Decrease)
	Rate	Volume		Rate	Volume	
Interest-earning assets:						
Loans	\$ (871)	\$ 5,353	\$ 4,482	\$ (5,579)	\$ 15,277	\$ 9,698
Short-term investments	(70)	179	109	(357)	160	(197)
Debt securities available-for-sale	(52)	(70)	(122)	(251)	(263)	(514)
Federal Home Loan Bank stock	(40)	(29)	(69)	(29)	(93)	(122)
Total interest-earning assets	<u>(1,033)</u>	<u>5,433</u>	<u>4,400</u>	<u>(6,216)</u>	<u>15,081</u>	<u>8,865</u>
Interest-bearing liabilities:						
Savings accounts	(147)	29	(118)	(133)	28	(105)
Money market accounts	(1,126)	647	(479)	(1,277)	579	(698)
Now accounts	(189)	87	(102)	(11)	106	95
Certificates of deposit	(963)	(456)	(1,419)	(1,157)	810	(347)
Total interest-bearing deposits	<u>(2,425)</u>	<u>307</u>	<u>(2,118)</u>	<u>(2,578)</u>	<u>1,523</u>	<u>(1,055)</u>
Borrowings	157	(600)	(443)	(555)	(607)	(1,162)
Total interest-bearing liabilities	<u>(2,268)</u>	<u>(293)</u>	<u>(2,561)</u>	<u>(3,133)</u>	<u>916</u>	<u>(2,217)</u>
Change in net interest and dividend income	<u>\$ 1,235</u>	<u>\$ 5,726</u>	<u>\$ 6,961</u>	<u>\$ (3,083)</u>	<u>\$ 14,165</u>	<u>\$ 11,082</u>

Comparison of Results of Operations for the Years Ended December 31, 2021 and 2020

General. Net income increased \$4.2 million, or 34.7%, to \$16.1 million for the year ended December 31, 2021 from \$12.0 million for the year ended December 31, 2020. The increase was primarily due to an increase of \$7.0 million, or 12.8%, in net interest and dividend income, an increase in noninterest income of \$1.6 million, or 45.8%, a decrease in provision for loan losses of \$1.7 million, or 30.6%, a decrease in write downs of other assets and receivables of \$2.0 million, or 89.8%, partially offset by an increase in salaries and employee benefits expense of \$5.6 million, or 24.2%, and an increase in income tax expense of \$1.3 million, or 28.7%.

Interest and Dividend Income. Interest and dividend income increased \$4.4 million, or 7.3%, to \$64.8 million for the year ended December 31, 2021 from \$60.4 million for the year ended December 31, 2020. This was caused by an increase in interest and fees on loans, which increased \$4.5 million, or 7.5%, partially offset by a decrease in interest and dividends on securities of \$191,000, or 20.9%.

The increase in interest income on loans was due to an increase in average loan balance of \$110.4 million, or 9.1%, to \$1.32 billion for the year ended December 31, 2021 from \$1.21 billion for the year ended December 31, 2020. The increase was partially offset by a decrease in the yield on loans of seven basis points, to 4.84% for the year ended December 31, 2021 from 4.91% for the year ended December 31, 2020, due to lower market interest rates, and the origination of mortgage warehouse loans which typically yield a lower rate than the rest of our portfolio.

The decrease in interest and dividends on securities was due to a decrease in the average balance of debt securities available-for-sale of \$3.3 million, or 8.8%, to \$34.0 million for the year ended December 31, 2021 from \$37.3 million for the year ended December 31, 2020 and a 14 basis point decrease in the yield on such securities to 2.08% for 2021 from 2.22% for 2020.

Interest Expense. Interest expense decreased \$2.6 million, or 43.2%, to \$3.4 million for the year ended December 31, 2021 from \$5.9 million for the year ended December 31, 2020. The decrease was caused by decreases in interest expense on deposits and borrowings. Interest expense on deposits decreased \$2.1 million, or 40.7%, to \$3.1 million for the year ended December 31, 2021 from \$5.2 million for the year ended December 31, 2020. This was primarily due to a decrease in the cost of interest-bearing deposits of 34 basis points to 0.37% for the year ended December 31, 2021 from 0.71% for the year ended December 31, 2020. This decrease was partially offset by an increase in the average balance of interest-bearing deposits of \$110.4 million, or 15.1%, to \$843.2 million for the year ended December 31, 2021 from \$732.8 million for the year ended December 31, 2020. The increase resulted primarily from an increase in the average balance of money market accounts, which increased \$110.9 million, or 37.5%.

Interest expense on borrowings, which consists of advances from the Federal Home Loan Bank of Boston and borrowings from the Federal Reserve Bank borrower-in-custody program, decreased \$443,000, or 60.9%, to \$285,000 for the year ended December 31, 2021 from \$728,000 for the year ended December 31, 2020. This decrease was primarily due to a decrease in the average balance of borrowings of \$30.2 million, or 69.1%, to \$13.5 million for the year ended December 31, 2021 from \$43.7 million for the year ended December 31, 2020, primarily due to increased deposits funding loan growth.

Net Interest and Dividend Income. Net interest and dividend income increased \$7.0 million, or 12.8%, to \$61.4 million for the year ended December 31, 2021 from \$54.5 million for the year ended December 31, 2020. The growth in net interest and dividend income was primarily the result of an increase in our average interest-earning assets of \$228.0 million, or 17.7%, offset by an increase in average interest-bearing liabilities of \$80.2 million, or 10.3%, and a decrease in net interest margin of 17 basis points to 4.06%. The decrease in the net interest margin was the result of a combination of factors including a decreasing rate environment, and an increase in short-term investments, which have a lower rate. The net interest margin benefitted from the accretion of fee income related to the forgiveness of the SBA PPP loans. The amount of income recognized from the forgiveness totaled \$2.4 million for the year ended December 31, 2021. As of December 31, 2021, there was \$503,000 in SBA PPP fee income remaining to be accreted.

Provision for Loan Losses. The provision for loan losses was \$3.9 million for the year ended December 31, 2021 compared to \$5.6 million for the year ended December 31, 2020, which is a decrease of \$1.7 million, or 30.6%. The changes in the provision were based on management's assessment of economic conditions, including the impact of the COVID-19 pandemic, loan portfolio growth and composition changes, historical charge-off trends, levels of problem loans and other asset quality trends. For the year ended December 31, 2021, the decreased provision was offset by an increase in net charge-offs, which were \$2.9 million for the year ended December 31, 2021 compared to \$923,000 for the year ended December 31, 2020.

The provision recorded resulted in an allowance for loan losses of \$19.5 million, or 1.34% of total loans at December 31, 2021, compared to \$18.5 million, or 1.39% of total loans at December 31, 2020. Allowance for loan losses as a percentage of loans is lower in the current year primarily due to improvements in economic conditions, reduction in warehouse reserves, offset by increases in classified loans. During the year ended December 31, 2020, we had increases in provision for loan losses and the related allowance due to the COVID-19 pandemic. Included in total loans was \$12.4 million and \$41.8 million at December 31, 2021 and 2020, respectively, in PPP loans originated as part of the CARES Act that we believe have no credit risk due to a government guarantee, therefore, we have not provided for losses for these loans. Excluding these loans, the allowance for loan losses as a percentage of total loans was 1.35% and 1.43% as of December 31, 2021 and 2020, respectively. As of December 31, 2021 and 2020, there was \$253.8 million and \$265.4 million, respectively, in outstanding mortgage warehouse loan balances. Loans in this segment are facility lines to non-bank mortgage origination companies for sale into secondary markets, which is typically within 15 days of loan closure. Due to their short-term nature, these loans are assessed at a lower credit risk and do not carry the same allocation as traditional loans. The allowance for loans losses as a percentage of non-performing loans was 674.14% as of December 31, 2021 compared to 341.72% as of December 31, 2020. Non-performing loans were \$2.9 million, or 0.17% of total assets as of December 31, 2021 compared to \$5.4 million, or 0.36% of total assets, as of December 31, 2020. As of December 31, 2021, the largest non-performing loan relationships consisted of two commercial relationship totaling \$1.8 million. These loan relationships were evaluated for impairment and specific reserves of \$1.6 million were allocated as of December 31, 2021.

Noninterest Income. Noninterest income information is as follows.

	Years Ended		Change	
	December 31,		Amount	Percent
(Dollars in thousands)	2021	2020		
Customer service fees on deposit accounts	\$ 1,832	\$ 1,331	\$ 501	37.6 %
Service charges and fees - other	2,003	1,322	681	51.5 %
Bank owned life insurance	1,195	809	386	47.7 %
Other income	136	81	55	67.9 %
Total noninterest income	\$ 5,166	\$ 3,543	\$ 1,623	45.8 %

Customer service fees on deposit accounts increased \$501,000, or 37.6%, primarily due to fees generated from cash vault services for our customers who operate Bitcoin ATMs, which totaled \$274,000. In addition, 2021 fees reflect higher income compared to 2020 due to fees being waived for customers impacted by COVID-19. Other service charges and fees increased \$681,000, or 51.5%, primarily due to increased late fee charges as well as income from loan prepayment penalties related to two commercial loan relationships. The increase in bank owned life insurance income of \$386,000, or 47.7%, is primarily due to the receipt of a death benefit payout during the third quarter of 2021 as well as the purchase of additional insurance policies in the second quarter of 2020.

Noninterest Expense. Noninterest expense information is as follows.

	Years Ended December 31,		Change	
	2021	2020	Amount	Percent
<i>(Dollars in thousands)</i>				
Salaries and employee benefits	\$ 28,782	\$ 23,175	\$ 5,607	24.2 %
Occupancy expense	1,687	1,684	3	0.2 %
Equipment expense	514	577	(63)	(10.9) %
Deposit insurance	482	416	66	15.9 %
Data processing	1,325	1,000	325	32.5 %
Marketing expense	279	223	56	25.1 %
Professional fees	2,083	1,868	215	11.5 %
Directors' compensation	992	750	242	32.3 %
Software amortization and implementation	1,014	959	55	5.7 %
Write down of other assets and receivables	225	2,207	(1,982)	— %
Other	3,236	2,949	287	9.7 %
Total noninterest expense	<u>\$ 40,619</u>	<u>\$ 35,808</u>	<u>\$ 4,811</u>	13.4 %

Salaries and employee benefits expense increased \$5.6 million, or 24.2%, for the year ended December 31, 2021 from the year ended December 31, 2020 primarily due to stock-based compensation expense for new grants awarded and an increase in staff to support the development and implementation of new technologies and specialty lending products. Also included in salaries and employee benefit expense is a \$984,000 expense relating to an agreement entered into on November 1, 2021 between the Bank and the President and Chief Lending Officer in connection with his retirement. Data processing fees increased \$325,000 or 32.5%, primarily due to new contracts for deposit services. Directors' compensation increased \$242,000, or 32.3%, primarily due to increase stock-based compensation expense. The increase of \$287,000, or 9.7%, in other expense was primarily due to increased costs related to third-party services for both marketing and information technology, as well as increased costs associated with conferences and training which were largely canceled during 2020 due to the COVID-19 pandemic. Professional fees increased \$215,000, or 11.5%, primarily due to an increase in audit and compliance costs. These increases were offset by a decrease in write downs of other assets and receivables of \$2.0 million. In the first quarter of 2020 a write-down of a notes receivable balance was completed after the Company evaluated the collectability and determined that \$500,000 was uncollectible and in the third quarter of 2020 a write-down of an SBA receivable balance was completed after the Company evaluated the collectability and determined \$1.3 million was uncollectible. In the fourth quarter of 2020 a write-down of other assets was also completed after the Company evaluated the collectability and determined \$400,00 was impaired and uncollectible. The decrease in the write-downs was partially offset by a write-down of an SBA receivable in the third quarter of 2021 after the Company evaluated the collectability and determined \$195,000 was uncollectible.

Income Tax Provision. We recorded a provision for income taxes of \$6.0 million for the year ended December 31, 2021, reflecting an effective tax rate of 26.9%, compared to \$4.6 million, or an effective tax rate of 27.8%, for the year ended December 31, 2020.

Management of Market Risk

General. The majority of our assets and liabilities are monetary in nature. Consequently, our most significant form of market risk is interest rate risk. Our assets, consisting primarily of loans, have longer maturities than our liabilities, consisting primarily of deposits. As a result, a principal part of our business strategy is to manage interest rate risk and reduce the exposure of our net interest income to changes in market interest rates. Accordingly, we have established a management-level Asset/Liability Management Committee, which takes initial responsibility for developing an asset/liability management process and related procedures, establishing and monitoring reporting systems and developing asset/liability strategies. On at least a quarterly basis, the Asset/Liability Management Committee reviews asset/liability management with the Investment Asset/Liability Committee that has been established by the board of directors. This committee also reviews any changes in strategies as well as the performance of any specific asset/liability management actions that have been implemented previously. On a quarterly basis, an outside consulting firm provides us with detailed information and analysis as to asset/liability management, including our interest rate risk profile. Ultimate responsibility for effective asset/liability management rests with our board of directors.

We have sought to manage our interest rate risk in order to minimize the exposure of our earnings and capital to changes in interest rates. We have implemented the following strategies to manage our interest rate risk: originating loans with adjustable interest rates; promoting core deposit products; and adjusting the interest rates and maturities of funding sources, as necessary. In addition, we no longer originate single-family residential real estate loans, which often have longer terms and fixed rates. By following these strategies, we believe that we are better positioned to react to changes in market interest rates.

Net Interest Income Simulation. We analyze our sensitivity to changes in interest rates through a net interest income simulation model. Net interest income is the difference between the interest income we earn on our interest-earning assets, such as loans and securities, and the interest we pay on our interest-bearing liabilities, such as deposits and borrowings. We estimate what our net interest income would be for a 12-month period in the current interest rate environment. We then calculate what the net interest income would be for the same period under the assumption that interest rates increase 200 basis points from current market rates and under the assumption that interest rates decrease 100 basis points from current market rates, with changes in interest rates representing immediate and permanent, parallel shifts in the yield curve.

The following table presents the estimated changes in net interest income of BankProv, calculated on a bank-only basis, that would result from changes in market interest rates over twelve-month periods beginning December 31, 2021 and 2020.

	At December 31,			
	2021		2020	
	Estimated Net Interest Income Over Next 12 Months	Change	Estimated Net Interest Income Over Next 12 Months	Change
<i>(Dollars in thousands)</i>				
Changes in Interest Rates (Basis Points)				
200	\$ 66,384	3.40 %	\$ 55,856	2.90 %
0	64,190	—	54,301	—
-100	63,345	(1.30)	54,222	(0.10)

Economic Value of Equity Simulation. We also analyze our sensitivity to changes in interest rates through an economic value of equity (“EVE”) model. EVE represents the present value of the expected cash flows from our assets less the present value of the expected cash flows arising from our liabilities adjusted for the value of off-balance sheet contracts. The EVE ratio represents the dollar amount of our EVE divided by the present value of our total assets for a given interest rate scenario. EVE attempts to quantify our economic value using a discounted cash flow methodology while the EVE ratio reflects that value as a form of capital ratio. We estimate what our EVE would be as of a specific date. We then calculate what EVE would be as of the same date throughout a series of interest rate scenarios representing immediate and permanent, parallel shifts in the yield curve. We currently calculate EVE under the assumptions that interest rates increase 100, 200, 300 and 400 basis points from current market rates, and under the assumption that interest rates decrease 100 basis points from current market rates.

The following table presents the estimated changes in EVE of BankProv, calculated on a bank-only basis, that would result from changes in market interest rates as of December 31, 2021 and 2020.

	At December 31,			
	2021		2020	
	Economic Value of Equity	Change	Economic Value of Equity	Change
<i>(Dollars in thousands)</i>				
Changes in Interest Rates (Basis Points)				
400	\$ 372,659	13.00 %	\$ 270,977	13.00 %
300	364,387	10.50	265,117	10.60
200	354,639	7.60	258,078	7.60
100	344,675	4.60	250,743	4.60
0	329,666	—	239,739	—
(100)	285,977	(13.30)	205,526	(14.30)

Certain shortcomings are inherent in the methodologies used in the above interest rate risk measurements. Modeling changes require making certain assumptions that may or may not reflect the manner in which actual yields and costs respond to changes in market interest rates. In this regard, the tables presented above assume that the composition of our interest-sensitive assets and liabilities existing at the beginning of a period remains constant over the period being measured and assume that a particular change in interest rates is reflected uniformly across the yield curve regardless of the duration or repricing of specific assets and liabilities. Accordingly, although the 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 interest income and will differ from actual results.

Liquidity and Capital Resources

Liquidity is the ability to meet current and future financial obligations of a short-term nature. Our primary sources of funds consist of deposit inflows, loan repayments and maturities and sales of securities. While maturities and scheduled amortization of loans and securities are predictable sources of funds, deposit flows and loan prepayments are greatly influenced by general interest rates, economic conditions and competition.

We regularly review the need to adjust our investments in liquid assets based upon our assessment of: (1) expected loan demand, (2) expected deposit flows, (3) yields available on interest-earning deposits and securities, and (4) the objectives of our asset/liability management program. Excess liquid assets are invested generally in interest-earning deposits and short- and intermediate-term securities.

Our most liquid assets are cash and cash equivalents. The levels of these assets are dependent on our operating, financing, lending and investing activities during any given period. At December 31, 2021, cash and cash equivalents totaled \$153.1 million. Debt securities classified as available-for-sale, which provide additional sources of liquidity, totaled \$36.8 million at December 31, 2021. Warehouse loans that have a short-term duration also provide additional sources of liquidity. The balance that meets the definition of a liquid assets totaled \$222.9 million as of December 31, 2021.

At December 31, 2021, we had a borrowing capacity of \$141.3 million with the Federal Home Loan Bank of Boston, of which \$13.5 million in advances were outstanding. At December 31, 2021, we also had an available line of credit with the Federal Reserve Bank of Boston's borrower-in-custody program of \$194.1 million, none of which was outstanding as of that date.

We have no material commitments or demands that are likely to affect our liquidity other than as set forth below. In the event loan demand were to increase faster than expected, or any unforeseen demand or commitment were to occur, we could access our borrowing capacity with the Federal Home Loan Bank of Boston or obtain additional funds through brokered certificates of deposit.

We are a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of our customers. These financial instruments include commitments to extend credit, which involve elements of credit and interest rate risk in excess of the amount recognized in the consolidated balance sheets. At December 31, 2021 and 2020, we had \$16.4 million and \$31.9 million in loan commitments outstanding, respectively. In addition to commitments to originate loans, at December 31, 2021 and 2020, we had \$307.5 million and \$202.0 million in unadvanced funds to borrowers, respectively. We also had \$1.3 and \$1.7 million in outstanding letters of credit at December 31, 2021 and 2020, respectively.

A significant decrease in deposits could result in the Company having to seek other sources of funds, including brokered certificates of deposit, QwickRate deposits, and Federal Home Loan Bank of Boston advances. Depending on market conditions, we may be required to pay higher rates on such deposits or other borrowings than we currently pay. We believe, however, based on past experience that a significant portion of our deposits will remain with us. We have the ability to attract and retain deposits by adjusting the interest rates offered.

Non-core deposits, or volatile deposits, are accounts where full banking services are not utilized or there is significant volatility expected. The Company has identified \$44.0 million in volatile deposits as of December 31, 2021.

The Company maintains access to multiple sources of liquidity. We have utilized wholesale funding markets and have remained open but with rates that have 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 large numbers of the Company's deposit customers to withdraw their funds, the Company might become more reliant on volatile or more expensive sources of funding.

BankProv is subject to various regulatory capital requirements administered by Massachusetts Commissioner of Banks, and the Federal Deposit Insurance Corporation. At December 31, 2021, BankProv exceeded all applicable regulatory capital requirements, and was considered "well capitalized" under regulatory guidelines. See Note 12 of the Notes to the Consolidated Financial Statements for additional information.

Recent Accounting Pronouncements

For information with respect to recent accounting pronouncements that are applicable to Provident Bancorp, Inc., see Note 2 of the Notes to the Consolidated Financial Statements.

Effect of Inflation and Changing Prices

The consolidated financial statements and related financial data included in this annual report have been prepared in accordance with generally accepted accounting principles in the United States of America, which require the measurement of financial position and operating results in terms of historical dollars without considering the change 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, virtually all the assets and liabilities of a financial institution are monetary in nature. As a result, interest rates generally have a more significant impact on a financial institution's performance than do general levels of inflation. Interest rates do not necessarily move in the same direction or to the same extent as the prices of goods and services.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The information required by this item is incorporated herein by reference to Part II, Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations."

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

The Consolidated Financial Statements, including supplemental data, of Provident Bancorp, Inc. begin on page F-1 of this Annual Report.

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

None.

ITEM 9A. CONTROLS AND PROCEDURES

An evaluation was performed under the supervision and with the participation of the Company's management, including the President and Chief Executive Officer and the Executive Vice President and Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures (as defined in Rule 13a-15(e) promulgated under the Securities and Exchange Act of 1934, as amended) as of December 31, 2021. Based on that evaluation, the Company's management, including the President and Chief Executive Officer and the Executive Vice President and Chief Financial Officer, concluded that the Company's disclosure controls and procedures were effective.

During the quarter ended December 31, 2021, there have been no changes in the Company's internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

Management's Report Regarding Internal Control Over Financial Reporting

The Company's management is responsible for establishing and maintaining adequate internal control over financial reporting as such terms are defined in Rule 13a-15(f) of the Exchange Act of 1934. Our system of internal controls is designed to provide reasonable assurance that the financial statements that we provide to the public are fairly presented.

Our internal control over financial reporting includes policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect transactions and dispositions of assets, (ii) provide reasonable assurances that transactions are recorded as necessary to permit preparation of financial statements in accordance with accounting principles generally accepted in the United States of America and that receipts and expenditures are being made only in accordance with authorizations of management and the directors of the Company; and (iii) 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 our financial statements.

All internal control systems, no matter how well designed, have inherent limitations. Therefore, even those systems determined to be effective can provide only reasonable assurance with respect to financial statement preparation and presentation. Accordingly, absolute assurance cannot be provided that the effectiveness of the internal control systems may not become inadequate in future periods because of changes in conditions, or because the degree of compliance with the policies or procedures may deteriorate.

Management assessed the effectiveness of the Company's internal control over financial reporting as of December 31, 2020. In making this assessment, the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission in Internal Control-Integrated Framework (2013) was utilized. Based on this assessment, management believes that, as of December 31, 2021, the Company's internal control over financial reporting is effective at the reasonable assurance level.

The Annual Report on Form 10-K does not include an attestation report on the Company's internal control over financial reporting from the Company's independent registered public accounting firm due to the Company's status as a smaller reporting company.

ITEM 9B. OTHER INFORMATION

Not applicable.

ITEM 9C. DISCLOSURE REGARDING FOREIGN JURISDICTIONS THAT PREVENT INSPECTIONS

Not applicable.

PART III

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

The information in the Company’s definitive Proxy Statement for the 2022 Annual Meeting of Stockholders under the captions “Proposal 1—Election of Directors,” “Information About Executive Officers,” “Delinquent Section 16(a) Reports,” “Corporate Governance—Code of Ethics for Senior Officers,” “Nominating and Corporate Governance Committee Procedures—Procedures to be Followed by Stockholders,” “Corporate Governance—Committees of the Board of Directors” and “—Audit Committee” is incorporated herein by reference.

A copy of the Code of Ethics is available to shareholders on the “Corporate Governance” portion of the Investor Relations’ section on the Company’s website at www.bankprov.com.

ITEM 11. EXECUTIVE COMPENSATION

The information in the Company’s definitive Proxy Statement for the 2022 Annual Meeting of Stockholders under the caption “Executive Compensation,” “Director Compensation,” and “Corporate Governance—Committees of the Board of Directors—Compensation Committee” is incorporated herein by reference.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDERS MATTERS

The information in the Company’s definitive Proxy Statement for the 2021 Annual Meeting of Stockholders under the caption “Stock Ownership” is incorporated herein by reference.

Equity Compensation Plan Information

Information regarding stock-based compensation awards outstanding and available for future grants as of December 31, 2021 is presented in Note 10 – Employee Benefits & Share-Based Compensation Plans, in the Notes to Consolidated Financial Statements included in Item 8, Financial Statements and Supplementary Data, within this report.

	Equity Compensation Plan Information		
	Number of Securities to Be Issued Upon Exercise of Outstanding Options, Warrants and Rights	Weighted-average Exercise Price of Outstanding Options, Warrants and Rights ⁽¹⁾	Number of Securities Remaining Available for Future Issuance Under Share-based Compensation Plans (excluding securities reflected in first column)
Equity compensation plans approved by security holders	1,558,963	\$ 10.72	220,631
Equity compensation plans not approved by security holders	—	—	—
Total	<u>1,558,963</u>	<u>\$ 10.72</u>	<u>220,631</u>

(1) Reflects weighted average price of stock options only

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

The information in the Company’s definitive Proxy Statement for the 2022 Annual Meeting of Stockholders under the captions “Transactions with Certain Related Persons” and “Proposal 1 — Election of Directors” is incorporated herein by reference.

ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES

The information in the Company’s definitive Proxy Statement for the 2022 Annual Meeting of Stockholders under the captions “Proposal 2—Ratification of Independent Registered Public Accounting Firm—Audit Fees” and “—Pre-Approval of Services by the Independent Registered Public Accounting Firm” is incorporated herein by reference.

PART IV

ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

(a)(1) Financial Statements

The following documents are filed as part of this Form 10-K.

- (i) Reports of Independent Registered Public Accounting Firms
- (ii) Consolidated Balance Sheets
- (iii) Consolidated Statements of Income
- (iv) Consolidated Statements of Comprehensive Income
- (v) Consolidated Statements of Changes in Shareholders' Equity
- (vi) Consolidated Statements of Cash Flows
- (vii) Notes to Consolidated Financial Statements

(a)(2) Financial Statement Schedules

None.

(a)(3) Exhibits

- 3.1 Articles of Organization of Provident Bancorp, Inc. (incorporated by reference to Exhibit 3.1 to the Registration Statement on Form S-1 of Provident Bancorp, Inc. (file no. 333-232018), initially filed with the Securities and Exchange Commission on June 7, 2019)
- 3.2 Bylaws of Provident Bancorp, Inc. (incorporated by reference to Exhibit 3.2 to the Registration Statement on Form S-1 of Provident Bancorp, Inc. (file no. 333-232018), initially filed with the Securities and Exchange Commission on June 7, 2019)
- 3.3 Amendment to Bylaws of Provident Bancorp, Inc. (incorporated by reference to the Company's Current Report on Form 8-K (file no. 001-39090), filed with the Securities and Exchange Commission on March 29, 2021.
- 4.1 Form of Common Stock Certificate of Provident Bancorp, Inc. (incorporated by reference to Exhibit 4 to the Registration Statement on Form S-1 of Provident Bancorp, Inc. (file no. 333-232018), initially filed with the Securities and Exchange Commission on June 7, 2019)
- 4.2 Description of registrant's securities (incorporated by reference to Exhibit 4.2 to the Annual Report on Form 10-K of Provident Bancorp, Inc. for the year ended December 31, 2019 (file no. 001-39090), filed by the Company under the Exchange Act on March 13, 2020)
- 10.1 Employment Agreement with David P. Mansfield † (incorporated by reference to Exhibit 10.2 to the Registration Statement on Form S-1 of Provident Bancorp, Inc. (file no. 333-202716), initially filed with the Securities and Exchange Commission on March 13, 2015)
- 10.2 Employment Agreement with Carol L. Houle † (incorporated by reference to Exhibit 10.4 to the Registration Statement on Form S-1 of Provident Bancorp, Inc. (file no. 333-202716), initially filed with the Securities and Exchange Commission on March 13, 2015)
- 10.3 Amended and Restated Supplemental Executive Retirement Agreement with David P. Mansfield † (incorporated by reference to Exhibit 10.5 to the Registration Statement on Form S-1 of Provident Bancorp, Inc. (file no. 333-202716), initially filed with the Securities and Exchange Commission on March 13, 2015)
- 10.4 Amended and Restated Supplemental Executive Retirement Agreement with Charles F. Withee † (incorporated by reference to Exhibit 10.6 to the Registration Statement on Form S-1 of Provident Bancorp, Inc. (file no. 333-202716), initially filed with the Securities and Exchange Commission on March 13, 2015)
- 10.5 Supplemental Executive Retirement Agreement with Carol L. Houle † (incorporated by reference to Exhibit 10.7 to the Registration Statement on Form S-1 of Provident Bancorp, Inc. (file no. 333-202716), initially filed with the Securities and Exchange Commission on March 13, 2015)
- 10.6 The Provident Bank Executive Annual Incentive Plan † (incorporated by reference to Exhibit 10.8 to the Registration Statement on Form S-1 of Provident Bancorp, Inc. (file no. 333-202716), initially filed with the Securities and Exchange Commission on March 13, 2015)

- 10.7 The Provident Bank 2005 Amended and Restated Long-Term Incentive Plan † (incorporated by reference to Exhibit 10.9 to the Registration Statement on Form S-1 of Provident Bancorp, Inc. (file no. 333-202716), initially filed with the Securities and Exchange Commission on March 13, 2015)
- 10.8 Provident Bancorp, Inc. 2016 Equity Incentive Plan† (incorporated by reference to Appendix A to the definitive proxy statement for the Special Meeting of Shareholders of Provident Bancorp, Inc. (File No. 001-37504), filed by the Company under the Exchange Act on August 9, 2016)
- 10.9 Form of Incentive Stock Option Award Agreement† (incorporated by reference to Exhibit 10.2 to the Registration Statement on Form S-8 (File No. 333-214702), filed with the Securities and Exchange Commission on November 18, 2016)
- 10.10 Form of Non-Statutory Incentive Stock Option Award Agreement† (incorporated by reference to Exhibit 10.3 to the Registration Statement on Form S-8 (File No. 333-214702), filed with the Securities and Exchange Commission on November 18, 2016)
- 10.11 Form of Restricted Stock Award Agreement† (incorporated by reference to Exhibit 10.4 to the Registration Statement on Form S-8 (File No. 333-214702), filed with the Securities and Exchange Commission on November 18, 2016)
- 10.12 First Amendment to Employment Agreement with David P. Mansfield† (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K of Provident Bancorp, Inc. (File No. 001-37504), filed by the Company under the Exchange Act on December 26, 2018)
- 10.13 First Amendment to Employment Agreement with Carol L. Houle† (incorporated by reference to Exhibit 10.3 to the Current Report on Form 8-K of Provident Bancorp, Inc. (File No. 001-37504), filed by the Company under the Exchange Act on December 26, 2018)
- 10.14 Provident Bancorp, Inc. 2020 Equity Incentive Plan (incorporated by reference to Appendix A to the proxy statement for the Special Meeting of Shareholders of Provident Bancorp, Inc. (file no. 001-39090), filed by the Company under the Exchange Act on October 19, 2020)
- 10.15 Amendment One to the Amended and Restated Supplemental Executive Retirement Agreement for David P. Mansfield† (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K of Provident Bancorp, Inc. (File No. 001-39090), filed under the Exchange Act on December 23, 2020)
- 10.16 Amendment One to the Amended and Restated Supplemental Executive Retirement Agreement for Charles F. Withee† (incorporated by reference to Exhibit 10.2 to the Current Report on Form 8-K of Provident Bancorp, Inc. (File No. 001-39090), filed under the Exchange Act on December 23, 2020)
- 10.17 Deferred Cash Bonus Agreement with David P. Mansfield† (incorporated by reference to Exhibit 10.3 to the Current Report on Form 8-K of Provident Bancorp, Inc. (File No. 001-39090), filed under the Exchange Act on December 23, 2020)
- 10.18 Employment Agreement with Charles F. Withee† (incorporated by reference to Exhibit 10.4 to the Current Report on Form 8-K of Provident Bancorp, Inc. (File No. 001-39090), filed under the Exchange Act on December 23, 2020)
- 10.19 Form of Incentive Stock Option Award Agreement† (incorporated by reference to Exhibit 10.2 to the Registration Statement on Form S-8 (File No. 333-250886), filed with the Securities and Exchange Commission on November 23, 2020)
- 10.20 Form of Non-Qualified Stock Options Award Agreement† (incorporated by reference to Exhibit 10.3 to the Registration Statement on Form S-8 (File No. 333-250886), filed with the Securities and Exchange Commission on November 23, 2020)
- 10.21 Form of Restricted Stock Award Agreement† (incorporated by reference to Exhibit 10.4 to the Registration Statement on Form S-8 (File No. 333-250886), filed with the Securities and Exchange Commission on November 23, 2020)
- 10.22 Resignation, Separation Agreement and Full and Final Release of Claims with Charles F. Withee† (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K of Provident Bancorp, Inc. (File No. 001-39090), filed under the Exchange Act on November 4, 2021)
- 10.23 Employment Agreement with Joseph Mancini†
- 21 Subsidiaries of the Registrant (incorporated by reference to Exhibit 21 to the Registration Statement on Form S-1 of Provident Bancorp, Inc. (file no. 333-232018), initially filed with the Securities and Exchange Commission on June 7, 2019)
- 23.1 Consent of Independent Registered Public Accounting Firm (Crowe LLP)
- 31.1 Certification of Chief Executive Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 31.2 Certification of Chief Financial Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 32 Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 101 The following financial statements from Provident Bancorp, Inc.'s Annual Report on Form 10-K for the year ended December 31, 2021, filed on March 24, 2022, formatted in XBRL: (i) Consolidated Balance Sheets, (ii) Consolidated Statements of Income, (iii) Consolidated Statements of Comprehensive Income, (iv) Consolidated Statements of Changes in Shareholders' Equity, (v) Consolidated Statements of Cash Flows, and (vi) the Notes to Consolidated Financial Statements.

† Compensatory arrangements.

ITEM 16. FORM 10-K SUMMARY

None.

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.

PROVIDENT BANCORP, INC.

Date: March 24, 2022

/s/ David P. Mansfield
David P. Mansfield
President and Chief Executive 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.

<u>Signatures</u>	<u>Title</u>	<u>Date</u>
<u>/s/ David P. Mansfield</u> David P. Mansfield	President, Chief Executive Officer and Director (Principal Executive Officer)	March 24, 2022
<u>/s/ Carol L. Houle</u> Carol L. Houle	Executive Vice President and Chief Financial Officer (Principal Financial and Accounting Officer)	March 24, 2022
<u>/s/ Frank G. Cousins, Jr.</u> Frank G. Cousins, Jr.	Director	March 24, 2022
<u>/s/ James A. DeLeo</u> James A. DeLeo	Director	March 24, 2022
<u>/s/ Lisa B. DeStefano</u> Lisa B. DeStefano	Director	March 24, 2022
<u>/s/ Jay E. Gould</u> Jay E. Gould	Director	March 24, 2022
<u>/s/ Laurie H. Knapp</u> Laurie H. Knapp	Director	March 24, 2022
<u>/s/ Barbara A. Piette</u> Barbara A. Piette	Director	March 24, 2022
<u>/s/ Joseph B. Reilly</u> Joseph B. Reilly	Director	March 24, 2022
<u>/s/ Arthur W. Sullivan</u> Arthur W. Sullivan	Director	March 24, 2022
<u>/s/ Kathleen Chase Curran</u> Kathleen Chase Curran	Director	March 24, 2022
<u>/s/ Mohammad Shaikh</u> Mohammad Shaikh	Director	March 24, 2022

PROVIDENT BANCORP, INC. AND SUBSIDIARY

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Shareholders and the Board of Directors of Provident Bancorp, Inc. and Subsidiary
Amesbury, Massachusetts

Opinion on the Financial Statements

We have audited the accompanying consolidated balance sheets of Provident Bancorp, Inc. and Subsidiary (the "Company") as of December 31, 2021 and 2020, the related consolidated statements of income, comprehensive income, changes in stockholders' equity, and cash flows for each of the years in the two-year period ended December 31, 2021, 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 as of December 31, 2021 and 2020, and the results of its operations and its cash flows for each of the years in the two-year period ended December 31, 2021, 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 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 provide a reasonable basis for our opinion.

Critical Audit Matter

The critical audit matter communicated below is a matter arising from the current period audit of the financial statements that was communicated or required to be communicated to the audit committee and that: (1) relates to accounts or disclosures that are material to the financial statements and (2) involved our especially challenging, subjective, or complex judgments. The communication of the critical audit matter 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 below, providing a separate opinion on the critical audit matter or on the accounts or disclosures to which it relates.

Allowance for Loan Losses – Qualitative Factors

The allowance for loan losses is a valuation allowance for probable incurred credit losses as described in the notes to the consolidated financial statements. Refer to Note 2 – *Accounting Policies* for the Company's accounting policy related to the allowance for loan losses and Note 5 – *Loans* for the Company's disclosures related to loans and the associated allowance for loan losses. The Company has identified the allowance for loan losses as a critical accounting estimate. The allowance consists of specific and general components. The specific component relates to loans that are individually classified as impaired when, based on current information and events, it is probable that the Company will be unable to collect all amounts due according to the contractual terms of the loan agreement. The general component of the allowance for loan losses is based on historical loss experience adjusted for qualitative factors stratified by all loan segments.

The determination of the qualitative factors is subjective and subject to measurement uncertainty. We considered auditing the qualitative factors of the allowance for loan losses to be a critical audit matter due to the high degree of auditor effort and judgment involved in evaluating management's judgments applied in the determination of qualitative factors.

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

- Substantively testing management’s process to estimate the qualitative factors of the allowance for loan losses including testing:
 - The relevance and reliability of the data utilized in the determination of the qualitative factors.
 - The mathematical accuracy of the allowance for loan loss calculation, including the qualitative factors.
 - The reasonableness of management’s judgments and significant assumptions used in the development of the qualitative factors.

We have served as the Company's auditor since 2020.

/s/ Crowe LLP

Boston, Massachusetts

March 24, 2022

PROVIDENT BANCORP, INC.
CONSOLIDATED BALANCE SHEETS
December 31, 2021 and 2020

(In thousands)	2021	2020
Assets		
Cash and due from banks	\$ 22,470	\$ 11,830
Short-term investments	130,645	71,989
Cash and cash equivalents	153,115	83,819
Debt securities available-for-sale (at fair value)	36,837	32,215
Federal Home Loan Bank stock, at cost	785	895
Loans held for sale	22,846	—
Loans, net of allowance for loan losses of \$19,496 and \$18,518 as of December 31, 2021 and 2020, respectively	1,433,803	1,314,810
Bank owned life insurance	42,569	36,684
Premises and equipment, net	14,258	14,716
Accrued interest receivable	5,703	6,371
Right-of-use assets	4,102	4,258
Other assets	15,265	12,013
Total assets	\$ 1,729,283	\$ 1,505,781
Liabilities and Shareholders' Equity		
Deposits:		
Noninterest-bearing	\$ 626,587	\$ 383,079
Interest-bearing	833,308	854,349
Total deposits	1,459,895	1,237,428
Long-term borrowings	13,500	13,500
Operating lease liabilities	4,387	4,488
Other liabilities	17,719	14,509
Total liabilities	1,495,501	1,269,925
Shareholders' equity:		
Preferred stock; authorized 50,000 shares: no shares issued and outstanding	—	—
Common stock, \$0.01 par value, 100,000,000 shares authorized; 17,854,649 and 19,047,544 shares issued and outstanding at December 31, 2021 and 2020, respectively	179	191
Additional paid in capital	123,498	139,450
Retained earnings	118,087	104,508
Accumulated other comprehensive income	649	1,058
Unearned compensation - ESOP	(8,631)	(9,351)
Total shareholders' equity	233,782	235,856
Total liabilities and shareholders' equity	\$ 1,729,283	\$ 1,505,781

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

PROVIDENT BANCORP, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF INCOME
For the Years Ended December 31, 2021 and 2020

(In thousands)	2021	2020
Interest and dividend income:		
Interest and fees on loans	\$ 63,873	\$ 59,391
Interest and dividends on debt securities available-for-sale	722	913
Interest on short-term investments	208	99
Total interest and dividend income	<u>64,803</u>	<u>60,403</u>
Interest expense:		
Interest on deposits	3,085	5,203
Interest on borrowings	285	728
Total interest expense	<u>3,370</u>	<u>5,931</u>
Net interest and dividend income	61,433	54,472
Provision for loan losses	3,887	5,597
Net interest and dividend income after provision for loan losses	<u>57,546</u>	<u>48,875</u>
Noninterest income:		
Customer service fees on deposit accounts	1,832	1,331
Service charges and fees - other	2,003	1,322
Bank owned life insurance	1,195	809
Other income	136	81
Total noninterest income	<u>5,166</u>	<u>3,543</u>
Noninterest expense:		
Salaries and employee benefits	28,782	23,175
Occupancy expense	1,687	1,684
Equipment expense	514	577
Deposit insurance	482	416
Data processing	1,325	1,000
Marketing expense	279	223
Professional fees	2,083	1,868
Directors' compensation	992	750
Software depreciation and implementation	1,014	959
Write down of other assets and receivables	225	2,207
Other	3,236	2,949
Total noninterest expense	<u>40,619</u>	<u>35,808</u>
Income before income tax expense	22,093	16,610
Income tax expense	5,954	4,625
Net income	<u>\$ 16,139</u>	<u>\$ 11,985</u>
Earnings per share:		
Basic	\$ 0.96	\$ 0.66
Diluted	\$ 0.93	\$ 0.66
Weighted Average Shares:		
Basic	16,772,628	18,090,229
Diluted	17,302,007	18,131,025

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

PROVIDENT BANCORP, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
For the Years Ended December 31, 2021 and 2020

(In thousands)	2021	2020
Net income	\$ 16,139	\$ 11,985
Other comprehensive income:		
Unrealized holding (loss) gain on available-for-sale securities	(548)	805
Unrealized (loss) gain	(548)	805
Income tax effect	139	(205)
Other comprehensive (loss) income, net of tax	(409)	600
Total comprehensive income	\$ 15,730	\$ 12,585

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

PROVIDENT BANCORP, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
For the Years Ended December 31, 2021 and 2020

(In thousands, except share data)	Shares of Common Stock	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income	Unearned Compensation ESOP	Total
Balance, December 31, 2019	19,473,818	\$ 195	\$ 146,174	\$ 94,159	\$ 458	\$ (10,053)	\$ 230,933
Net income	—	—	—	11,985	—	—	11,985
Dividends declared (\$0.09 per share)	—	—	—	(1,636)	—	—	(1,636)
Other comprehensive income	—	—	—	—	600	—	600
Stock-based compensation	—	—	1,089	—	—	—	1,089
Restricted stock award grants net of forfeitures	311,769	3	(3)	—	—	—	—
Repurchase of common stock	(724,741)	(7)	(7,818)	—	—	—	(7,825)
Shares surrendered related to tax withholdings on restricted stock awards	(13,302)	—	(131)	—	—	—	(131)
ESOP shares earned	—	—	139	—	—	702	841
Balance, December 31, 2020	19,047,544	191	139,450	104,508	1,058	(9,351)	235,856
Net income	—	—	—	16,139	—	—	16,139
Dividends declared (\$0.15 per share)	—	—	—	(2,560)	—	—	(2,560)
Other comprehensive loss	—	—	—	—	(409)	—	(409)
Stock-based compensation	—	—	2,545	—	—	—	2,545
Restricted stock award grants net of forfeitures	21,320	—	—	—	—	—	—
Repurchase of common stock	(1,240,304)	(12)	(18,336)	—	—	—	(18,348)
Stock options exercised, net	58,392	—	(241)	—	—	—	(241)
Shares surrendered related to tax withholdings on restricted stock awards	(32,303)	—	(614)	—	—	—	(614)
ESOP shares earned	—	—	694	—	—	720	1,414
Balance, December 31, 2021	<u>17,854,649</u>	<u>\$ 179</u>	<u>\$ 123,498</u>	<u>\$ 118,087</u>	<u>\$ 649</u>	<u>\$ (8,631)</u>	<u>\$ 233,782</u>

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

PROVIDENT BANCORP, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS
For the Years Ended December 31, 2021 and 2020

(In thousands)	2021	2020
Cash flows from operating activities:		
Net income	\$ 16,139	\$ 11,985
Adjustments to reconcile net income to net cash provided by operating activities:		
Amortization of securities premiums, net of accretion	181	266
ESOP expense	1,414	841
Change in deferred loan fees, net	(123)	2,023
Provision for loan losses	3,887	5,597
Depreciation and amortization	1,026	1,091
Decrease (increase) in accrued interest receivable	668	(3,267)
Deferred tax benefit	(578)	(2,202)
Share-based compensation expense	2,545	1,089
Bank-owned life insurance income	(1,195)	(809)
Principal payments on operating lease liabilities	(101)	(82)
Increase in other assets	(2,760)	(785)
Increase in other liabilities	3,210	2,434
Net cash provided by operating activities	<u>24,313</u>	<u>18,181</u>
Cash flows from investing activities:		
Purchases of debt securities available-for-sale	(13,626)	—
Proceeds from pay downs, maturities and calls of debt securities available-for-sale	8,275	10,114
Redemption of Federal Home Loan Bank stock	110	521
Loan originations and purchases, net of paydowns	(145,603)	(296,472)
Cash paid for mortgage warehouse asset purchase, net	—	(66,962)
Additions to premises and equipment	(412)	(911)
Purchase of bank owned life insurance	(5,500)	(8,950)
Proceeds from distribution of bank owned life insurance	810	—
Write down of other assets and receivables	225	2,207
Net cash used in investing activities	<u>(155,721)</u>	<u>(360,453)</u>

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

PROVIDENT BANCORP, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS (CONTINUED)
For the Years Ended December 31, 2021 and 2020

(In thousands)	2021	2020
Cash flows from financing activities:		
Net increase in noninterest-bearing accounts	243,508	160,991
Net (decrease) increase in interest-bearing accounts	(21,041)	226,532
Cash dividends paid on common stock	(2,560)	(1,636)
Proceeds from exercise of stock options, net	(241)	—
Payments made on Federal Home Loan Bank long-term advances	—	(11,498)
Shares surrendered related to tax withholdings on restricted stock awards	(614)	(131)
Repurchase of common stock	(18,348)	(7,825)
Net cash provided by financing activities	<u>200,704</u>	<u>366,433</u>
Net increase in cash and cash equivalents	69,296	24,161
Cash and cash equivalents at beginning of year	83,819	59,658
Cash and cash equivalents at end of year	<u>\$ 153,115</u>	<u>\$ 83,819</u>
Supplemental disclosures:		
Interest paid	\$ 3,085	\$ 5,932
Income taxes paid	8,379	6,264
Transfer from loans to loans held for sale	22,846	—
Recognition of right-of-use assets in premises and equipment	—	693
Recognition of operating lease liabilities	—	693
Reclassification of premises and equipment to other assets	—	3

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 — NATURE OF OPERATIONS

Provident Bancorp, Inc. (the “Company”) is a Maryland corporation that was incorporated in June 2019 to be the successor corporation to Provident Bancorp, Inc. (“Old Provident”), a Massachusetts corporation, upon completion of the second-step mutual-to-stock conversion (the “Conversion”) of Provident Bancorp (the “MHC”), the top tier mutual holding company of Old Provident. Old Provident was the former mid-tier holding company for The Provident Bank (“BankProv” or the “Bank”). Prior to completion of the Conversion, approximately 52% of the shares of common stock of Old Provident were owned by the MHC. In conjunction with the Conversion, the MHC was merged into the Company (and ceased to exist) and the Company became its successor under the name Provident Bancorp, Inc. The Conversion was completed on October 16, 2019. The Company raised gross proceeds of \$102.1 million by selling 10,212,397 shares of common stock at \$10.00 per share in the second-step stock offering. The Company utilized \$8.2 million of the proceeds to lend to its Employee Stock Ownership Plan (the “ESOP”) for the acquisition of an additional 816,992 shares at \$10.00 per share. Expenses incurred related to the offering were \$2.4 million, and were recorded against offering proceeds. The Company invested \$45.8 million of the net proceeds it received from the sale into the Bank’s operations and has retained the remaining amount for general corporate purposes. Concurrent with the completion of the stock offering, each share of Old Provident common stock owned by public stockholders (stockholders other than the MHC) was exchanged for 2.0212 shares of Company common stock. A total of 19,484,343 shares of common stock were outstanding following the completion of the stock offering.

The Bank, headquartered in Amesbury, Massachusetts, operates its business from seven banking offices located in Amesbury and Newburyport, Massachusetts and Portsmouth, Exeter, Bedford, and Seabrook, New Hampshire. The Bank also has loan production offices in Boston, Massachusetts and Ponte Vedra, Florida. The Bank provides a variety of financial services to small businesses and individuals. Its primary deposit products are checking, savings and term certificate accounts and its primary lending products are commercial mortgages, commercial loans and mortgage warehouse loans.

NOTE 2 — ACCOUNTING POLICIES

The accounting and reporting policies of the Company conform to accounting principles generally accepted in the United States of America (“GAAP”) and predominant practices within the banking industry. The consolidated financial statements were prepared using the accrual basis of accounting.

Use of Estimates

To prepare financial statements in conformity with GAAP management makes estimates and assumptions based on available information. These estimates and assumptions affect the amounts reported in the financial statements and the disclosures provided, and actual results could differ.

Basis of Presentation

The consolidated financial statements include the accounts of Provident Bancorp, Inc., its wholly owned subsidiary, the Bank, and the Bank’s wholly owned subsidiaries, Provident Security Corporation and 5 Market Street Security Corporation. Provident Security Corporation and 5 Market Street Security Corporation were established to buy, sell, and hold investments for their own account. All material intercompany balances and transactions have been eliminated in consolidation.

Significant Concentrations of Credit Risk

The primary lending area for the includes Northeastern Massachusetts and Southern New Hampshire, with a focus on Essex County, Massachusetts, and Hillsborough and Rockingham Counties, New Hampshire, which are part of, and bedroom communities to, the technology corridor between Boston, Massachusetts and Concord, New Hampshire. In 2018, the Bank started offering its enterprise value loan product nationally. In 2020, the Bank purchased a warehouse lending business located in Ponte Vedra, Florida that targets national credit worthy, small to mid-cap non-bank mortgage origination companies for facility lines. The primary deposit-gathering area is currently concentrated in Essex County, Massachusetts, and Rockingham County and Hillsborough County, New Hampshire. The Company believes that it does not have any significant loan concentrations or investment securities in any one industry or with any customer.

Reclassification

Certain amounts in the prior year have been reclassified to be consistent with the current year's consolidated financial statement presentation, and the reclassifications had no effect on the net income reported in the consolidated statements of income.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Cash and Cash Equivalents

Cash and cash equivalents include cash, and deposits with other financial institutions with maturities fewer than 90 days. Net cash flows are reported for customer loan and deposit transactions and interest-bearing deposits in other financial institutions.

Debt Securities

Debt securities are classified as held to maturity and carried at amortized cost when management has the positive intent and ability to hold them to maturity. Debt securities are classified as available-for-sale when they might be sold before maturity. Debt securities available-for-sale are carried at fair value, with unrealized holding gains and losses reported in other comprehensive income, net of tax.

Interest income includes amortization of purchase premium or discount. Premiums and discounts on securities are amortized on the level-yield method without anticipating prepayments, except for mortgage backed securities where prepayments are anticipated. Gains and losses on sales are recorded on the trade date and determined using the specific identification method.

The Company evaluates debt securities for other-than-temporary impairment (“OTTI”) on at least a quarterly basis, and more frequently when economic or market conditions warrant such an evaluation. For debt securities in an unrealized loss position, management considers the extent and duration of the unrealized loss, and the financial condition and near-term prospects of the issuer. The Company also assesses whether it intends to sell, or it is more likely than not that it will be required to sell, a debt security in an unrealized loss position before recovery of its amortized cost basis. If either of the criteria regarding intent or requirement to sell is met, the entire difference between amortized cost and fair value is recognized as impairment through earnings.

For debt securities that do not meet the aforementioned criteria, the amount of impairment is split into two components as follows: 1) OTTI related to credit loss, which must be recognized in the income statement and 2) OTTI related to other factors, which is recognized in other comprehensive income. The credit loss is defined as the difference between the present value of the cash flows expected to be collected and the amortized cost basis.

Federal Home Loan Bank Stock

As a member of the Federal Home Loan Bank of Boston (the “FHLB”), the Company is required to invest in \$100 par value stock of the FHLB. The FHLB capital structure mandates that members own stock as determined by their Total Stock Investment Requirement which is the sum of a member’s Membership Stock Investment Requirement and Activity-Based Stock Investment Requirement. FHLB stock is 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 Held for Sale

Loans originated and intended for sale are carried at the lower of cost or estimated fair value in the aggregate. Net unrealized losses, if any, are recognized through a valuation allowance by charges to income. As of December 31, 2021, we transferred our salable residential real estate loan portfolio to held for sale.

Loans

Loan receivables that management has the intent and ability to hold until maturity or payoff are reported at their outstanding principal balances adjusted for amounts due to borrowers on unadvanced loans, any charge-offs, the allowance for loan losses and any deferred fees or costs on originated loans, or unamortized premiums or discounts on purchased loans.

Interest income is accrued on the unpaid principal balance.

Loan origination and commitment fees and certain direct origination costs are deferred, and the net amount is recognized as an adjustment of the related loan yield using the interest method. The Company is amortizing these amounts over the contractual life of the related loans.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Commercial real estate loans and commercial business loans and leases which are 90 days or more past due are generally placed on non-accrual status, unless secured by sufficient cash or other assets immediately convertible to cash. Residential real estate loans are generally placed on non-accrual status when reaching 90 days past due. Past due status is based on the contractual terms of the loan. All closed-end consumer loans 90 days or more past due and any equity line in the process of foreclosure are placed on non-accrual status. Secured consumer loans are written down to realizable value and unsecured consumer loans are charged-off upon reaching 120 or 180 days past due depending on the type of loan. When a loan has been placed on non-accrual status, previously accrued and uncollected interest is reversed against interest on loans. A loan can be returned to accrual status when collectability of principal is reasonably assured and the loan has performed for a period of time, generally six months. Interest income received on non-accrual loans is accounted for on the cash basis or cost-recovery method, until qualifying for return to accrual.

Cash receipts of interest income on impaired loans are credited to principal to the extent necessary to eliminate doubt as to the collectability of the net carrying amount of the loan. Some or all of the cash receipts of interest income on impaired loans is recognized as interest income if the remaining net carrying amount of the loan is deemed to be fully collectible. When recognition of interest income on an impaired loan on a cash basis is appropriate, the amount of income that is recognized is limited to that which would have been accrued on the net carrying amount of the loan at the contractual interest rate. Any cash interest payments received in excess of the limit and not applied to reduce the net carrying amount of the loan are recorded as recoveries of charge-offs until the charge-offs are fully recovered.

Troubled debt restructurings: Loans are considered to be troubled debt restructurings (“TDRs”) when the Company has granted concessions to a borrower due to the borrower’s financial condition that it otherwise would not have considered. These concessions may include modifications of the terms of the debt such as deferral of payments, extension of maturity, reduction of principal balance, reduction of the stated interest rate other than normal market rate adjustments, or a combination of these concessions. Debt may be bifurcated with separate terms for each tranche of the restructured debt. Restructuring of a loan in lieu of aggressively enforcing the collection of the loan may benefit the Company by increasing the ultimate probability of collection.

Restructured loans are classified as accruing or non-accruing based on management’s assessment of the collectability of the loan. Loans which are already on nonaccrual status at the time of the restructuring generally remain on non-accrual status for approximately six months before management considers such loans for return to accruing status. Accruing restructured loans are placed into non-accrual status if and when the borrower fails to comply with the restructured terms and management deems it unlikely that the borrower will return to a status of compliance in the near term.

Loan modifications and payment deferrals as a result of COVID-19 that meet the criteria established under Section 4013 of the CARES Act or under applicable interagency guidance of the federal banking regulators are excluded from evaluation of TDR classification and will continue to be reported as current during the payment deferral period. The Company’s policy is to continue to accrue interest during the deferral period. The Company continues to monitor the accrued interest receivable related to these loan modifications for collectability. Loans not meeting the CARES Act or regulatory guidance are evaluated for TDR and non-accrual treatment under the Company’s existing policies and procedures.

Allowance for Loan Losses

The allowance for loan losses is a valuation allowance for probable incurred credit losses. Loan losses are charged against the allowance when management believes the uncollectability of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance. Management estimates the allowance balance required using past loan loss experience, the size and composition of the portfolio, information about specific borrower situations and estimated collateral values, economic conditions, and other factors. Allocations of the allowance may be made for specific loans, but the entire allowance is available for any loan that, in management’s judgment, should be charged off.

The allowance consists of specific and general components. The specific component relates to loans that are individually classified as impaired when, based on current information and events, it is probable that the Company will be unable to collect all amounts due according to the contractual terms of the loan agreement. Loans for which the terms have been modified resulting in a concession, and for which the borrower is experiencing financial difficulties, are considered troubled debt restructurings (“TDRs”) and are classified as impaired.

The Company classifies a loan as impaired when, based on current information and events, it is probable that it will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower’s prior payment record, and the amount of the shortfall in relation to the principal and interest owed.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Large groups of smaller balance homogeneous loans are collectively evaluated for impairment. Accordingly, we do not separately identify individual consumer and residential loans for impairment disclosures.

The allocated component relates to loans that are classified as impaired. Impairment is measured on a loan by loan basis for commercial, commercial real estate and construction loans by either the present value of expected future cash flows discounted at the loan's effective interest rate or the fair value of the collateral if the loan is collateral dependent. An allowance is established when the discounted cash flows (or collateral value) of the impaired loan is lower than the carrying value of that loan.

Troubled debt restructurings are individually evaluated for impairment and included in the separately identified impairment disclosures. TDRs are measured at the present value of estimated future cash flows using the loan's effective rate at inception. If a TDR is considered to be a collateral dependent loan, the loan is reported, net, at the fair value of the collateral. For TDRs that subsequently default, the Company determines the amount of the allowance on that loan in accordance with the accounting policy for the allowance for loan losses on loans individually identified as impaired.

The general component of the allowance for loan losses is based on historical loss experience adjusted for qualitative factors stratified by all loan segments. Management uses a rolling average of historical losses based on a time frame appropriate to capture relevant loss data for each loan segment. The historical loss factors are adjusted for the following qualitative factors: levels/trends in delinquencies and non-accruals, economic conditions, portfolio trends, portfolio concentrations, loan grading and management's discretion. The determination of qualitative factors involves significant judgment.

The allowance for loan loss is determined based on the various risk characteristics of each loan segment. Risk characteristics relevant to each portfolio segment are as follows:

Commercial real estate: Loans in this segment are primarily income-producing properties throughout Massachusetts and New Hampshire. The underlying cash flows generated by the properties are adversely impacted by a downturn in the economy as evidenced by increased vacancy rates, which in turn, will have an effect on the credit quality in this segment. Management periodically obtains rent rolls and continually monitors the cash flows of these loans.

Commercial: Loans in this segment are made to businesses and are generally secured by assets of the business. Also included in this segment are loans to digital asset customers which are secured by digital mining asset equipment or by the United States dollar ("USD") value of the digital currency. Repayment is expected from the cash flows of the business. A weakened economy, and resultant decreased consumer spending, will have an effect on the credit quality in this segment.

Residential real estate: The Company generally does not originate loans with a loan-to-value ratio greater than 80% and does not grant subprime loans. Loans with loan to value ratios greater than 80% require the purchase of private mortgage insurance. All loans in this segment are collateralized by owner-occupied residential real estate and repayment is dependent on the credit quality of the individual borrower. The overall health of the economy, including unemployment rates and housing prices, will have an effect on the credit quality in this segment. In December 2021, we transferred the salable loans in this portfolio to held for sale.

Construction and land development: Loans in this segment primarily include speculative and pre-sold real estate development loans for which payment is derived from sale of the property and a conversion of the construction loans to permanent loans for which payment is then derived from cash flows of the property. Credit risk is affected by cost overruns, time to sell at an adequate price, and market conditions.

Consumer: Loans in this segment are generally unsecured and repayment is dependent on the credit quality of the individual borrower.

Mortgage warehouse: Loans in this segment are primarily facility lines to non-bank mortgage origination companies. The underlying collateral of these loans are residential real estate loans. Loans are originated by the mortgage companies for sale into secondary markets, which is typically within 15 days of the loan funding. The primary source of repayment is the cash flow upon the sale of the loans. The credit risk associated with this type of lending is the risk that the mortgage companies are unable to sell the loans.

An unallocated component can be maintained to cover uncertainties that could affect management's estimate of probable losses. The unallocated component of the allowance reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating allocated and general reserves in the portfolio.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Bank Owned Life Insurance

Bank owned life insurance policies are reflected on the consolidated balance sheets at cash surrender value. Changes in the net cash surrender value of the policies, as well as insurance proceeds received, are reflected in non-interest income on the consolidated statements of income and are not subject to income taxes.

Premises and Equipment

Premises and equipment are stated at cost, less accumulated depreciation and amortization. Cost and related allowances for depreciation and amortization of premises and equipment retired or otherwise disposed of are removed from the respective accounts with any gain or loss included in income or expense. Depreciation on building and leasehold improvements is calculated primarily using the straight-line method with useful lives of seven to 40 years. Furniture and fixtures are depreciated using the straight-line method with useful lives of one to 15 years. Computer equipment is also depreciated using the straight-line method with useful lives ranging from two to five years.

Other Real Estate Owned and Repossessed Assets

Assets acquired through, or in lieu of, loan foreclosure or repossession are held for sale and are initially recorded at the lower of the investment in the loan or fair value less estimated costs to sell at the date of foreclosure or repossession, establishing a new cost basis. Subsequently, valuations are periodically performed by management and the assets are carried at the lower of carrying amount or fair value less estimated costs to sell. Revenue and expenses from operations, changes in the valuation allowance, any direct write-downs and gains or losses on sales are included in other real estate owned expense.

Revenue Recognition

Revenue from contracts with customers in the scope of Accounting Standards Codification (“ASC”) (“Topic 606”) is measured based on the consideration specified in the contract with a customer and excludes amounts collected on behalf of third parties. The Company recognizes revenue from contracts with customers when it satisfies its performance obligations.

The Company’s performance obligations are generally satisfied as services are rendered and can either be satisfied at a point in time or over time. Unsatisfied performance obligations at the report date are not material to our consolidated financial statements.

The Company recognizes revenue that is transactional in nature and such revenue is earned at a point in time. Revenue that is recognized at a point in time includes card interchange fees (fee income related to debit card transactions), ATM fees, wire transfer fees, overdraft charge fees, and stop-payment and returned check fees. Additionally, revenue is collected from loan fees, such as letters of credit, line renewal fees and application fees. Such revenue is derived from transactional information and is recognized as revenue immediately as the transactions occur or upon providing the service to complete the customer’s transaction.

Leases

The Company determines if an arrangement is a lease at inception. Lease right-of-use (“ROU”) assets represent the Company’s right to use an underlying asset for the lease term and operating lease liabilities represent the Company’s obligation to make lease payments arising from the lease. Lease ROU assets and lease liabilities are recognized at commencement date based on the present value of lease payments over the lease term. As the Company’s leases do not provide an implicit rate, the Company uses its incremental borrowing rate based on the information available at commencement date in determining the present value of lease payments. The lease ROU asset also includes any lease payments made and excludes lease incentives. The lease terms may include options to extend or terminate the lease when it is reasonably certain that the Company will exercise that option. Lease expense for lease payments is recognized on a straight-line basis over the lease term. The Company has lease agreements with lease and non-lease components, which are generally accounted for separately.

Advertising

The Company directly expenses costs associated with advertising as they are incurred.

Earnings per Share

Basic earnings per common share is net income divided by the weighted average number of common shares outstanding during the period. ESOP shares are considered outstanding for this calculation unless unallocated. Diluted earnings per common share includes the dilutive effect of additional potential common shares issuable under stock options. Earnings and dividends per share are restated for all stock splits and stock dividends through the date of issuance of the financial statements, if applicable.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The Company's unvested share-based payment awards do not contain rights to nonforfeitable dividends and as such are not considered participating.

Employee Stock Ownership Plan

Compensation expense for The Provident Bank Employee Stock Ownership Plan (the "ESOP") is recorded at an amount equal to the shares allocated by the ESOP multiplied by the average fair value of the shares during the period. The Company recognizes compensation expense ratably over the year based upon the Company's estimate of the number of shares expected to be allocated by the ESOP. Unearned compensation applicable to the ESOP is reflected as a reduction of shareholders' equity on the consolidated balance sheets. The difference between the average fair value and the cost of the shares by the ESOP is recorded as an adjustment to additional paid-in-capital.

Stock-based Compensation Plans

The Company measures and recognizes compensation cost relating to stock-based payment transactions based on the grant-date fair value of the equity instruments issued. Stock-based compensation is recognized over the period the employee is required to provide services for the award. The Company uses the Black-Scholes option-pricing model to determine the fair value of stock options granted. The determination of fair value involves a number of significant estimates, which require a number of assumptions to determine the model inputs. The fair value of restricted stock is recorded based on the grant date value of the equity instrument issued.

Income Taxes

The Company recognizes income taxes under the asset and liability method. Under this method, deferred tax assets and liabilities are established for the temporary differences between the accounting basis and the tax basis of the Company's assets and liabilities at enacted tax rates expected to be in effect when the amounts related to such temporary differences are realized or settled. A tax valuation allowance is established, as needed, to reduce net 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. The Company recognizes interest and/or penalties related to income tax matters in income tax expense.

Comprehensive Income (Loss)

Comprehensive income (loss) consists of net income (loss) and other comprehensive income (loss). Other comprehensive income (loss) includes unrealized gains and losses on debt securities available-for-sale which are also recognized as separate components of equity.

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 now 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 the holding company or by the holding company to shareholders.

Fair Value of Financial Instruments

Fair values of financial instruments are estimated using relevant market and other assumptions, as more fully disclosed in a separate note. Fair value estimates involve uncertainties and matters of significant judgment regarding interest rates, credit risk, prepayments, and other factors, especially in the absence of broad markets for particular items. Changes in assumptions or in market conditions could significantly affect these estimates.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Loan Commitments and Related Financial Instruments

Financial instruments include off-balance sheet credit instruments, such as commitments to make loans and commercial letters of credit, issued to meet customer financing needs. The face amount for these items represents the exposure to loss, before considering customer collateral or ability to repay. Such financial instruments are recorded when they are funded.

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

Recent Accounting Pronouncements

In June 2016, the Financial Accounting Standards Board (“FASB”) issued *Accounting Standards Update (“ASU”) No. 2016-13, Financial Instruments—Credit Losses (Topic 326): “Measurement of Credit Losses on Financial Instruments.”* The ASU changes the impairment model for most financial assets and certain other instruments. For trade and other receivables, held-to-maturity debt securities, loans and other instruments, entities will be required to use a new forward-looking “expected loss” model that will replace the current “incurred loss” model and can result in the earlier recognition of credit losses. For available-for-sale debt securities with unrealized losses, entities will measure credit losses in a manner similar to current practice, except that the losses will be recognized as an allowance. On October 16, 2019, FASB approved a delay on the implementation until January 2023 for smaller reporting companies as defined by the SEC. The amendments in this update will be effective for the Company on January 1, 2023. Early adoption is permitted as of the fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Management is currently evaluating the impact of its pending adoption of this guidance on the Company’s financial statements.

In December 2019, the FASB issued *ASU No. 2019-12, Income Taxes (Topic 740) - Simplifying the Accounting for Income Taxes (“ASU 2019-12”)*. This ASU simplifies the accounting for income taxes and is effective for fiscal years beginning after December 15, 2020, with early adoption permitted. Certain provisions under ASU 2019-12 require prospective application, some require modified retrospective application through a cumulative-effect adjustment to retained earnings as of the beginning of the year of adoption, while other provisions require retrospective application to all periods presented in the consolidated financial statements upon adoption. The Company adopted the provision of ASU 2019-12 effective January 1, 2021 and the adoption did not have a material impact on the Company’s consolidated financial statements.

In March 2020, the FASB issued *ASU No. 2020-04, Reference Rate Reform (Topic 848) - Facilitation of the Effects of Reference Rate Reform on Financial Reporting (“ASU 2020-04”)*, to ease the potential burden in accounting for recognizing the effects of reference rate reform on financial reporting. Such challenges include the accounting and operational implications for contract modifications and hedge accounting. The provisions in ASU 2020-04 provide optional expedients and exceptions for applying GAAP to loan and lease agreements, contracts, hedging relationships, and other transactions affected by reference rate reform. These provisions apply to contract modifications that reference LIBOR or another reference rate expected to be discounted because of reference rate reform. Qualifying modifications of loan agreements should be accounted for by prospectively adjusting the effective interest rate and the modification would be considered "minor" so that any existing unamortized deferred loan origination fees and costs would carry forward and continue to be amortized. Qualifying modifications of lease agreements should be accounted for as a continuation of the existing agreement with no reassessments of the lease classification and the discount rate or remeasurements of lease payments that otherwise would be required for modifications not accounted for as separate contracts. ASU 2020-04 also provides numerous optional expedients for hedge accounting.

ASU 2020-04 is effective as of March 12, 2020 through December 31, 2022, with adoption permitted as of any date from the beginning of an interim period that includes or is subsequent to March 12, 2020, or prospectively from a date within an interim period that includes or is subsequent to March 12, 2020, up to the date that the financial statements are available to be issued. Once elected, the amendments must be applied prospectively for all eligible contract modifications. The Company is currently evaluating the effect that this ASU will have on the Company’s consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

In October 2020, the FASB issued *ASU No. 2020-08, Receivables (Topic 310) – Nonrefundable Fees and Other Costs (“ASU 2020-08”)*, to provide further clarification and update the previously issued guidance in ASU 2017-08, “Receivables - Nonrefundable Fees and Other Costs (Subtopic 310-20) Premium Amortization on Purchased Callable Debt Securities” (“ASU 2017-08”). ASU 2017-08 shortened the amortization period for certain callable debt securities purchased at a premium by requiring that the premium be amortized to the earliest call date. The Company early adopted the provisions of ASU 2017-08, effective January 1, 2017. ASU 2017-08 requires that at each reporting period, to the extent that the amortized cost of an individual callable debt security exceeds the amount repayable by the issuer at the next call date, the excess premium shall be amortized to the next call date. ASU 2020-08 is effective for fiscal years ending after December 15, 2020 and early adoption is not permitted. The provisions under ASU 2020-08 are required to be applied prospectively. The Company adopted the provision of ASU 2020-08 effective January 1, 2021 and the adoption did not have a material impact on the consolidated financial statements.

NOTE 3 – RISKS AND UNCERTAINTIES

The outbreak of COVID-19 has adversely impacted a broad range of industries in which the Company’s customers operate and could impair their ability to fulfill their financial obligations. The World Health Organization declared COVID-19 to be a global pandemic indicating that almost all public commerce and related business activities were to be, to varying degrees, curtailed with the goal of decreasing the rate of new infections. The spread of the outbreak has caused significant disruption in the U.S. economy and has disrupted banking and other financial activity in the areas in which the Company operates.

The U.S. government and regulatory agencies have taken several actions to provide support to the U.S. economy. Most notably, the Coronavirus Aid, Relief and Economic Security Act (the “CARES Act”) was signed into law on March 27, 2020 as a \$2 trillion legislative package. The goal of the CARES Act was 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 CARES Act also included extensive emergency funding for hospitals and providers. In addition to the general impact of the COVID-19 pandemic, certain provisions of the CARES Act, as well as other recent legislative and regulatory relief efforts, have had a material impact on the Company’s operations. Also, the actions of the Board of Governors of the Federal Reserve System (the “FRB”) to combat the economic contraction caused by the COVID-19 pandemic, including the reduction of the target federal funds rate and quantitative easing programs, could, if prolonged, adversely affect the Company’s net interest income, margins, and profitability.

Federal banking agencies issued guidance encouraging financial institutions to work with borrowers that may be unable to meet contractual obligations due to the effects of COVID-19. In addition, Section 4013 of the CARES Act states, “banks may elect not to categorize loan modifications as TDRs if they are (1) related to COVID-19; (2) executed on a loan that was not more than 30 days past due as of December 31, 2019; and (3) executed between March 1, 2020, and the earlier of (A) 60 days after the date of termination of the National Emergency or (B) December 31, 2020.” The December 31, 2020 date was subsequently extended to January 1, 2022 under the Consolidated Appropriations Act, 2021.

The Company implemented its business continuity and pandemic plans, which include remote working arrangements for the majority of its workforce. While there has been no material impact to the Company’s employees as of this report date, if COVID-19 escalates further it could also potentially create business continuity issues. The Company does not currently anticipate significant challenges to its ability to maintain systems and controls in light of the measures the Company has taken in response to COVID-19. While it is not possible to know the full extent of these impacts as of the date of this filing, detailed below are potentially material items of which we are aware.

Financial position and results of operations

In keeping with the guidance from regulators, during the height of the pandemic, the Company worked with COVID-19 affected customers to waive fees from a variety of sources and worked with affected borrowers to defer payments, interest and fees. The Company continues to monitor and measure the impact and potential future impact on operations.

Allowance for loan losses

Continued uncertainty regarding the severity and duration of the COVID-19 pandemic and related economic effects will continue to affect the accounting for credit losses, which could cause the provision for loan losses to increase. It also is possible that asset quality could worsen, expenses associated with collection efforts could increase and loan charge-offs could increase. The Company participated in the both rounds of the Small Business Administration’s (“SBA’s”) Paycheck Protection Program (“PPP”), providing loans to small businesses negatively impacted by the COVID-19 pandemic. PPP loans are fully guaranteed by the U.S. government; if that should change, the Company could be required to increase its allowance for loan losses through an additional provision for loan losses charged to earnings.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

In accordance with guidance issued by federal banking agencies, the Company actively worked with borrowers that were unable to meet contractual obligations due to the effects of COVID-19. In order to mitigate the risk associated with these modifications the Company has incorporated covenants that require borrowers to submit quarterly financial statements, prohibits them from distributing funds to any owner or stockholder (with the exception of payroll) and also prohibits them from making any payments on debt owed to subordinated debt holders for the duration of their modification. If borrowers are unable to return to their normal payment plan following their modification period, the Company could be required to increase its allowance for loan losses through an additional provision for loan losses charged to earnings.

Valuation

Valuation and fair value measurement challenges may occur. For example, COVID-19 could cause further and sustained decline in the financial markets or the occurrence of what management would deem a valuation triggering event that could result in an impairment charge to earnings, such as our investment securities.

NOTE 4 — DEBT SECURITIES

The following table summarizes the amortized cost and fair value of securities available-for-sale at December 31, 2021 and 2020 and the corresponding amounts of gross unrealized gains and losses recognized in accumulated other comprehensive income:

(In thousands)	Amortized Cost Basis	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
December 31, 2021				
State and municipal	\$ 12,002	\$ 625	\$ 36	\$ 12,591
Asset-backed securities	8,141	118	4	8,255
Government mortgage-backed securities	15,842	208	59	15,991
Total debt securities available-for-sale	<u>\$ 35,985</u>	<u>\$ 951</u>	<u>\$ 99</u>	<u>\$ 36,837</u>
December 31, 2020				
State and municipal	\$ 10,211	\$ 683	\$ —	\$ 10,894
Asset-backed securities	4,432	278	—	4,710
Government mortgage-backed securities	16,172	449	10	16,611
Total debt securities available-for-sale	<u>\$ 30,815</u>	<u>\$ 1,410</u>	<u>\$ 10</u>	<u>\$ 32,215</u>

The scheduled maturities of debt securities were as follows at December 31, 2021. Actual maturities of asset and mortgage-backed securities may differ from contractual maturities because the mortgages underlying the securities may be repaid without any penalties. Because asset- and mortgage-backed securities are not due at a single maturity date, they are not included in the maturity categories in the following maturity summary.

(In thousands)	Available-for-Sale	
	Amortized Cost	Fair Value
Due after one year through five years	\$ 582	\$ 611
Due after five years through ten years	598	602
Due after ten years	10,822	11,378
Government mortgage-backed securities	15,842	15,991
Asset-backed securities	8,141	8,255
	<u>\$ 35,985</u>	<u>\$ 36,837</u>

There were no realized gains or losses on sales and calls during the year ended December 31, 2021 or 2020.

There were no securities of issuers whose aggregate carrying amount exceeded 10% of equity at December 31, 2021 or 2020.

Securities with carrying amounts of \$14.4 million and \$21.3 million were pledged to secure available borrowings with the Federal Home Loan Bank at December 31, 2021 and 2020, respectively.

As of December 31, 2021, the Company' security portfolio consisted of 57 securities, six of which were in an unrealized loss position.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The aggregate fair value and unrealized losses of securities that have been in a continuous unrealized-loss position for less than twelve months and for twelve months or more, and are temporarily impaired, are as follows at December 31, 2021 and 2020:

(In thousands)	Less than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
December 31, 2021						
Temporarily impaired securities:						
State and municipal	\$ 2,950	\$ 36	\$ —	\$ —	\$ 2,950	\$ 36
Asset-backed securities	4,797	4	—	—	4,797	4
Government mortgage-backed securities	5,022	54	113	5	5,135	59
Total temporarily impaired debt securities	<u>\$ 12,769</u>	<u>\$ 94</u>	<u>\$ 113</u>	<u>\$ 5</u>	<u>\$ 12,882</u>	<u>\$ 99</u>
December 31, 2020						
Temporarily impaired securities:						
Government mortgage-backed securities	\$ —	\$ —	\$ 817	\$ 10	\$ 817	\$ 10
Total temporarily impaired debt securities	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 817</u>	<u>\$ 10</u>	<u>\$ 817</u>	<u>\$ 10</u>

State and municipal, asset-backed and government mortgage-backed securities: The gross unrealized losses on securities were primarily attributable to relative changes in interest rates since the time of purchase. Management believes that the unrealized losses on these debt security holdings are a function of changes in investment spreads and interest rate movements and not changes in credit quality. Management expects to recover the entire amortized cost basis of these securities. Furthermore, the Company does not intend to sell these securities and it is not more-likely-than-not that the Company will be required to sell these securities before recovery of their cost basis, which may be maturity. Therefore, management does not consider these investments to be other-than-temporarily impaired at December 31, 2021.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 5 — LOANS

Loans consisted of the following at December 31, 2021 and 2020:

(In thousands)	2021	2020
Commercial real estate	\$ 432,275	\$ 438,949
Commercial (1)(2)	726,241	565,976
Residential real estate	812	32,785
Construction and land development	42,800	28,927
Consumer	1,519	5,547
Mortgage warehouse	253,764	265,379
	<u>1,457,411</u>	<u>1,337,563</u>
Allowance for loan losses	(19,496)	(18,518)
Deferred loan fees, net (3)	(4,112)	(4,235)
Net loans	<u>\$ 1,433,803</u>	<u>\$ 1,314,810</u>

(1) Includes \$12.4 million and \$41.8 million in PPP loans at December 31, 2021 and December 31, 2020, respectively.

(2) Includes \$120.5 million and \$15.0 million in digital asset loans at December 31, 2021 and December 31, 2020, respectively.

(3) Includes \$503,000 and \$993,000 in deferred fees related to PPP loans at December 31, 2021 and December 31, 2020, respectively.

The following tables set forth information regarding the allowance for loans and gross impaired loans by portfolio segment as of and for the years ended December 31, 2021 and 2020:

(In thousands)	Commercial		Residential		Construction and Land		Mortgage		Unallocated	Total
	Real Estate	Commercial	Real Estate	Development	Consumer	Warehouse				
December 31, 2021										
Allowance for loan losses:										
Beginning balance	\$ 6,095	\$ 10,543	\$ 184	\$ 447	\$ 586	\$ 663	\$ —	\$ —	\$ —	\$ 18,518
Charge-offs	(150)	(2,980)	—	—	(315)	—	—	—	—	(3,445)
Recoveries	92	368	2	—	74	—	—	—	—	536
Provision (credit)	(1,102)	5,564	(148)	32	(177)	(282)	—	—	—	3,887
Ending balance	<u>\$ 4,935</u>	<u>\$ 13,495</u>	<u>\$ 38</u>	<u>\$ 479</u>	<u>\$ 168</u>	<u>\$ 381</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 19,496</u>
Ending balance:										
Individually evaluated for impairment	\$ —	\$ 1,616	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ 1,616
Ending balance:										
Collectively evaluated for impairment	<u>4,935</u>	<u>11,879</u>	<u>38</u>	<u>479</u>	<u>168</u>	<u>381</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>17,880</u>
Total allowance for loan losses ending balance	<u>\$ 4,935</u>	<u>\$ 13,495</u>	<u>\$ 38</u>	<u>\$ 479</u>	<u>\$ 168</u>	<u>\$ 381</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 19,496</u>
Loans (1):										
Ending balance:										
Individually evaluated for impairment	\$ 20,188	\$ 3,929	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ 24,117
Ending balance:										
Collectively evaluated for impairment	<u>412,087</u>	<u>722,312</u>	<u>812</u>	<u>42,800</u>	<u>1,519</u>	<u>253,764</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>1,433,294</u>
Total loans ending balance	<u>\$ 432,275</u>	<u>\$ 726,241</u>	<u>\$ 812</u>	<u>\$ 42,800</u>	<u>\$ 1,519</u>	<u>\$ 253,764</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 1,457,411</u>

(1) Balances represent gross loans. The difference between gross loans versus recorded investment, which would consist of unpaid principal balance, net of charge-offs, interest payments received applied to principal and unamortized deferred loan origination fees and costs, is not material.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(In thousands)	Commercial Real Estate	Commercial	Residential Real Estate	Construction and Land Development	Consumer	Mortgage Warehouse	Unallocated	Total
December 31, 2020								
Allowance for loan losses:								
Beginning balance	\$ 6,104	\$ 6,086	\$ 254	\$ 749	\$ 650	\$ —	\$ 1	\$ 13,844
Charge-offs	(117)	(176)	—	(24)	(772)	—	—	(1,089)
Recoveries	—	7	4	—	155	—	—	166
Provision (credit)	108	4,626	(74)	(278)	553	663	(1)	5,597
Ending balance	<u>\$ 6,095</u>	<u>\$ 10,543</u>	<u>\$ 184</u>	<u>\$ 447</u>	<u>\$ 586</u>	<u>\$ 663</u>	<u>\$ —</u>	<u>\$ 18,518</u>
Ending balance:								
Individually evaluated for impairment	\$ —	\$ 2,024	\$ —	\$ —	\$ —	\$ —	\$ —	\$ 2,024
Ending balance:								
Collectively evaluated for impairment	6,095	8,519	184	447	586	663	—	16,494
Total allowance for loan losses ending balance	<u>\$ 6,095</u>	<u>\$ 10,543</u>	<u>\$ 184</u>	<u>\$ 447</u>	<u>\$ 586</u>	<u>\$ 663</u>	<u>\$ —</u>	<u>\$ 18,518</u>
Loans (1):								
Ending balance:								
Individually evaluated for impairment	\$ 21,039	\$ 4,458	\$ 162	\$ —	\$ —	\$ —	\$ —	\$ 25,659
Ending balance:								
Collectively evaluated for impairment	417,910	561,518	32,623	28,927	5,547	265,379	—	1,311,904
Total loans ending balance	<u>\$ 438,949</u>	<u>\$ 565,976</u>	<u>\$ 32,785</u>	<u>\$ 28,927</u>	<u>\$ 5,547</u>	<u>\$ 265,379</u>	<u>\$ —</u>	<u>\$ 1,337,563</u>

(1) Balances represent gross loans. The difference between gross loans versus recorded investment, which would consist of unpaid principal balance, net of charge-offs, interest payments received applied to principal and unamortized deferred loan origination fees and costs, is not material.

At December 31, 2021 and 2020, loans with an aggregate principal balance of \$194.1 million and \$360.5 million, respectively, were pledged to secure possible borrowings from the Federal Reserve Bank.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following tables set forth information regarding non-accrual loans and loan delinquencies by portfolio segment at December 31, 2021 and 2020:

(In thousands)	30 - 59 Days	60 - 89 Days	90 Days or More Past Due	Total Past Due	Total Current	Total Loans	90 Days or More Past Due and Accruing	Nonaccrual Loans
December 31, 2021								
Commercial real estate	\$ —	\$ —	\$ —	\$ —	\$ 432,275	\$ 432,275	\$ —	\$ —
Commercial	13	111	1,860	1,984	724,257	726,241	—	2,080
Residential real estate	—	—	555	555	257	812	—	812
Construction and land development	—	—	—	—	42,800	42,800	—	—
Consumer	15	11	—	26	1,493	1,519	—	—
Mortgage warehouse	—	—	—	—	253,764	253,764	—	—
Total	<u>\$ 28</u>	<u>\$ 122</u>	<u>\$ 2,415</u>	<u>\$ 2,565</u>	<u>\$ 1,454,846</u>	<u>\$ 1,457,411</u>	<u>\$ —</u>	<u>\$ 2,892</u>
December 31, 2020								
Commercial real estate	\$ —	\$ —	\$ —	\$ —	\$ 438,949	\$ 438,949	\$ —	\$ —
Commercial	4,358	—	291	4,649	561,327	565,976	—	4,198
Residential real estate	255	346	1,030	1,631	31,154	32,785	—	1,156
Construction and land development	—	—	—	—	28,927	28,927	—	—
Consumer	61	21	64	146	5,401	5,547	—	65
Mortgage warehouse	—	—	—	—	265,379	265,379	—	—
Total	<u>\$ 4,674</u>	<u>\$ 367</u>	<u>\$ 1,385</u>	<u>\$ 6,426</u>	<u>\$ 1,331,137</u>	<u>\$ 1,337,563</u>	<u>\$ —</u>	<u>\$ 5,419</u>

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Information about the Company's impaired loans by portfolio segment was as follows at December 31, 2021 and 2020:

(In thousands)	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
December 31, 2021					
With no related allowance recorded:					
Commercial real estate	\$ 20,188	\$ 20,339	\$ —	\$ 20,282	\$ 652
Commercial	2,015	2,205	—	2,068	183
Residential real estate	—	—	—	—	—
Construction and land development	—	—	—	—	—
Consumer	—	—	—	—	—
Mortgage warehouse	—	—	—	—	—
Total impaired with no related allowance	<u>\$ 22,203</u>	<u>\$ 22,544</u>	<u>\$ —</u>	<u>\$ 22,350</u>	<u>\$ 835</u>
With an allowance recorded:					
Commercial real estate	\$ —	\$ —	\$ —	\$ —	\$ —
Commercial	1,914	3,086	1,616	2,576	4
Residential real estate	—	—	—	—	—
Construction and land development	—	—	—	—	—
Consumer	—	—	—	—	—
Mortgage warehouse	—	—	—	—	—
Total impaired with an allowance recorded	<u>\$ 1,914</u>	<u>\$ 3,086</u>	<u>\$ 1,616</u>	<u>\$ 2,576</u>	<u>\$ 4</u>
Total					
Commercial real estate	\$ 20,188	\$ 20,339	\$ —	\$ 20,282	\$ 652
Commercial	3,929	5,291	1,616	4,644	187
Residential real estate	—	—	—	—	—
Construction and land development	—	—	—	—	—
Consumer	—	—	—	—	—
Mortgage warehouse	—	—	—	—	—
Total impaired loans	<u>\$ 24,117</u>	<u>\$ 25,630</u>	<u>\$ 1,616</u>	<u>\$ 24,926</u>	<u>\$ 839</u>

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(In thousands)	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
December 31, 2020					
With no related allowance recorded:					
Commercial real estate	\$ 21,039	\$ 21,312	\$ —	\$ 21,356	\$ 350
Commercial	434	441	—	476	19
Residential real estate	162	162	—	164	8
Construction and land development	—	—	—	—	—
Consumer	—	—	—	—	—
Mortgage Warehouse	—	—	—	—	—
Total impaired with no related allowance	<u>\$ 21,635</u>	<u>\$ 21,915</u>	<u>\$ —</u>	<u>\$ 21,996</u>	<u>\$ 377</u>
With an allowance recorded:					
Commercial real estate	\$ —	\$ —	\$ —	\$ —	\$ —
Commercial	4,024	4,605	2,024	4,177	1
Residential real estate	—	—	—	—	—
Construction and land development	—	—	—	—	—
Consumer	—	—	—	—	—
Mortgage Warehouse	—	—	—	—	—
Total impaired with an allowance recorded	<u>\$ 4,024</u>	<u>\$ 4,605</u>	<u>\$ 2,024</u>	<u>\$ 4,177</u>	<u>\$ 1</u>
Total					
Commercial real estate	\$ 21,039	\$ 21,312	\$ —	\$ 21,356	\$ 350
Commercial	4,458	5,046	2,024	4,653	20
Residential real estate	162	162	—	164	8
Construction and land development	—	—	—	—	—
Consumer	—	—	—	—	—
Mortgage Warehouse	—	—	—	—	—
Total impaired loans	<u>\$ 25,659</u>	<u>\$ 26,520</u>	<u>\$ 2,024</u>	<u>\$ 26,173</u>	<u>\$ 378</u>

The following summarizes TDRs entered into during the years ended December 31, 2021 and 2020:

(Dollars in thousands)	Year Ended December 31,					
	2021			2020		
	Number of Contracts	Pre- Modification Outstanding Recorded Investment	Post- Modification Outstanding Recorded Investment	Number of Contracts	Pre- Modification Outstanding Recorded Investment	Post- Modification Outstanding Recorded Investment
Troubled debt restructurings:						
Commercial real estate	—	\$ —	\$ —	9	\$ 18,811	\$ 20,311
Commercial	3	1,868	1,868	1	81	81
	<u>3</u>	<u>\$ 1,868</u>	<u>\$ 1,868</u>	<u>10</u>	<u>\$ 18,892</u>	<u>\$ 20,392</u>

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

In 2021, the Bank approved three TDRs, all related to one commercial relationship totaling \$1.9 million. As of December 31, 2020, this relationship was deemed impaired, placed on non-accrual status and specific reserves of \$1.8 million were allocated. A troubled debt restructuring was completed to provide the borrower with a three-month principal and interest deferral through April 2021; upon review in the second quarter an additional three-month principal and interest deferral was granted through August 2021. As of December 31, 2021, \$1.6 million relating to this commercial relationship was charged-off. The remaining balance is on non-accrual status with specific reserves of \$343,000.

In 2020, the Bank approved 10 TDRs. Of the 10 TDRs, seven were for one commercial real estate loan relationship totaling \$20.1 million. The Bank analyzed the relationship and modified the relationship as follows:

- \$16.5 million was placed on interest-only payments for three years at a reduced rate;
- \$2.1 million was restructured to amortize and pay out over a 10-year term at a reduced rate; and
- \$1.5 million was advanced for necessary capital expenditures. The advance was placed on interest-only payments for three years at a reduced rate.

Upon completion of the restructuring in the first quarter of 2020, the commercial relationship was placed on non-accrual status and after demonstrating the ability to pay the loan under the restructured terms, it was taken off non-accrual status in the fourth quarter of 2020 and specific reserves of \$1.2 million were removed due to sufficient collateral. As of December 31, 2021, these loans were paying in accordance with the restructured terms and no new specific reserves have been attributed to the relationship.

The Bank approved two TDRs for another commercial real estate relationship totaling \$165,000. These loans have a reduced rate for a period of two years. An impairment analysis was performed and a specific reserve of \$8,000 was allocated to this relationship. The Bank also approved one troubled debt restructuring of a commercial loan totaling \$81,000. This commercial loan was placed on an extended six-month interest-only period with a new term and re-amortization to follow. An impairment analysis was performed and a specific reserve of \$40,000 was allocated to this relationship.

The total recorded investment in TDRs was \$22.7 million and \$23.3 million at December 31, 2021 and 2020, respectively. At December 31, 2021, there were no commitments to lend additional funds to borrowers whose loans were modified in troubled debt restructurings.

Additionally, the Company has worked with borrowers impacted by COVID-19 and provided modifications to allow for deferral of interest or principal and interest payments on a case-by-case basis. These modifications are excluded from troubled debt restructuring classification under Section 4013 of the CARES Act or under applicable interagency guidance of the federal banking regulators and will continue to be reported as current during the payment deferral period.

The Company's policy is to continue to accrue interest during the deferral period. Loans not meeting the CARES Act or regulatory guidance are evaluated for TDR and non-accrual treatment under the Company's existing policies and procedures. All loan modifications made pursuant to the CARES Act or interagency guidance that were in payment deferral have resumed repayment as of December 31, 2021. At December 31, 2020, loan modifications totaled approximately \$44.0 million. There were eight commercial real estate loans that amounted to \$12.4 million, 28 commercial and industrial loans that amounted to \$22.4 million, and one residential mortgage loan that amounted to \$177,000. There were no consumer loans that were in payment deferral at December 31, 2020 based on modifications made pursuant to the CARES Act or interagency guidance.

Credit Quality Information

The Company utilizes a seven grade internal loan rating system for commercial real estate, construction and land development, commercial loans and mortgage warehouse as follows:

Loans rated 1-3: Loans in these categories are considered "pass" rated loans with low to average risk.

Loans rated 4: Loans in this category are considered "special mention." These loans are starting to show signs of potential weakness and are being closely monitored by management.

Loans rated 5: Loans in this category are considered "substandard." Generally, a loan is considered substandard if it is inadequately protected by the current net worth and paying capacity of the obligors and/or the collateral pledged. There is a distinct possibility that the Company will sustain some loss if the weakness is not corrected.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Loans rated 6: Loans in this category are considered “doubtful.” Loans classified as doubtful have all the weaknesses inherent in those classified substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, highly questionable and improbable.

Loans rated 7: Loans in this category are considered uncollectible (“loss”) and of such little value that their continuance as loans is not warranted.

On an annual basis, or more often if needed, the Company formally reviews the ratings on all commercial real estate, construction and land development, and commercial loans.

On an annual basis, or more often if needed, the Company completes a credit recertification on all mortgage warehouse originators.

For residential real estate loans, the Company initially assesses credit quality based upon the borrower’s ability to pay and rates such loans as pass. Ongoing monitoring is based upon the borrower’s payment activity.

Consumer loans are not formally rated.

The following tables present the Company’s loans by portfolio segment as well as risk ratings at December 31, 2021 and 2020:

(In thousands)	Commercial Real Estate	Commercial	Residential Real Estate	Construction and Land Development	Consumer	Mortgage Warehouse	Total
December 31, 2021							
Grade:							
Pass	\$ 383,460	\$ 676,081	\$ —	\$ 41,762	\$ —	\$ 253,764	\$ 1,355,067
Special mention	29,004	41,921	—	—	—	—	70,925
Substandard	19,811	7,677	812	1,038	—	—	29,338
Doubtful	—	562	—	—	—	—	562
Not formally rated	—	—	—	—	1,519	—	1,519
Total	<u>\$ 432,275</u>	<u>\$ 726,241</u>	<u>\$ 812</u>	<u>\$ 42,800</u>	<u>\$ 1,519</u>	<u>\$ 253,764</u>	<u>\$ 1,457,411</u>
December 31, 2020							
Grade:							
Pass	\$ 401,541	\$ 538,449	\$ —	\$ 28,927	\$ —	\$ 265,379	\$ 1,234,296
Special mention	17,702	13,625	—	—	—	—	31,327
Substandard	19,706	13,902	1,560	—	—	—	35,168
Not formally rated	—	—	31,225	—	5,547	—	36,772
Total	<u>\$ 438,949</u>	<u>\$ 565,976</u>	<u>\$ 32,785</u>	<u>\$ 28,927</u>	<u>\$ 5,547</u>	<u>\$ 265,379</u>	<u>\$ 1,337,563</u>

Loans serviced for others are not included in the accompanying consolidated balance sheets. The unpaid principal balances of mortgage and other loans serviced for others were \$23.7 million and \$14.0 million at December 31, 2021 and 2020, respectively.

Certain directors and executive officers of the Company and companies in which they have significant ownership interests were customers of the Bank during 2021. The following is a summary of the loans to such persons and their companies at December 31, 2021 and 2020:

(In thousands)	
Beginning balance, January 1, 2020	\$ 3,705
Advances	12,329
Principal payments	(656)
Ending balance, December 31, 2020	<u>\$ 15,378</u>
Beginning balance, January 1, 2021	\$ 15,378
Advances	3,912
Principal payments	(1,251)
Ending balance, December 31, 2021	<u>\$ 18,039</u>

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 6 — PREMISES AND EQUIPMENT

The following is a summary of premises and equipment at December 31, 2021 and 2020:

(In thousands)	2021	2020
Land	\$ 2,424	\$ 2,424
Buildings and leasehold improvements	13,838	13,828
Furniture and equipment	5,705	5,308
Leasehold improvements	<u>3,526</u>	<u>3,526</u>
	25,493	25,086
Accumulated depreciation and amortization	<u>(11,235)</u>	<u>(10,370)</u>
Premises and equipment, net	<u>\$ 14,258</u>	<u>\$ 14,716</u>

Depreciation and amortization expense was \$870,000 and \$944,000 for the years ended December 31, 2021 and 2020, respectively.

NOTE 7 — DEPOSITS

The following is a summary of deposit balances by type at December 31, 2021 and 2020:

(In thousands)	2021	2020
NOW and demand	\$ 824,471	\$ 554,095
Regular savings	155,267	151,341
Money market deposits	<u>419,625</u>	<u>353,793</u>
Total non-certificate accounts	<u>1,399,363</u>	<u>1,059,229</u>
Certificate accounts of \$250,000 or more	5,078	5,167
Certificate accounts less than \$250,000	<u>55,454</u>	<u>173,032</u>
Total certificate accounts	<u>60,532</u>	<u>178,199</u>
Total deposits	<u>\$ 1,459,895</u>	<u>\$ 1,237,428</u>

At December 31, 2021 and 2020, the aggregate amount of brokered certificates of deposit was \$20.2 million and \$114.1 million, respectively. Brokered certificates of deposit are not included in the totals for time deposits in denominations over \$250,000 listed above.

At December 31, 2021, the scheduled maturities for certificate accounts for each of the following five years are as follows:

(In thousands)	
2022	\$ 51,134
2023	6,873
2024	1,106
2025	1,246
2026	<u>173</u>
Total	<u>\$ 60,532</u>

Deposits from related parties held by the Company at December 31, 2021 and 2020 amounted to \$14.6 million and \$8.8 million, respectively.

NOTE 8 — BORROWINGS

Advances consist of funds borrowed from the FHLB. Maturities of advances from the FHLB for years ending after December 31, 2021 and 2020 are summarized as follows:

(In thousands)	2021	2020
2023	\$ 8,500	\$ 8,500
2024	—	—
2025	<u>5,000</u>	<u>5,000</u>
Total	<u>\$ 13,500</u>	<u>\$ 13,500</u>

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Borrowings from the FHLB, which aggregated \$13.5 million at December 31, 2021 and 2020, respectively, are secured by a blanket lien on qualified collateral, consisting primarily of loans with first mortgages secured by one- to four-family properties, certain commercial loans and qualified mortgage-backed government securities. At December 31, 2021, the interest rates on FHLB advances ranged from 1.21% to 3.01%, and the weighted average interest rate on FHLB advances was 2.11%. At December 31, 2021, the Company had the ability to borrow \$141.3 million from the FHLB.

NOTE 9 — INCOME TAXES

The components of income tax expense are as follows for the years ended December 31, 2021 and 2020:

(In thousands)	2021	2020
Current tax expense (benefit):		
Federal	\$ 4,715	\$ 4,906
State	1,817	1,928
Net operating loss carryforward	—	(7)
	<u>6,532</u>	<u>6,827</u>
Deferred tax benefit:		
Federal	(401)	(1,525)
State	(177)	(677)
	<u>(578)</u>	<u>(2,202)</u>
Income tax expense	<u>\$ 5,954</u>	<u>\$ 4,625</u>

The following is a summary of the differences between the statutory federal income tax rate and the effective tax rates for the years ended December 31, 2021 and 2020:

	2021	2020
Federal income tax at statutory rate	21.0 %	21.0 %
Increase (decrease) in tax resulting from:		
State tax, net of federal tax benefit	5.9	6.0
Tax exempt income and dividends received deduction	(0.3)	(0.4)
Other	0.3	1.2
Effective tax rate	<u>26.9 %</u>	<u>27.8 %</u>

The following is a summary of the Company's gross deferred tax assets and gross deferred tax liabilities at December 31, 2021 and 2020:

(In thousands)	2021	2020
Deferred tax assets:		
Allowance for loan losses	\$ 5,403	\$ 5,132
Employee benefit plans and share-based compensation plans	3,081	2,849
Deferred loan fees, net	1,140	1,174
Write down of other assets and receivables	111	111
Reserve for unfunded commitments	56	37
Other	467	344
Gross deferred tax assets	<u>10,258</u>	<u>9,647</u>
Deferred tax liabilities:		
Depreciation	(37)	(5)
Prepaid expenses	(60)	(60)
Net unrealized holding gain on securities	(203)	(342)
Gross deferred tax liabilities	<u>(300)</u>	<u>(407)</u>
Net deferred tax asset	<u>\$ 9,958</u>	<u>\$ 9,240</u>

The Company reduces the deferred tax asset by a valuation allowance if, based on the weight of the available evidence, it is not "more likely than not" that some portion or all of the deferred tax assets will be realized. The Company assesses the realizability of its deferred tax assets by assessing the likelihood of the Company generating federal and state income tax, as applicable, in future periods in amounts

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

sufficient to offset the deferred tax charges in the periods they are expected to reverse. Based on this assessment, management concluded that a valuation allowance was not required as of December 31, 2021 or 2020.

It is the Company's policy to provide for uncertain tax positions and the related interest and penalties based upon management's assessment of whether a tax benefit is more likely than not to be sustained upon examination by tax authorities. At December 31, 2021 and 2020, there was no material uncertain tax positions related to federal and state income tax matters. The Company is currently open to audit under the statute of limitations by the Internal Revenue Service and state taxing authorities for the years ended December 31, 2018 through December 31, 2020.

NOTE 10 — EMPLOYEE BENEFITS & STOCK-BASED COMPENSATION PLANS

401(k) Plan

The Company sponsors a 401(k) plan. All employees are eligible to join the 401(k) plan. A Safe Harbor Plan was adopted by the Company effective January 1, 2007. Under the Safe Harbor Plan, the Company matches 100% of employee contributions up to 6% of compensation. In addition, the Company may make a discretionary contribution to the 401(k) plan determined on an annual basis. Employees may contribute up to 75% of their salary subject to certain limits based on federal tax laws. The expense recognized under the 401(k) plan was \$955,000 and \$781,000 for the years ended December 31, 2021 and 2020, respectively.

Supplemental Executive Retirement Plans

The Company has Supplemental Executive Retirement Agreements with certain executive officers. These agreements are designed to supplement the benefits available through the Company's retirement plan. The liability for the retirement benefits amounted to \$10.9 million and \$9.1 million at December 31, 2021 and 2020, respectively, and is included in other liabilities. The expense recognized for these benefits was \$1.8 million and \$1.3 million for the years ended December 31, 2021 and 2020, respectively.

Employee Stock Ownership Plan

Old Provident established an ESOP to provide eligible employees the opportunity to own Old Provident stock. The plan is a tax-qualified plan for the benefit of all eligible Bank employees. Contributions are allocated to eligible participants on the basis of compensation, subject to federal tax law limits. The ESOP acquired 721,876 shares in Old Provident's initial stock offering with the proceeds of a loan totaling \$3.6 million. The loan was payable annually over 15 years at a rate per annum equal to the prime rate. In conjunction with the Conversion, the Company refinanced the original loan to the ESOP with an additional \$8.2 million payable over 15 years at a rate per annum equal to the prime rate (3.25% as of December 31, 2021 and 2020) to acquire an additional 816,992 shares at \$10.00 per share, representing 8% of the shares sold in the Company's second-step offering. After the Conversion, the unallocated shares had an average price of \$8.01 per share. Shares used as collateral to secure the loan are released and available for allocation to eligible employees as the principal and interest on the loan is paid. The number of shares committed to be released per year through 2033 is 89,758.

Shares held by the ESOP include the following:

	December 31, 2021	December 31, 2020
Allocated	372,014	282,256
Committed to be allocated	89,758	89,758
Unallocated	1,077,096	1,166,854
Total	<u>1,538,868</u>	<u>1,538,868</u>

The fair value of unallocated shares was approximately \$20.0 million at December 31, 2021.

Total compensation expense recognized for the years ended December 31, 2021 and 2020 was \$1.4 million and \$841,000 respectively.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Stock-Based Compensation Plan

The shareholders of the Company approved the Provident Bancorp, Inc. 2020 Equity Incentive Plan (the "2020 Equity Plan") on November 23, 2020, which is in addition to the Provident Bancorp, Inc. 2016 Equity Incentive Plan (the "2016 Equity Plan"), (collectively called the "Equity Incentive Plans"). Under the Equity Incentive Plans the Company may grant options, restricted stock, restricted units or performance awards to its directors, officers and employees. Both incentive stock options and non-qualified stock options may be granted under the Equity Incentive Plans, with 902,344 and 1,021,239 shares reserved for options under the 2016 Equity Plan and 2020 Equity Plan, respectively. The exercise price of each option equals the market price of the Company's stock on the date of grant and the maximum term of each option is ten years. The total number of shares reserved for restricted stock or restricted units is 360,935 and 408,495 under the 2016 Equity Plan and 2020 Equity Plan, respectively. The value of restricted stock grants is based on the market price of the stock on grant date. Options and awards vest ratably over 3 to 5 years. The Company has elected to recognize forfeitures of awards as they occur.

Expense related to options and restricted stock granted to directors is recognized as directors' fees within non-interest expense.

Stock Options

The fair value of each option is estimated on the date of the grant using the Black-Scholes option-pricing model with the following assumptions:

- Expected volatility is based on historical volatility of the Company's common stock price.
- Expected life represents the period of time that the option is expected to be outstanding, taking into account the contractual term, and the vesting period.
- The dividend yield assumption is based on the Company's expectation of dividend payouts.
- The risk-free rate is based on the U.S. Treasury yield curve in effect at the time of grant for a period equivalent to the expected life of the option.

The fair value of options granted was determined using the following weighted-average assumptions as of grant date.

	2021	2020
Expected volatility	34.41 %	34.63 %
Expected life (years)	7.5	7.5
Expected dividend yield	1.07 %	1.04 %
Risk free interest rate	1.19 %	0.66 %
Fair value per option	\$ 5.06	\$ 3.79

A summary of the status of the Company's stock option grants for the year ended December 31, 2021, is presented in the table below:

	Stock Option Awards	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (years)	Aggregate Intrinsic Value
Outstanding at January 1, 2021	1,644,731	\$ 10.25		
Granted	150,000	15.00		
Forfeited	(96,700)	12.41		
Exercised	(139,068)	8.61		
Outstanding at December 31, 2021	1,558,963	\$ 10.72	7.13	\$ 12,290,000
Outstanding and expected to vest at December 31, 2021	1,558,963	\$ 10.72	7.13	\$ 12,290,000
Vested and Exercisable at December 31, 2021	826,484	\$ 9.46	5.51	\$ 7,558,000
Unrecognized compensation cost	\$ 2,792,000			
Weighted average remaining recognition period (years)	3.80			

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Total expense for the stock options was \$1.1 million and \$462,000 for the years ended December 31, 2021 and 2020, respectively. The intrinsic value of options exercised was \$1.3 million for the year ended December 31, 2021. The tax benefit from option exercises was \$288,000 for the year ended December 31, 2021. There were no exercises for the year ended December 31, 2020.

Restricted Stock

Shares issued upon the granting of restricted stock may come from authorized but unissued shares or reacquired shares held by the Company. Any shares forfeited because vesting requirements are not met will again be available for issuance under the Equity Plan. The fair market value of shares awarded, based on the market prices at the date of grant, is recognized as compensation expense over the applicable vesting period.

The following table presents the activity in unvested restricted stock awards under the Equity Plan for the year ended December 31, 2021:

	Number of Shares	Weighted Average Grant Price
Unvested restricted stock awards at January 1, 2021	387,683	\$ 11.10
Granted	60,000	15.00
Forfeited	(38,680)	12.41
Vested	(131,078)	10.28
Unvested restricted stock awards at December 31, 2021	277,925	\$ 12.15
Unrecognized compensation cost	\$ 3,202,000	
Weighted average remaining recognition period (years)	3.81	

Total expense for the restricted stock awards was \$1.4 million and \$627,000 for the years ended December 31, 2021 and 2020, respectively. The tax benefit from restricted awards was \$390,000 and \$177,000 for the years ended December 31, 2021 and 2020. The total fair value of shares vested during the years ended December 31, 2021 and 2020 was \$2.5 million and \$631,000, respectively.

NOTE 11 — EARNINGS PER SHARE

Basic earnings per share represents income available to common stockholders divided by the weighted-average number of common shares outstanding during the period. Diluted earnings per share is computed in a manner similar to that of basic earnings per share except that the weighted-average number of common shares outstanding is increased to include the number of incremental common shares (computed using the treasury method) that would have been outstanding if all potentially dilutive common stock equivalents were issued during the period. Unallocated ESOP shares, treasury stock and unvested restricted stock is not deemed outstanding for earnings per share calculations.

(Dollars in thousands)	2021	2020
Net income attributable to common shareholders	\$ 16,139	\$ 11,985
Average number of common shares outstanding	18,242,576	19,422,096
Less:		
Average unallocated ESOP shares	(1,118,037)	(1,207,892)
Average unvested restricted stock	(351,911)	(123,975)
Average number of common shares outstanding to calculate basic earnings per common share	16,772,628	18,090,229
Effect of dilutive unvested restricted stock and stock option awards	529,379	40,796
Average number of common shares outstanding to calculate diluted earnings per common share	17,302,007	18,131,025
Earnings per common share:		
Basic	\$ 0.96	\$ 0.66
Diluted	\$ 0.93	\$ 0.66

Stock options for 236,722 and 73,399 shares of common stock were not considered in computing diluted earnings per common share for 2021 and 2020, respectively, because they were antidilutive, meaning the exercise price for such options were higher than the average price for the Company for such period.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 12 — REGULATORY MATTERS

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

The Bank is subject to capital regulations that require a Common Equity Tier 1 ("CET1") capital ratio of 4.5%, a minimum Tier 1 capital to risk-weighted assets ratio of 6.0%, a minimum total capital to risk-weighted assets ratio of 8.0% and a minimum Tier 1 leverage ratio of 4.0%. CET1 generally consists of common stock and retained earnings, subject to applicable adjustments and deductions. In order to be considered "well capitalized," the Bank must maintain a CET1 capital ratio of 6.5% and a Tier 1 ratio of 8.0%, a total risk-based capital ratio of 10% and a Tier 1 leverage ratio of 5.0%. As of December 31, 2021 and 2020, the FDIC categorized the Bank as well capitalized under the regulatory framework for prompt corrective action.

Applicable regulations limit capital distributions and certain discretionary bonus payments to management if the institution does not hold a "capital conservation buffer" consisting of 2.5% of common equity Tier 1 capital to risk-weighted assets above the amount necessary to meet its minimum risk-based capital requirements. At December 31, 2021, the Bank exceeded the regulatory requirement for the capital conservation buffer.

In 2019, the federal banking agencies adopted a final rule to implement Section 201 of the Economic Growth, Regulatory Relief, and Consumer Protection Act, effective January 1, 2020, establishing a community bank leverage ratio ("CBLR") framework for community banking organizations having total consolidated assets of less than \$10 billion, having a leverage ratio of greater than 9%, and satisfying other criteria, such as limitations on the amount of off-balance sheet exposures and on trading assets and liabilities. A community banking organization that qualifies for and elects to use the CBLR framework and that maintains a leverage ratio of greater than 9% will be considered to have satisfied the generally applicable risk-based and leverage capital requirements in the banking agencies' generally applicable capital rules and, if applicable, will be considered to have met the well-capitalized ratio requirements for purposes of Section 38 of the Federal Deposit Insurance Act. The CARES Act temporarily lowered the community bank leverage ratio to 8% through 2020. The CBLR requirement transitioned from 8% to 8.5% for the calendar year 2021 and will then transition to 9% beginning in 2022. As of December 31, 2021, the Bank has not opted into the CBLR framework.

The Bank's actual capital amounts and ratios at December 31, 2021 and 2020 are summarized as follows:

(Dollars in thousands)	Actual Capital		For Capital Adequacy Purposes			To Be Well Capitalized Under Prompt Corrective Action Provisions		
	Amount	Ratio	Amount	Ratio	Amount	Ratio		
December 31, 2021								
Total Capital (to Risk Weighted Assets)	\$ 221,865	14.18 %	\$ 125,177	≥	8.0 %	\$ 156,472	≥	10.0 %
Tier 1 Capital (to Risk Weighted Assets)	202,369	12.93	93,883	≥	6.0	125,177	≥	8.0
Common Equity Tier 1 Capital (to Risk Weighted Assets)	202,369	12.93	70,412	≥	4.5	101,706	≥	6.5
Tier 1 Capital (to Average Assets)	202,369	12.07	67,072	≥	4.0	83,840	≥	5.0
December 31, 2020								
Total Capital (to Risk Weighted Assets)	\$ 199,377	14.60 %	\$ 109,273	≥	8.0 %	\$ 136,591	≥	10.0 %
Tier 1 Capital (to Risk Weighted Assets)	182,286	13.35	81,955	≥	6.0	109,273	≥	8.0
Common Equity Tier 1 Capital (to Risk Weighted Assets)	182,286	13.35	61,466	≥	4.5	88,784	≥	6.5
Tier 1 Capital (to Average Assets)	182,286	12.37	58,926	≥	4.0	73,658	≥	5.0

Liquidation Accounts

Upon the completion of the Company's initial stock offering in 2015 and the second step offering in 2019, liquidation accounts were established for the benefit of certain depositors of the Bank in amounts equal to:

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. The product of (i) the percentage of the stock issued in the initial stock offering in 2015 to persons other than MHC and (ii) the net worth of the mid-tier holding company as of the date of the latest balance sheet contained in the prospectus utilized in connection with the offering.
2. The MHC's ownership interest in the retained earnings of the Company as of the date of the latest balance sheet contained in the 2019 prospectus plus the MHC's net assets (excluding its ownership of the Company).

The Company and the Bank are not permitted to pay dividends on their capital stock if the shareholders' equity of the Company, or the shareholder's equity of the Bank, would be reduced below the amount of the respective liquidation accounts. The liquidation accounts will be reduced annually to the extent that eligible account holders have reduced their qualifying deposits. Subsequent increases will not restore an eligible account holder's interest in the liquidation accounts.

Other Restrictions

The Company's principal source of funds for dividend payments is dividends received from the Bank. Federal and state banking regulations restrict the amount of dividends that may be paid in a year, without prior approval of regulatory agencies, to the net income of the Bank for the year plus the retained net income of the previous two years. As of December 31, 2021, 2020 and 2019, \$16.1 million, \$12.1 million and \$10.7 million, respectively, of retained earnings was available to pay dividends

The Company may, at times, repurchase its own shares in the open market. Such transactions are subject to the Federal Reserve Board's notice provisions for stock repurchases. In October 2020, the Company announced its plan to repurchase 1,000,000 shares of its common stock. The repurchase program was adopted following the receipt of non-objection from the Federal Reserve Bank of Boston, and in compliance with applicable state and federal regulations. The Company completed the repurchase of 1,000,000 shares of its common stock under this repurchase program in February 2021. In March 2021, the Company announced its plan to repurchase 1,400,000 shares of its common stock. The repurchase program was adopted following the receipt of non-objection from the Federal Reserve Bank of Boston, and in compliance with applicable state and federal regulations. As of December 31, 2021, the Company had repurchased 1,240,304 shares of its outstanding common stock under these programs.

NOTE 13 — LEASES

The Company has committed to rent premises used in business operations under non-cancelable operating leases and determines if an arrangement meets the definition of a lease upon inception. Operating leases are included in operating lease right-of-use ("ROU") assets and operating lease liabilities on the Company's balance sheet.

Operating lease ROU assets represent the Company's right to use an underlying asset for the lease term and lease liabilities represent the Company's obligation to make lease payments arising from the lease. Operating lease ROU assets and lease liabilities are recognized at the commencement date based on the present value of lease payments over the lease term. The Company's leases do not provide an implicit rate, therefore the Company used its incremental collateralized borrowing rates commensurate with the underlying lease terms to determine present value of operating lease liabilities. The Company's lease terms may include lease extension and termination options when it is reasonably certain that the Company will exercise the option. The Company recognized right-of-use assets totaling \$4.1 million and \$4.3 million and operating lease liabilities totaling \$4.4 million and \$4.5 million at December 31, 2021 and December 31, 2020, respectively. The lease liabilities recognized by the Company represent two leased branch locations and one loan production office.

Lease expense for lease payments is recognized on a straight-line basis over the lease term. Variable lease components, such as fair market value adjustments, are expensed as incurred and not included in ROU assets and operating lease liabilities. Leases with an initial term of 12 months or less are not recorded on the balance sheet; we recognize lease expense for these leases on a straight-line basis over the lease term. For the year ended December 31, 2021 and 2020, rent expense for the operating leases totaled \$315,000 and \$307,000, respectively.

The following table presents information regarding the Company's operating leases:

	December 31, 2021	December 31, 2020
Weighted-average discount rate	3.57%	3.54%
Range of lease expiration dates	1 - 14 years	2 - 15 years
Range of lease renewal options	5 - 20 years	5 - 20 years
Weighted-average remaining lease term	27.0 years	27.6 years

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following table presents the undiscounted annual lease payments under the terms of the Company's operating leases at December 31, 2021, including a reconciliation to the present value of operating lease liabilities recognized in the unaudited Consolidated Balance Sheets:

(In thousands)		
2022	\$	261
2023		264
2024		270
2025		280
2026		291
Years thereafter		<u>6,033</u>
Total lease payments		7,399
Less imputed interest		<u>(3,012)</u>
Total lease liabilities	\$	<u><u>4,387</u></u>

NOTE 14 — FINANCIAL INSTRUMENTS WITH OFF-BALANCE SHEET RISK

The Company is 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 originate loans, standby letters of credit and unadvanced funds on loans. The instruments involve, to varying degrees, elements of credit risk in excess of the amount recognized in the balance sheet. The contract amounts of those instruments reflect the extent of involvement the Company has in particular classes of financial instruments.

The Company's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for loan commitments and standby letters of credit is represented by the contractual amounts of those instruments. The Company uses the same credit policies in making commitments and conditional obligations as it does for on-balance sheet instruments.

Commitments to originate loans are agreements to lend to a customer provided there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Company evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Company upon extension of credit, is based on management's credit evaluation of the borrower. Collateral held varies, but may include secured interests in real property, accounts receivable, inventory, property, plant and equipment and income producing properties.

Standby letters of credit are conditional commitments issued by the Company to guarantee the performance by a customer to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. The Company's outstanding letters of credit generally have a term of less than one year. If a letter of credit is drawn upon, the Company may seek recourse through the customer's underlying line of credit. If the customer's line of credit is also in default, the Company may take possession of the collateral, if any, securing the line of credit.

Notional amounts of financial instruments with off-balance sheet credit risk are as follows at December 31, 2021 and 2020:

(In thousands)	2021	2020
Commitments to originate loans	\$ 16,376	\$ 31,920
Letters of credit	1,314	1,682
Unadvanced portions of loans	<u>307,453</u>	<u>202,015</u>
	<u>\$ 325,143</u>	<u>\$ 235,617</u>

NOTE 15 — FAIR VALUE MEASUREMENTS

The Company reports certain assets at fair value in accordance with GAAP, which defines fair value and establishes a framework for measuring fair value in accordance with generally accepted accounting principles. Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability (exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. The guidance 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 values:

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Basis of Fair Value Measurements

- Level 1 - Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities;
- Level 2 - Quoted prices in markets that are not active, or inputs that are observable either directly or indirectly, for substantially the full term of the asset or liability;
- Level 3 - Prices or valuation techniques that require inputs that are both significant to the fair value measurement and unobservable (i.e., supported by little or no market activity).

An asset's level within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement.

Fair Values of Assets Measured on a Recurring Basis

The Company's investments in state and municipal, asset-backed and government mortgage-backed debt securities available-for-sale are generally classified within Level 2 of the fair value hierarchy. For these investments, the Company obtains fair value measurements from independent pricing services. The fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, trading levels, market consensus prepayment speeds, credit information and the instrument's terms and conditions.

The following summarizes assets measured at fair value on a recurring basis at December 31, 2021 and 2020:

(In thousands)	Fair Value Measurements at Reporting Date Using			
	Total	Quoted Prices in Active Markets Identical Assets Level 1	Significant Other Observable Inputs Level 2	Significant Unobservable Inputs Level 3
December 31, 2021				
State and municipal	\$ 12,591	\$ —	\$ 12,591	\$ —
Asset-backed securities	8,255	—	8,255	—
Mortgage-backed securities	15,991	—	15,991	—
Totals	\$ 36,837	\$ —	\$ 36,837	\$ —
December 31, 2020				
State and municipal	\$ 10,894	\$ —	\$ 10,894	\$ —
Asset-backed securities	4,710	—	4,710	—
Mortgage-backed securities	16,611	—	16,611	—
Totals	\$ 32,215	\$ —	\$ 32,215	\$ —

Fair Values of Assets Measured on a Nonrecurring Basis

The Company may also be required, from time to time, to measure certain other assets at fair value on a non-recurring basis in accordance with generally accepted accounting principles. These adjustments to fair value usually result from the application of lower-of-cost-or-market accounting or write-downs of individual assets.

Certain impaired loans were adjusted to fair value, less cost to sell, of the underlying collateral securing these loans resulting in losses. The loss is not recorded directly as an adjustment to current earnings, but rather as a component in determining the allowance for loan losses. Fair value was measured using appraised values of collateral and adjusted as necessary by management based on unobservable inputs for specific properties.

The following summarizes assets measured at fair value on a nonrecurring basis at December 31, 2021 and 2020:

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Fair Value Measurements at Reporting Date Using:

(In thousands)	Total	Quoted Prices in Active Markets for Identical Assets Level 1	Significant Other Observable Inputs Level 2	Significant Unobservable Inputs Level 3
December 31, 2021				
Impaired loans				
Commercial	\$ 361	\$ —	\$ —	\$ 361
Totals	<u>\$ 361</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 361</u>
December 31, 2020				
Impaired loans				
Commercial	\$ 2,000	\$ —	\$ —	\$ 2,000
Totals	<u>\$ 2,000</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 2,000</u>

The following is a summary of the valuation methodology and unobservable inputs for Level 3 assets measured at fair value on a nonrecurring basis at December 31, 2021 and 2020:

(In thousands)	Fair Value	Valuation Technique	Unobservable Input	Range
December 31, 2021				
Impaired loans				
Commercial	\$ 361	Business valuation	Comparable company evaluations	0% - 24%
December 31, 2020				
Impaired loans				
Commercial	\$ 2,000	Business valuation	Comparable company evaluations	—

At December 31, 2021, the carrying amount of impaired commercial loans measured at fair value on a nonrecurring basis was \$3.2 million, net of specific reserves of \$1.6 million and charge offs of \$1.2 million. At December 31, 2020, the carrying amount of impaired commercial loans measured at fair value on a nonrecurring basis was \$4.0 million, net of specific reserves of \$2.0 million.

GAAP requires disclosure of fair value information about financial instruments, whether or not recognized in the balance sheet, for which it is practicable to estimate that value. Certain financial instruments and all nonfinancial instruments are excluded from the disclosure requirements. Accordingly, the aggregate fair value amounts presented do not represent the underlying value of the Company.

The carrying amounts and estimated fair values of the Company's financial instruments, all of which are held or issued for purposes other than trading, are as follows at December 31, 2021 and 2020:

(In thousands)	Carrying Amount	Fair Value			Total
		Level 1	Level 2	Level 3	
December 31, 2021					
Financial assets:					
Cash and cash equivalents	\$ 153,115	\$ 153,115	\$ —	\$ —	\$ 153,115
Debt securities available-for-sale	36,837	—	36,837	—	36,837
Federal Home Loan Bank of Boston stock	785	N/A	N/A	N/A	N/A
Loans and loans held for sale, net	1,456,649	—	—	1,468,013	1,468,013
Accrued interest receivable	5,703	—	5,703	—	5,703
Financial liabilities:					
Deposits	1,459,895	—	1,459,841	—	1,459,841
Borrowings	13,500	—	13,698	—	13,698
December 31, 2020					
Financial assets:					
Cash and cash equivalents	\$ 83,819	\$ 83,819	\$ —	\$ —	\$ 83,819

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Debt securities available-for-sale	32,215	—	32,215	—	32,215
Federal Home Loan Bank of Boston stock	895	N/A	N/A	N/A	N/A
Loans, net	1,314,810	—	—	1,321,143	1,321,143
Accrued interest receivable	6,371	—	6,371	—	6,371
Financial liabilities:					
Deposits	1,237,428	—	1,237,867	—	1,237,867
Borrowings	13,500	—	14,016	—	14,016

The carrying amounts of financial instruments shown above are included in the consolidated balance sheets under the indicated captions. Accounting policies related to financial instruments are described in Note 2.

NOTE 16 — CONDENSED FINANCIAL STATEMENTS OF PARENT ONLY

Financial information pertaining only to Provident Bancorp, Inc. is as follows:

Provident Bancorp, Inc. - Parent Only Balance Sheet
(In thousands)

	2021	2020
Assets		
Cash and due from banks	\$ 21,747	\$ 42,850
Investment in common stock of The Provident Bank	203,018	183,343
Other assets	9,215	9,821
Total assets	<u>\$ 233,980</u>	<u>\$ 236,014</u>
Liabilities and Shareholders' Equity		
Other liabilities	\$ 198	\$ 158
Shareholders' equity	233,782	235,856
Total liabilities and shareholders' equity	<u>\$ 233,980</u>	<u>\$ 236,014</u>

Provident Bancorp, Inc. - Parent Only Income Statement
(In thousands)

	Years Ended December 31,	
	2021	2020
Total income	\$ 137	\$ 371
Operating expenses	117	494
Income before income taxes and equity in undistributed net income of The Provident Bank	20	(123)
Applicable income tax (benefit) provision	6	(34)
Income before equity in income of subsidiaries	14	(89)
Equity in undistributed net income of The Provident Bank	16,125	12,074
Net income	<u>\$ 16,139</u>	<u>\$ 11,985</u>

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Provident Bancorp, Inc. - Parent Only Statement of Cash Flows (In thousands)	Twelve Months Ended December 31,	
	2021	2020
Cash flows from operating activities:		
Net income	\$ 16,139	\$ 11,985
Adjustments to reconcile net income to net cash provided by operating activities:		
Equity in undistributed earnings of subsidiaries	(16,125)	(12,074)
Deferred tax benefit	—	111
Decrease in other assets	606	704
Increase in other liabilities	40	82
Net cash provided by operating activities	660	808
Cash flows from financing activities:		
Cash dividends paid on common stock	(2,560)	(1,636)
Proceeds from exercise of stock options, net	(241)	—
Shares surrendered related to tax withholdings on restricted stock awards	(614)	(131)
Purchase of common stock	(18,348)	(7,825)
Net cash used in financing activities	(21,763)	(9,592)
Net increase in cash and cash equivalents	(21,103)	(8,784)
Cash and cash equivalents at beginning of year	42,850	51,634
Cash and cash equivalents at end of year	\$ 21,747	\$ 42,850

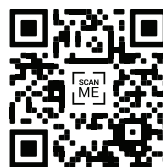
NOTE 17 — SELECTED QUARTERLY FINANCIAL DATA (UNAUDITED)

(In thousands)	First Quarter		Second Quarter		Third Quarter		Fourth Quarter	
	2021	2020	2021	2020	2021	2020	2021	2020
Interest and dividend income	\$ 15,889	\$ 14,089	\$ 15,513	\$ 14,654	\$ 16,336	\$ 15,178	\$ 17,065	\$ 16,482
Interest expense	981	2,017	910	1,619	832	1,183	647	1,112
Net interest and dividend	14,908	12,072	14,603	13,035	15,504	13,995	16,418	15,370
Provision for loan losses	753	3,099	1,669	872	232	760	1,233	866
Total noninterest income	1,018	1,010	1,103	704	1,823	911	1,222	918
Total noninterest expense	9,213	8,306	9,528	8,361	10,068	9,686	11,810	9,455
Income tax expense	1,663	446	1,343	1,256	1,940	1,258	1,008	1,665
Net income	\$ 4,297	\$ 1,231	\$ 3,166	\$ 3,250	\$ 5,087	\$ 3,202	\$ 3,589	\$ 4,302
Earnings per share:								
Basic	\$ 0.24	\$ 0.06	\$ 0.19	\$ 0.18	\$ 0.31	\$ 0.18	\$ 0.22	\$ 0.24
Diluted	\$ 0.24	\$ 0.06	\$ 0.18	\$ 0.18	\$ 0.30	\$ 0.18	\$ 0.21	\$ 0.24
Weighted Average								
Basic	17,263,759	18,115,970	16,778,698	18,150,106	16,637,852	18,185,995	16,481,684	17,912,975
Diluted	17,558,160	18,261,282	17,338,662	18,179,858	17,235,852	18,222,766	17,180,466	18,007,580

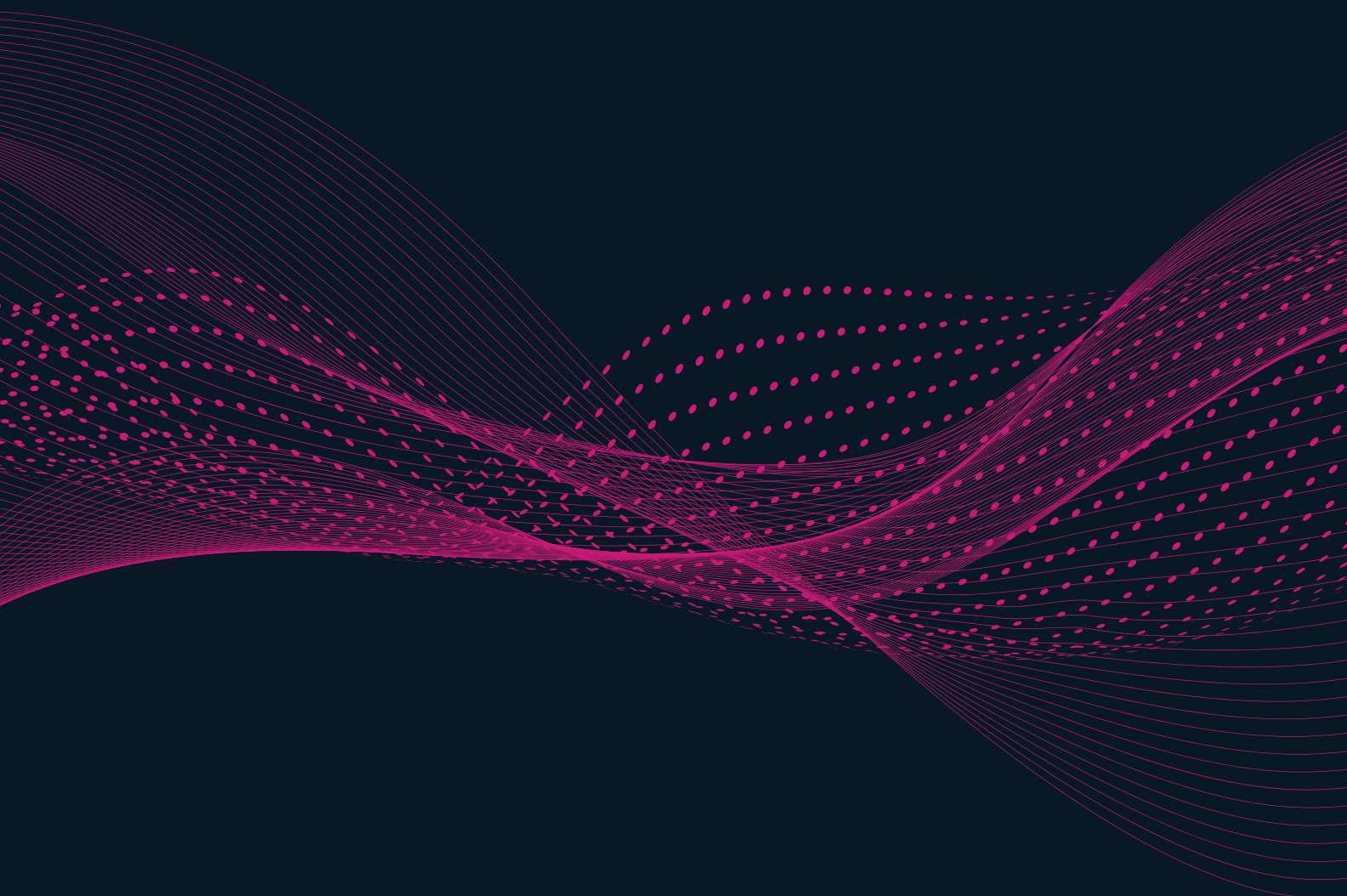


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