

COMMUNITY FINANCIAL CORP /MD/  
Form DEF 14A  
March 25, 2014

**SCHEDULE 14A**

**Proxy Statement Pursuant to Section 14(a) of the Securities Exchange Act of 1934**

(Amendment No. \_\_\_\_)

Filed by the Registrant

Filed by a Party other than the Registrant

Check the appropriate box:

Preliminary Proxy Statement

Confidential, for Use of the Commission Only (as permitted by Rule 14a-6(e)(2))

Definitive Proxy Statement

Definitive Additional Materials

Soliciting Material Pursuant to §240.14a-12

**THE COMMUNITY FINANCIAL CORPORATION**

(Name of Registrant as Specified in Its Charter)

(Name of Person(s) Filing Proxy Statement, if other than the Registrant)

Payment of Filing Fee (Check the appropriate box):

No fee required.

Fee computed on table below per Exchange Act Rules 14a-6(i)(1) and 0-11.

1. Title of each class of securities to which transaction applies:

2. Aggregate number of securities to which transaction applies:

3. Per unit price or other underlying value of transaction computed pursuant to Exchange Act Rule 0-11 (Set forth the amount on which the filing fee is calculated and state how it was determined):

4. Proposed maximum aggregate value of transaction:

5. Total fee paid:

Fee paid previously with preliminary materials:

Check box if any part of the fee is offset as provided by Exchange Act Rule 0-11(a)(2) and identify the filing for which the offsetting fee was paid previously. Identify the previous filing by registration statement number, or the Form or Schedule and the date of its filing.

1. Amount Previously Paid:

2. Form, Schedule or Registration Statement No.:

3. Filing Party:

4. Date Filed:

**[LETTERHEAD OF THE COMMUNITY FINANCIAL CORPORATION]**

March 25, 2014

Dear Stockholder:

I am pleased to invite you to attend the annual meeting of stockholders of The Community Financial Corporation (the “Company”) to be held in the Board Room at the main office of Community Bank of the Chesapeake, 3035 Leonardtown Road, Waldorf, Maryland on Monday, May 5, 2014 at 10:00 a.m.

The enclosed Annual Report on Form 10-K and the notice and proxy statement describe the formal business to be transacted at the annual meeting. Directors and officers of the Company, as well as a representative of the Company’s independent registered public accounting firm, Stegman & Company, will be present to respond to any questions stockholders may have.

Your vote is important, regardless of the number of shares you own. **On behalf of the Board of Directors, I urge you to vote via the Internet, by telephone or by signing, dating and returning a proxy card as soon as possible, even if you plan to attend the annual meeting.**

Sincerely,

/s/ Michael L. Middleton

Michael L. Middleton

*Chairman of the Board and Chief Executive Officer*

**THE COMMUNITY FINANCIAL CORPORATION**

**3035 LEONARDTOWN ROAD**

**WALDORF, MARYLAND 20601**

**(301) 645-5601**

**NOTICE OF 2014 ANNUAL MEETING OF STOCKHOLDERS**

**TIME AND DATE** 10:00 a.m. on Monday, May 5, 2014

**PLACE** Board Room  
Community Bank of the Chesapeake  
3035 Leonardtown Road  
Waldorf, Maryland 20601

**ITEMS OF BUSINESS**

- (1) To elect three directors to serve for a term of three years;
- (2) To ratify the appointment of Stegman & Company as the independent registered public accounting firm for 2014;
- (3) To vote on a non-binding resolution to approve the compensation of the named executive officers; and
- (4) To transact such other business as may properly come before the meeting or any adjournments or postponement thereof.

**RECORD DATE** To vote, you must have been a stockholder at the close of business on March 7, 2014.

**PROXY VOTING**

It is important that your shares be represented and voted at the meeting. You can vote your shares via the Internet, by telephone or by completing and signing the enclosed proxy or voting instruction card sent to you. Voting instructions are printed on your proxy or voting instruction card and included in the accompanying proxy statement. A printed proxy card for the annual meeting and a self-addressed, postage pre-paid envelope will be mailed to all shareholders of record on or about April 7, 2014. You can revoke a proxy at any time before the meeting by following the instructions in the proxy statement.

Gregory C. Cockerham

*Secretary*

March 25, 2014

**IMPORTANT: The prompt return of proxies will save the Company the expense of further requests for proxies to ensure a quorum. A self-addressed envelope is enclosed for your convenience. No postage is required if mailed in the United States.**

**PROXY STATEMENT**

**OF**

**THE COMMUNITY FINANCIAL CORPORATION**

**3035 LEONARDTOWN ROAD**

**WALDORF, MARYLAND 20601**

**(301) 645-5601**

**GENERAL INFORMATION**

We are providing this proxy statement to you in connection with the solicitation of proxies by the Board of Directors of The Community Financial Corporation for the 2014 annual meeting of stockholders and for any adjournment or postponement of the meeting. In this proxy statement, we may also refer to The Community Financial Corporation as “The Community Financial,” the “Company,” “we,” “our” or “us.”

The Community Financial is the holding company for Community Bank of the Chesapeake. In this proxy statement, we may also refer to Community Bank of the Chesapeake as the “Bank.”

We are holding the 2014 annual meeting in the Board Room at the main office of the Bank, 3035 Leonardtown Road, Waldorf, Maryland on Monday, May 5, 2014 at 10:00 a.m., local time.

We intend to provide access to this proxy statement and a proxy card to stockholders of record beginning on or about March 25, 2014.

**IMPORTANT NOTICE REGARDING THE AVAILABILITY OF PROXY MATERIALS**

**FOR THE STOCKHOLDERS MEETING TO BE HELD ON MAY 5, 2014**

The Proxy Statement and Annual Report to Stockholders are available at:

[www.cbtc.com/proxyandannualreport](http://www.cbtc.com/proxyandannualreport).

## INFORMATION ABOUT VOTING

**Who Can Vote at the Meeting.** You are entitled to vote the shares of The Community Financial common stock that you owned as of the close of business on March 7, 2014. As of the close of business on March 7, 2014, 4,688,159 shares of Company common stock were outstanding. Each share of common stock has one vote.

**Voting by Proxy.** This proxy statement is being sent to you by the Board of Directors of The Community Financial to request that you allow your shares of The Community Financial common stock to be represented at the annual meeting by the persons named in the enclosed proxy card. All shares of The Community Financial common stock represented at the meeting by properly executed, dated proxies will be voted according to the instructions indicated on the proxy card. If you sign, date and return a proxy card without giving voting instructions, your shares will be voted as recommended by the Company's Board of Directors. **The Board of Directors recommends that you vote "FOR" each of the nominees for director, "FOR" ratification of the appointment of Stegman & Company as the Company's independent registered public accounting firm and "FOR" the approval of the compensation of the named executive officers.**

If any matters not described in this proxy statement are properly presented at the annual meeting, the persons named in the proxy card will use their judgment to determine how to vote your shares. This includes a motion to adjourn or postpone the meeting to solicit additional proxies. If the annual meeting is postponed or adjourned, your The Community Financial common stock may also be voted by the persons named on the proxy card on the new meeting date, unless you have revoked your proxy. The Company does not know of any other matters to be presented at the annual meeting.



Registered stockholders can vote their shares of The Community Financial Corporation common stock by mailing a proxy card, via the Internet or by telephone. Specific instructions for Internet or telephone voting are set forth on the enclosed proxy or voting instruction card. The Internet and telephone voting procedures are designed to authenticate stockholders' identities, allow stockholders to provide their voting instructions and confirm that their instructions have been recorded properly. The deadline for voting by telephone or via the Internet is 11:59 p.m., Eastern time, on May 4, 2014.

**Ownership of Shares; Attending the Meeting.** You may own shares of The Community Financial in one of the following ways:

Directly in your name as the stockholder of record;

Indirectly through a broker, bank or other holder of record in "street name"; or

Indirectly in the Community Bank of the Chesapeake Employee Stock Ownership Plan.

If your shares are registered directly in your name, you are the holder of record of these shares and we are sending these proxy materials directly to you. As the holder of record, you have the right to give your proxy directly to us or to vote in person at the annual meeting.

If you hold your shares in street name, your broker, bank or other holder of record is sending these proxy materials to you. As the beneficial owner, you have the right to direct your broker, bank or other holder of record how to vote by filling out a voting instruction form that accompanies your proxy materials. Your broker, bank or other holder of record may allow you to provide voting instructions by telephone or via the Internet. Please see the voting instruction form provided by your broker, bank or other holder of record that accompanies this proxy statement. If you hold your shares in street name, you will need proof of ownership to be admitted to the annual meeting. A recent brokerage statement or letter from a bank or broker are examples of proof of ownership. If you want to vote your shares of The Community Financial common stock held in street name in person at the annual meeting, you must obtain a written proxy in your name from the broker, bank or other nominee who is the record holder of your shares.

If you participate in the Community Bank of the Chesapeake Employee Stock Ownership Plan, you will receive a voting instruction card that reflects all shares you may direct the plan trustees to vote on your behalf under the plan. Under the terms of the Employee Stock Ownership Plan, all allocated shares of The Community Financial held by the plan are voted by the trustees, as directed by plan participants. All unallocated shares of Company common stock held by the plan, and allocated shares for which no voting instructions are received, are voted by the trustees in the same proportion as shares for which the trustees have received timely voting instructions, subject to the exercise of their fiduciary duties. **The deadline for returning your voting instructions to the Employee Stock Ownership Plan**

**trustees is April 28, 2014.**

**Quorum.** We will have a quorum and will be able to conduct the business of the annual meeting if the holders of a majority of the outstanding shares of common stock entitled to vote are represented at the meeting. If you return valid proxy instructions or attend the meeting in person, we will count your shares to determine whether there is a quorum, even if you abstain from voting. Broker non-votes (described below) also will be counted to determine the existence of a quorum.

**Votes Required for Proposals.** In voting on the election of directors, the ratification of the appointment of Stegman & Company as the Company's independent registered public accounting firm and on the non-binding resolution to approve the compensation of the named executive officers, you may vote in favor of the proposal, vote against the proposal or abstain from voting. All proposals will be decided by the affirmative vote of a majority of the shares cast at the annual meeting.

For all proposals, abstentions and broker non-votes will not be counted as votes cast and will have no effect on the outcome of the voting on the proposals.

**Effect of Not Casting Your Vote.** If you hold your shares in street name it is critical that you cast your vote if you want it to count in the election of directors (Item 1 of this proxy statement) and the approval of the non-binding advisory vote on executive compensation (Item 3 of this proxy statement). Current regulations restrict the ability of your bank or broker to vote your shares on these matters on a discretionary basis. Thus, if you hold your shares in street name and you do not instruct your bank or broker how to vote in the election of directors and the approval of the non-binding advisory vote on executive compensation no votes will be cast on your behalf. These are referred to as broker non-votes. Your bank or broker will, however, continue to have discretion to vote any shares for which you do not provide voting instructions on the ratification of the appointment of the Company's independent registered public accounting firm (Item 2 of this proxy statement). If you are a stockholder of record and you do not cast your vote, no votes will be cast on your behalf on any of the items of business at the annual meeting.

**Revocation of Proxy.** Stockholders who execute proxies retain the right to revoke them at any time. Unless revoked, the shares represented by such proxies will be voted at the annual meeting and all adjournments thereof. Proxies may be revoked by written notice delivered in person or mailed to the Secretary of the Company, by delivering a later-dated proxy or by attending the annual meeting and voting in person. Attendance at the annual meeting will not in and of itself constitute revocation of your proxy.

## CORPORATE GOVERNANCE

**Director Independence.** The Company's Board of Directors currently consists of nine members, all of whom are independent under the listing requirements of The NASDAQ Stock Market, except for Michael L. Middleton and William J. Pasenelli, who are employees of the Company and the Bank. In determining the independence of its directors, the Board considered transactions, relationships and arrangements between the Company and its directors that are not required to be disclosed in this proxy statement under the heading "*Relationships and Transactions with the Company and the Bank*," including (1) legal services performed by the Jenkins Law Firm, LLC, of which Louis P. Jenkins, Jr. is a principal, and (2) loans or lines of credit that the Bank has directly or indirectly made to each of the directors on the Board.

**Board Leadership Structure.** The Chief Executive Officer also serves as Chairman of the Board, due in part to his long-standing tenure with the Company, which provides unique knowledge regarding the history, strategy, business and operations of the Company and the Bank. The Board has created a Lead Director position to enhance Board independence and oversight. Joseph V. Stone, Jr. is currently the Lead Director of the Board of Directors. Among other things, the Lead Director (1) presides at meetings of the Board at which the Chairman of the Board is not present, including executive sessions of the independent directors, and (2) may call meetings of the independent directors.

**The Board's Role in Risk Oversight.** Risk is inherent with every business and how well a business manages risk can ultimately determine its success. We face a number of risks, including credit risk, interest rate risk, liquidity risk, operational risk, strategic risk and reputation risk. Management is responsible for the day-to-day management of risks the Company faces, while the Board, as a whole and through its committees, has responsibility for the oversight of risk management. In its risk oversight role, the Board of Directors has the responsibility to satisfy itself that the risk management processes designed and implemented by management are adequate and functioning as designed. To do this, senior management attends the Board meetings and is available to discuss strategy and risks facing the Company and to address any questions or concerns raised by the Board on risk management and any other matters. The Board also provides strong oversight of the Company's management and affairs through its standing committees and, when necessary, special meetings of independent directors.

**Committees of the Board of Directors.** The following table identifies the members of the Board’s Audit, Governance and Compensation Committees as of March 7, 2014. All members of each committee are independent in accordance with the listing requirements of The NASDAQ Stock Market. Each committee operates under a written charter, which is approved by the Board of Directors, that governs its composition, responsibilities and operation. Each committee reviews and reassesses the adequacy on its charter at least annually. The charters of the committees are available in the Shareholder Information portion of the “About Community Bank” section of the Company’s website ([www.cbtc.com](http://www.cbtc.com)). In addition, the Company maintains an Enterprise Risk Management Committee that reviews and manages the Company’s material business risks by establishing and monitoring policies and procedures designated to identify, control, monitor and measure its material business risks, including credit, liquidity, operational, strategic and reputational risks.

<b>Director</b>	<b>Audit Committee</b>	<b>Governance Committee</b>	<b>Compensation Committee</b>
Philip T. Goldstein	X		X
Louis P. Jenkins, Jr.		X*	X*
Michael L. Middleton			
William J. Pasenelli			
Mary Todd Peterson	X*		
James R. Shepherd	X		
Austin J. Slater, Jr.	X		
H. Beaman Smith		X	X
Joseph V. Stone, Jr.**	X	X	X
<u>Number of Meetings in 2013</u>	4	2	2

\* Chairperson

\*\* Lead Director

**Audit Committee.** The Audit Committee engages the Company’s independent registered public accounting firm and meets with them in connection with their annual audit and reviews the Company’s accounting and financial reporting policies and practices. Other responsibilities of the Audit Committee include engagement of compliance and internal audit providers and the review with management of reports issued by such parties. The Board of Directors has determined that the Audit Committee does not have a member who is an “audit committee financial expert” as defined under the rules and regulations of the Securities and Exchange Commission. While the Board has not designated any

individual Board member as an “audit committee financial expert,” the Board believes the level of financial knowledge and experience of the current members of the Audit Committee, including the ability to read and understand financial statements, is cumulatively sufficient to discharge the Audit Committee’s responsibilities.

**Governance Committee.** The Governance Committee is responsible for promoting sound corporate governance policies that promote the best interests of the Company and its stockholders. The Committee's responsibilities include: identification of director candidates; director education; recommendations on the size and composition of the Board and the boards of any subsidiaries, review of any shareholder proposals; monitoring of regulatory and statutory compliance; review of committee charters; and evaluations of Board oversight and effectiveness. The Governance Committee also annually reviews and recommends, in conjunction with the Compensation Committee, the appropriate level of director compensation.

**Compensation Committee.** The Compensation Committee approves the compensation objectives for the Company and the Bank and establishes the compensation for the Chief Executive Officer and other executives. Our Chief Executive Officer and Director of Human Resources make recommendations to the Compensation Committee from time to time regarding the appropriate mix and level of compensation for other executives. The Compensation Committee reviews compensation for the Company's executive officers to ensure an appropriate balance between short-term pay and long-term incentives. In addition to reviewing competitive market values, the Compensation Committee also examines the total compensation mix, pay-for-performance relationship, and how all elements, in the aggregate, comprise the executive's total compensation package. Decisions by the Compensation Committee with respect to the compensation of executive officers are approved by the full Board of Directors. The Compensation Committee also annually reviews and recommends, in conjunction with the Governance Committee, the appropriate level of director compensation.

**Director Nomination Process.** The Governance Committee selects nominees for election as directors. The Governance Committee seeks to create a Board that is strong in its collective knowledge and has a diversity of skills and experience in accounting and finance, management and leadership, vision and strategy, business operations, business judgment, industry knowledge and corporate governance. To accomplish this, the Governance Committee considers a candidate's knowledge of the banking business and involvement in community, business and civic affairs, and also considers whether the candidate would adequately represent the Company's market area. Any nominee for director must be highly qualified with regard to some or all these attributes. In searching for qualified director candidates to fill vacancies on the Board, the Governance Committee solicits its current directors for the names of potential qualified candidates. The Governance Committee may also ask its directors to pursue their business contacts for the names of potentially qualified candidates. The Governance Committee would then consider the potential pool of director candidates, select the top candidates based on the candidates' qualifications and the Company's needs, and conduct a thorough investigation of each proposed candidate's background. If a stockholder has submitted a proposed nominee in accordance with the procedures specified below, the Governance Committee would consider the proposed nominee, along with any other proposed nominees recommended by directors, in the same manner in which the Governance Committee would evaluate nominees for director recommended by the Board of Directors.

**Consideration of Recommendations by Stockholders.** The Governance Committee will consider recommendations for directors submitted by stockholders. Stockholders who wish the Governance Committee to consider their recommendations for nominees for director should submit their recommendations in writing to the Governance Committee in care of the Secretary, The Community Financial Corporation, 3035 Leonardtown Road, Waldorf, Maryland 20601. Each written recommendation must set forth (1) the name of the recommended candidate, (2) the number of shares of stock of the Company that are beneficially owned by the stockholder making the recommendation

and by the recommended candidate, and (3) a detailed statement explaining why the stockholder believes the recommended candidate should be nominated for election as a director. In addition, the stockholder making such recommendation must promptly provide any other information reasonably requested by the Governance Committee. To be considered by the Governance Committee for nomination for election at an annual meeting of stockholders, the recommendation must be received by the January 1 preceding that annual meeting.



**Board and Committee Meetings.** During 2013, the Board of Directors of the Company held seven meetings. No director attended fewer than 75% of the meetings of the Board of Directors and Board committees on which they served in 2013.

**Director Attendance at Annual Meeting of Stockholders.** While the Company does not have a policy regarding Board member attendance at annual meetings of stockholders it encourages directors to attend the annual meeting of stockholders. All of the Company's directors attended the Company's 2013 annual meeting of stockholders.

**Code of Ethics.** The Community Financial maintains a Code of Ethics that is designed to ensure that the Company's directors and employees meet the highest standards of ethical conduct. The Code of Ethics, which applies to all employees and directors, addresses conflicts of interest, the treatment of confidential information, general employee conduct and compliance with applicable laws, rules and regulations. In addition, the Code of Ethics is designed to deter wrongdoing and promote honest and ethical conduct, the avoidance of conflicts of interest, full and accurate disclosure and compliance with all applicable laws, rules and regulations. Under the terms of the Code of Ethics, violations of the Code of Ethics are required to be reported to the Audit Committee of the Board of Directors. A copy of the Code of Ethics was filed as an exhibit to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2005.

## DIRECTOR COMPENSATION

The following table provides the compensation received by the non-employee directors of the Company during 2013.

Name	Fees Earned or Paid in Cash (\$)	Option Awards (\$)(1)	<b>Non-qualified Deferred Compensation Earnings (\$) (2)</b>	Total (\$)
Philip T. Goldstein	\$40,175	—	\$ —	\$40,175
Louis P. Jenkins, Jr.	45,250	—	—	45,250
Mary Todd Peterson	42,300	—	—	42,300
James R. Shepherd	40,825	—	—	40,825
Austin J. Slater, Jr.	42,125	—	—	42,125

H. Beaman Smith	36,925	–	5,486	42,411
Joseph V. Stone, Jr.	43,925	–	12,151	56,076

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(1) As of December 31, 2013, each non-employee director had the following number of stock options outstanding:

Name	Stock Options Outstanding
Philip T. Goldstein	500
Louis P. Jenkins, Jr.	13,500
Mary Todd Peterson	–
James R. Shepherd	12,375
Austin J. Slater, Jr.	12,375
H. Beaman Smith	15,750
Joseph V. Stone, Jr.	500

Represents the portion of non-qualified deferred compensation earnings under the Community Bank of the  
 (2) Chesapeake Retirement Plan for Directors that was above the IRS long-term rate. Under the plan, interest is credited quarterly at a rate equal to the Company's annualized return on equity.

**Cash Retainer and Meeting Fees for Directors.** The following tables set forth the applicable retainers and fees that will be paid to directors for their service on the Boards of Directors of the Company and the Bank for 2014.

***Board of Directors of the Company:***

Annual Retainer	\$15,000
Fee per Board Meeting (Regular or Special)	\$750 (\$225 per telephone meeting)
Fee per Committee Meeting	\$500 (\$225 per telephone meeting)
Annual Retainer for Governance, Audit, Compensation and Enterprise Risk Management Committee Chairs	\$2,500

***Board of Directors of the Bank:***

Annual Retainer	\$10,000
Fee per Board Meeting (Regular or Special)	\$650 (\$225 per telephone meeting)
Fee per Committee Meeting	\$425 (\$225 per telephone meeting)

If more than one meeting of the Bank, the Company or any committee is held on any given day, the aggregate fees cannot exceed \$1,400 per day. Employee directors receive only the annual retainer and Board meeting fees; they do not receive fees for committee meetings.

**Directors Retirement Plan.** The Bank maintains a retirement plan for non-employee members of the Board of Directors of the Bank (the “Directors’ Plan”). Under the Directors’ Plan, each eligible director of the Bank will receive an annual retirement benefit for ten years following his or her termination of service on the Bank’s Board in an amount equal to the product of his “Benefit Percentage” and \$3,500. A participant’s “Benefit Percentage” is 0% for less than five years of service, 33 % for five to nine years of service, 66 % for 10 to 14 years of service, and 100% for 15 or more years of service. If a participant terminates service on the Board due to disability, the Bank will pay the participant each year for ten years an amount equal to the product of his or her Benefit Percentage and \$3,500. If a participant dies before collecting either his or her retirement or disability benefit, the participant’s surviving spouse or estate will receive a lump sum payment having a present value equal to five times the annual retirement benefit to which the

participant was entitled, assuming the participant separated service on the date of death. If the participant dies after beginning to receive his or her retirement or disability benefits, the participant's surviving spouse or estate will receive a lump sum payment having a present value equal to the remaining benefits to which the participant was entitled from the date of death through the fifth annual payment thereafter. A participant will become fully vested in the event of a "change in control" (as defined in the Directors' Plan) or upon separation from service on the Board after attaining the age 72 or incurring a disability.

The Directors' Plan also establishes a deferred compensation program for participants, under which they may elect to defer all or any portion of the fees and/or salary otherwise payable. Deferred amounts will be credited quarterly and adjusted annually with a rate of return equal to the Company's return on equity for the calendar year, as determined under accounting principles generally accepted in the United States.

## AUDIT RELATED MATTERS

**Report of the Audit Committee.** The Company's management is responsible for the Company's internal controls and financial reporting process. The Company's independent registered public accounting firm is responsible for performing an independent audit of the Company's consolidated financial statements and issuing an opinion on the conformity of those financial statements with accounting principles generally accepted in the United States. The Audit Committee oversees the Company's internal controls and financial reporting process on behalf of the Board of Directors.

The Audit Committee has met and held discussions with management and the independent registered public accounting firm. Management represented to the Audit Committee that the Company's consolidated financial statements were prepared in accordance with accounting principles generally accepted in the United States and the Audit Committee has reviewed and discussed the consolidated financial statements with management and the independent registered public accounting firm. The Audit Committee discussed with the independent registered public accounting firm matters required to be discussed by Statement on Auditing Standard No. 16, as amended (AICPA, *Professional Standards*, Vol. 1. AU Section 380) as adopted by the Public Company Accounting Oversight Board in Rule 3200T, including the quality, not just the acceptability, of the accounting principles, the reasonableness of significant judgments and the clarity of the disclosures in the financial statements.

In addition, the Audit Committee has received the written disclosures and the letter from the independent registered public accounting firm required by the applicable requirements of the Public Company Accounting Oversight Board regarding the independent registered public accounting firm's communications with the Audit Committee concerning independence and has discussed with the independent registered public accounting firm the independent registered public accounting firm's independence from the Company and its management. In concluding that the registered public accounting firm is independent, the Audit Committee considered, among other factors, whether the non-audit services provided by the firm were compatible with its independence.

The Audit Committee discussed with the Company's independent registered public accounting firm the overall scope and plans for its audit. The Audit Committee meets with the independent registered public accounting firm, with and without management present, to discuss the results of its examination, its evaluation of the Company's internal controls, and the overall quality of the Company's financial reporting.

In performing all of these functions, the Audit Committee acts only in an oversight capacity. In its oversight role, the Audit Committee relies on the work and assurances of the Company's management, which has the primary responsibility for financial statements and reports, and of the independent registered public accounting firm that, in its report, expresses an opinion on the conformity of the Company's financial statements to accounting principles generally accepted in the United States. The Audit Committee's oversight does not provide it with an independent basis to determine that management has maintained appropriate accounting and financial reporting principles or

policies, or appropriate internal controls and procedures designed to assure compliance with accounting standards and applicable laws and regulations. Furthermore, the Audit Committee's considerations and discussions with management and the independent registered public accounting firm do not assure that the Company's financial statements are presented in accordance with accounting principles generally accepted in the United States, that the audit of the Company's financial statements has been carried out in accordance with generally accepted auditing standards or that the Company's independent registered public accounting firm is "independent."

In reliance on the reviews and discussions referred to above, the Audit Committee recommended to the Board of Directors, and the Board has approved, that the audited consolidated financial statements be included in the Company's Annual Report on Form 10-K for the year ended December 31, 2013 for filing with the Securities and Exchange Commission.

AUDIT COMMITTEE OF THE BOARD OF DIRECTORS  
OF THE COMMUNITY FINANCIAL CORPORATION

Mary Todd Peterson (Chair)

James R. Shepherd

Austin J. Slater, Jr.

Joseph V. Stone, Jr.

**Audit Fees.** The following table sets forth the fees billed to the Company by Stegman & Company for the fiscal years ended December 31, 2013 and 2012:

	2013	2012
Audit Fees	\$86,965	\$97,114
Audit Related Fees <sup>(1)</sup>	77,316	18,250
Tax Fees <sup>(2)</sup>	18,000	8,750
All Other Fees <sup>(3)</sup>	3,087	4,185

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<sup>(1)</sup> Represents fees for the audit of the 401(k) Plan and ESOP and, for 2013, fees related to the Company's public offering.

<sup>(2)</sup> Consists of tax filing and tax-related compliance and other advisory services.

<sup>(3)</sup> Consists of presentation at directors' retreat.

**Pre-Approval of Services by the Independent Registered Public Accounting Firm.** The Audit Committee's charter provides that the Audit Committee will approve in advance any non-audit services permitted by the Securities Exchange Act, including tax services that its independent registered public accounting firm renders to the Company, unless such prior approval may be waived because of permitted exceptions under the Securities Exchange Act, including but not limited to a 5% *de minimis* exception. The Audit Committee may delegate to one or more members



of the Audit Committee the authority to grant pre-approvals for auditing and allowable non-auditing services, which decision shall be presented to the full Audit Committee at its next scheduled meeting for ratification. During the fiscal year ended December 31, 2013, the Audit Committee approved 100% of all “audit-related,” “tax” and “other fees.”

**PRINCIPAL HOLDERS OF VOTING SECURITIES**

The following table sets forth, as of March 7, 2014, certain information as to those persons known by the Company to beneficially own more than 5% of the Company's outstanding shares of common stock and the shares of common stock beneficially owned by each director, each executive officer named in the summary compensation table and by all executive officers and directors of the Company as a group. All beneficial owners listed in the table have the same address as the Company, unless otherwise provided. Unless otherwise indicated, each of the named individuals has sole voting power and sole investment power with respect to the shares shown.

Name of Beneficial Owners	<b>Number of Shares Owned (Excluding Options) (1)(2)</b>		Number of Shares That May be Acquired within 60 Days by Exercising Options	<b>Percent of Shares of Common Stock Outstanding (3)</b>
<b>Directors</b>				
Philip T. Goldstein	7,027		500	* %
M. Arshed Javaid	3,500		—	*
Louis P. Jenkins, Jr.	18,056		13,500	*
Michael L. Middleton	257,115	(4)	32,030	6.1
William J. Pasenelli	31,377		20,039	1.1
Mary Todd Peterson	6,529		—	*
James R. Shepherd	8,000		12,375	*
Austin J. Slater, Jr.	17,419		10,375	*
H. Beaman Smith	104,037		15,750	2.6
Joseph V. Stone, Jr.	28,625	(5)	500	*
<b>Named Executive Officer Who is Not Also a Director</b>				
Gregory C. Cockerham	115,590		14,175	2.8
<b>All Directors, Executive Officers and Nominees as a Group (15 persons)</b>				
	634,314	(6)	125,225	15.8
<b>Community Bank of the Chesapeake Employee Stock Ownership Plan</b>				
	246,983	(7)	—	5.3
<b>Basswood Capital Management, L.L.C.</b>				
	250,065	(8)	—	5.3
<b>Matthew Lindenbaum</b>				

Bennett Lindenbaum

645 Madison Avenue, 10<sup>th</sup> Floor

New York, New York 10022

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\*Less than 1% of the shares outstanding

Includes shares allocated to the account of the individuals under the Community Bank of the Chesapeake Employee (1) Stock Ownership Plan, with respect to which the individual has voting but not investment power as follows: Mr. Cockerham – 27,827 shares; Mr. Middleton – 43,790 shares; and Mr. Pasenelli – 3,622 shares.

Includes shares of unvested restricted stock, with respect to which the individual has voting but no investment (2) power as follows: Mr. Goldstein – 800 shares; Mr. Javaid – 400 shares; Mr. Jenkins – 800 shares; Mr. Middleton – 1,684 shares; Mr. Pasenelli – 4,789 shares; Ms. Peterson – 800 shares; Mr. Shepherd – 800 shares; Mr. Slater – 800 shares; Mr. Smith – 800 shares; Mr. Stone – 800 shares; and Mr. Cockerham – 3,370 shares

Based upon 4,688,159 shares of Company common stock outstanding, plus, for each individual or group, the (3) number of shares of Company common stock that each individual or group may acquire through the exercise of options within 60 days of March 7, 2014.

Includes 69,351 shares owned by Mr. Middleton's wife and 4,877 shares owned by the individual retirement account (4) of Mr. Middleton's wife.

(5) Includes 2,000 shares owned by the individual retirement account of Mr. Stone's wife.

Amount includes an aggregate of 25,835 unvested shares of restricted stock over which certain officers of the (6) Company have voting but no dispositive power.

Includes 40,281 shares held in a suspense account for future allocation and/or distribution among participants as the (7) loan used to purchase the shares is repaid. The ESOP trustees, which are Company directors Joseph V. Stone, Jr., and H. Beaman Smith, vote all allocated shares in accordance with the instructions of the participating employees.

Unallocated shares and shares for which no instructions have been received are voted by the trustees in the same (8) proportion as shares for which the trustees have received timely voting instructions.

Based on information contained in a Schedule 13G filed with the U.S. Securities and Exchange Commission on (8) February 12, 2014.

## ITEMS TO BE VOTED ON BY STOCKHOLDERS

### Item 1 – Election of Directors.

The Community Financial's Board of Directors currently consists of nine members. H. Beaman Smith's term as a director will expire at the annual meeting. The Board is divided into three classes, each with terms of three years, one-third of whom are elected annually. The Board of Directors has nominated Philip T. Goldstein, James R. Shepherd and M. Arshed Javaid to serve for an additional three-year term and until their successors are elected and qualified. Messrs. Goldstein and Shepherd are currently directors of the Company and the Bank. Mr. Javaid is currently a director of the Bank.

It is intended that the persons named in the proxies solicited by the Board will vote for the election of the named nominees. If any nominee is unable to serve, the shares represented by all valid proxies will be voted for the election of such substitute nominee as the Board of Directors may recommend. At this time, the Board knows of no reason why any nominee might be unable to serve.

**The Board of Directors recommends a vote "FOR" the election of each of the nominees.**

Information regarding the nominees and the directors continuing in office is provided below. Unless otherwise stated, each individual has held his or her current occupation for the last five years. The age indicated in each biography is as of December 31, 2013. There are no family relationships among the directors or executive officers. The indicated period for service as a director includes service as a director of Community Bank of the Chesapeake.

### **Board Nominees with Terms Ending in 2017**

**Philip T. Goldstein** has owned and operated Philip T. Goldstein Real Estate Appraisals, a full-service real estate appraisal and consulting firm, located in Prince Frederick, Maryland, since 1975. He currently serves as a director of Asbury Communities, Inc., a non-profit continuing care retirement community headquartered in Gaithersburg, Maryland and Calvert County Nursing Center, Prince Frederick, Maryland. Age 65. Director since 2006.

Mr. Goldstein provides the Board with significant management, strategic and operational knowledge through his experience as owner of a real estate appraisal and consulting firm. Mr. Goldstein's background in commercial and

residential appraisal practice also provides a valuable perspective to the credit function of the Bank. Mr. Goldstein provides local community insight through his position as a director on various local non-profit organizations.

**James R. Shepherd** is a retired businessman and former local government executive. Mr. Shepherd holds an MS degree in Management from the University of Maryland and a BA from Roanoke College in Economics and Business Administration. Mr. Shepherd serves on numerous civic and charitable organizations. Age 68. Director since 2003.

Mr. Shepherd's background in economic development and management adds strength to the market intelligence required to direct strategic initiatives on franchise expansion. Mr. Shepherd also brings critical insight regarding the economic development of the communities in which the Bank operates.

**M. Arshed Javaid** is President of Smartronix, Inc., an information technology and engineering solutions provider. Mr. Javaid founded Smartronix, Inc. in 1995, and has extensive experience in business management and community relations. Currently, he serves on the Historic Sotterley Inc. Board of Trustees and is actively involved with the St. Mary's Chamber of Commerce and the Southern Maryland Navy Alliance. Age 58. Director since 2013.

Mr. Javaid provides the Board with significant management, strategic and operational knowledge through his experience as founder and president of an information technology and engineering solutions provider that has evolved from a start-up company to a company with over 550 employees. Mr. Javaid's experience in the information technology industry provides the Board with valuable insight into the data security and reputational risk issues facing businesses.

### **Directors with Terms Ending in 2015**

**William J. Pasenelli** is President and Chief Financial Officer of the Company and the Bank. Mr. Pasenelli joined the Bank as Chief Financial Officer in 2000 and was named President of the Bank in 2010 and President of the Company in May 2012. Before joining the Bank, Mr. Pasenelli had been Chief Financial Officer of Acacia Federal Savings Bank, Annandale, Virginia, since 1987. Mr. Pasenelli is a member of the American Institute of Certified Public Accountants, the Greater Washington Society of Certified Public Accountants and other civic groups. Age 55. Director since 2010.

Mr. Pasenelli's extensive experience in the local banking industry affords the Board valuable insight regarding the business and operations of the Bank. Mr. Pasenelli's financial acumen and knowledge of the Company's and the Bank's business and history position him well to serve as President and Chief Financial Officer and as a Director.

**Austin J. Slater, Jr.** is the President and Chief Executive Officer of the Southern Maryland Electric Cooperative, which is one of the ten largest electrical distribution cooperatives in the country. Mr. Slater also serves as the immediate past Chairman of the Board of the Maryland Chamber of Commerce and numerous other industry and civic organizations. He also serves as the Chairman of the Board of Trustees for the College of Southern Maryland. Mr. Slater holds a MBA in Finance from George Washington University and a BS in Accounting from Shepherd University. Age 60. Director since 2003.

Mr. Slater has extensive management level experience in a large company setting outside of the financial services industry. Mr. Slater's financial acumen and operational experience allow him to understand the complexities of the Company and the Bank. His experience in a regulated industry has exposed Mr. Slater to many of the issues facing companies today, particularly regulated entities, making Mr. Slater a valued component of a well-rounded board.

**Joseph V. Stone, Jr.** has owned and operated Joe Stone Insurance Agency, which provides multi-line insurance services to clients in Maryland and Virginia, since 1981. He has served as a director for the Southern Maryland Electric Cooperative since 1996 and currently serves as Chairman of the Board. Age 59. Director since 2006.

Mr. Stone provides the Board with significant marketing and operational knowledge through his experience as owner of an insurance agency and various director positions with companies outside of the financial services industry. Mr. Stone also has considerable experience in the insurance industry, corporate governance and risk assessment practices necessary in banking operations.

#### **Directors with Terms Ending in 2016**

**Louis P. Jenkins, Jr.** is the principal of Jenkins Law Firm, LLC, located in LaPlata, Maryland. Before entering private practice, Mr. Jenkins served as an Assistant State's Attorney in Charles County, Maryland from 1997 to 1999. In addition to his private practice, Mr. Jenkins serves as Court Auditor for the Circuit Court for Charles County, Maryland and attorney for the Charles County Board of Elections. Mr. Jenkins currently serves as Chairman of the Board of Directors of Civista Medical Center, a member hospital of the University of Maryland Medical System, and has served as a board member of several other public service organizations including the Southern Maryland Chapter of the American Red Cross, Charles County Chamber of Commerce and the Charles County Bar Association. Age 42. Director since 2000.

As an attorney, Mr. Jenkins provides the Board with substantial knowledge regarding issues facing the Company and the Bank. In addition, Mr. Jenkins brings a critical perspective to the lending and governance function of the Company and the Bank. Mr. Jenkins' experience in the public sector adds valuable expertise regarding local issues and provides first-hand understanding of the local political and business environment in which the Bank operates.

**Michael L. Middleton** is Chairman and Chief Executive Officer of the Company and the Bank. Mr. Middleton joined the Bank in 1973 and served in various management positions until 1979 when he became President of the Bank, which he served as until 2010. He remained President of the Company until May 2012. Mr. Middleton is a Certified Public Accountant and holds a Masters of Business Administration. From 1996 to 2004, Mr. Middleton served on the Board of Directors of the Federal Home Loan Bank of Atlanta, serving as Chairman of the Board in 2004. Mr. Middleton served on the Board of Directors of the Federal Reserve Bank, Baltimore Branch, from 2004 to 2009. He completed his term as Chairman of the Maryland Bankers Association in June 2013 and is currently the Chairman of the Board for the College of Southern Maryland, serves on the Advisory Board of the Robert H. Smith School of Business Center for Financial Policy and serves on the Federal Reserve's Community Depository Advisory Council. He also serves on several philanthropic and civic boards. Age 66. Director since 1979.

Mr. Middleton's extensive experience in the local banking industry and involvement in the communities in which the Bank serves affords the Board valuable insight regarding the business and operations of the Bank. In addition to Mr. Middleton's extensive background in finance and corporate management, Mr. Middleton also has significant expertise in large financial institution governance providing a unique and broad-based decision-making capability for the Company and the Bank. Mr. Middleton's knowledge of the Company's and the Bank's business and history, combined with his success and strategic vision, position him well to serve as our Chairman and Chief Executive Officer.

**Mary Todd Peterson** is the President and Chief Executive Officer of Medmarc Insurance Group and a Director of Medmarc Casualty Insurance Company and each of its subsidiaries. Ms. Peterson has been associated with Medmarc since 2001 where she has also held the positions of Chief Financial Officer and Chief Operating Officer. From 1993 to 2001, Ms. Peterson was a Partner with Johnson Lambert & Co., a certified public accounting firm. Ms. Peterson has also held positions with Acacia Life Insurance Company, Oxford Development Corporation and Ernst & Whinney (now Ernst & Young). Ms. Peterson currently serves as a member of the Property Casualty Insurers Association of America ("PCI") Board of Governors, Chair of PCI's Investment Committee and a member of PCI's Executive and Finance Committees. Ms. Peterson is a member of the American Institute of Certified Public Accountants. Age 59. Director since 2010.

Ms. Peterson has extensive management level experience in a mid-size company setting within the financial services industry. As a Virginia resident, Ms. Peterson provides valuable insight regarding local markets in Virginia. Ms. Peterson's financial and operational expertise within the insurance industry, including her corporate governance and risk assessment skills, provide the Board with a skill set critical to operating the Company and Bank in an efficient manner.





**Item 2 – Ratification of the Independent Registered Public Accounting Firm.**

Stegman & Company, which was the Company’s independent registered public accounting firm for 2013, has been retained by the Audit Committee of the Board of Directors to be the Company’s independent registered public accounting firm for 2014, subject to ratification by the Company’s stockholders. A representative of Stegman & Company is expected to be present at the annual meeting and will have the opportunity to make a statement if he or she desires to do so and will be available to respond to appropriate questions.

If the ratification of the appointment of the independent registered public accounting firm is not approved by a majority of the votes cast by stockholders at the annual meeting, the Audit Committee may consider other independent registered public accounting firms.

**The Board of Directors recommends that stockholders vote “FOR” the ratification of the appointment of Stegman & Company as the Company’s independent registered public accounting firm.**

**Item 3 – Advisory Vote on Executive Compensation**

The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the “Dodd-Frank Act”) requires that we provide our stockholders with the opportunity to express their views, on a non-binding basis, on the compensation of our named executive officers as disclosed in this proxy statement. This vote, which is often referred to as the “say-on-pay” vote, provides stockholders with the opportunity to endorse or not endorse the following resolution:

“Resolved, that the stockholders approve the compensation of the named executive officers, as described in the tabular disclosure regarding named executive officer compensation and the accompanying narrative disclosure in this proxy statement.”

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

**The Board of Directors unanimously recommends a vote “FOR” approval of the compensation of the named executive officers.**



**EXECUTIVE COMPENSATION**

**Summary Compensation Table.** The following table provides information concerning total compensation earned or paid to the Chief Executive Officer and the two most highly compensated executive officers of the Company who served in such capacity as of December 31, 2013. These three officers are referred to as the named executive officers in this proxy statement.

Name and Principal Position	Year	Salary (\$)	Bonus (\$)	Stock Awards (\$)	Non-qualified		Total (\$)
					Deferred Compensation Earnings (\$) (1)	All Other Compensation (\$) (2)	
Michael L. Middleton Chief Executive Officer	2013	\$478,899	\$–	\$–	\$ 36,509	\$ 56,565	\$571,973
	2012	454,960	–	65,508	22,720	48,865	592,053
William J. Pasenelli President and Chief Financial Officer	2013	355,131	56,497	32,652(3)	–	50,431	494,711
	2012	341,200	56,298	79,346	–	43,066	519,910
Gregory C. Cockerham Executive Vice President and Chief Lending Officer	2013	274,782	43,657	22,122(4)	–	13,419	353,980
	2012	263,670	43,506	53,764	–	12,036	372,976

Represents the portion of non-qualified deferred compensation earnings under the Community Bank of the Chesapeake Retirement Plan for Directors and the Community Bank of the Chesapeake Executive Deferred Compensation Plan that were above the applicable federal long-term rate. Under the plan, interest is credited quarterly at a rate equal to the Company's annualized return on equity.

(1) Details of the amounts reported in the "All Other Compensation" column for 2013 are provided in the table below.

(2) The table excludes perquisites, which did not exceed \$10,000 in the aggregate for each named executive officer.

Item	Mr. Middleton	Mr. Pasenelli	Mr. Cockerham
Directors' fees	\$ 36,925	\$ 36,925	\$ –
Market value of allocations under the employee stock ownership plan	2,150	2,150	2,150
Employer contribution to 401(k) Plan	9,359	9,359	9,359
Imputed income under split-dollar life insurance arrangement	8,015	1,968	1,883
Reimbursement of payroll taxes for supplemental retirement benefits	116	29	27

Represents the aggregate grant date fair value of the granting of 1,814 shares of restricted stock awards computed in accordance with FASB ASC Topic 718 based on a per share price of \$18.00, on the date of grant for awards in 2013.

Represents the aggregate grant date fair value of the granting of 1,229 shares of restricted stock awards computed in accordance with FASB ASC Topic 718 based on a per share price of \$18.00, on the date of grant for awards in 2013.

**Employment Agreements.** The Community Financial and Community Bank of the Chesapeake maintain employment agreements with each of the named executive officers. The term of Mr. Middleton's employment agreement is automatically extended by one day each day so that the term remains at five years. The term of the employment agreements with Mr. Pasenelli and Mr. Cockerham are automatically extended by one day each day so that the term remains at three years, until either party gives notice to the other of its intent to stop the renewal of the term of the agreement. Among other things, the agreements provide for an annual salary, for participation in an equitable manner in any stock option plan or incentive plan to the extent authorized by the Bank's Board of Directors for its key management employees and for participation in pension, group life insurance, medical coverage and in other employee benefits applicable to executive personnel.

See “*Retirement Benefits*” and “*Other Potential Post-Termination Benefits*” for a discussion of benefits and payments the named executive officers may receive under the employment agreements upon their retirement or termination of their employment.

**Outstanding Equity Awards at Fiscal Year End.** The following table provides information concerning unexercised options for each of the named executive officers outstanding as of December 31, 2013.

Name	Option Awards		Option Exercise Price (\$)	Option Expiration Date	Restricted Stock Awards	
	Number of Securities Underlying Unexercised Options (#) Exercisable	Number of Securities Underlying Unexercised Options (#) Unexercisable			Number of Shares or Units of Stock That Have Not Vested (#)	Market Value of Shares or Units of Stock That Have Not Vested (\$)(1)
Michael L. Middleton	5,830	—	\$27.70	07/17/2017		
	6,036	—	22.29	12/19/2015	4,210	\$87,189
	20,164	—	15.89	12/27/2014		
	4,344	—	27.70			
William J. Pasenelli	5,397	—	22.29	07/17/2017	2,868	\$59,396
	10,298	—	15.89	12/19/2015		
	4,407	—	27.70	12/27/2014		
Gregory C. Cockerham	4,407	—	27.70	07/17/2017	1,947	\$40,322
	5,476	—	22.29	12/19/2015		
	7,582	—	15.89	12/27/2014		

(1) Based upon the Company’s closing stock price of \$20.71 at December 31, 2013.

## **RETIREMENT BENEFITS**

The Bank maintains salary continuation agreements with each of the named executive officers to provide the executives with additional compensation at retirement or upon termination of employment due to death, disability or a change in control. Messrs. Middleton, Pasenelli and Cockerham are entitled to a total annual benefit for a period of 15 years of \$128,048, \$92,212 and \$77,035, respectively, upon normal retirement at or after age 62 for Mr. Middleton and 65 for Messrs. Pasenelli and Cockerham. A reduced benefit is payable if the executive retires before normal retirement age. The annual benefits are payable on a monthly basis to the executives or their designated beneficiaries.

The Bank also maintains a supplemental executive retirement plan (“SERP”) with Messrs. Middleton, Pasenelli and Cockerham to provide the executives with additional compensation at retirement or upon termination of employment due to death, disability or a change in control. Messrs. Middleton, Pasenelli and Cockerham are entitled to a total annual benefit for a period of 15 years of \$28,348, \$66,373 and \$10,484, respectively, upon normal retirement at or after age 65 for Messrs. Pasenelli and Cockerham and age 67 in the case of Mr. Middleton. A reduced benefit is payable if the executive retires before normal retirement age. The annual benefits are payable on an annual basis to the executives or their designated beneficiaries.

The Bank maintains an Executive Deferred Compensation Plan under which Messrs. Middleton, Pasenelli and Cockerham may defer all or any portion of their base salary. Deferred amounts will be credited annually with interest at a rate equal to the Company’s return on equity for the calendar year. The executive’s account balance under the plan will be distributed to the executive following the executive’s termination of service in either a lump sum or over a period of one to five years, as elected by the executive.

## **OTHER POTENTIAL POST-TERMINATION BENEFITS**

**Payments Made Upon Termination with Cause.** Each of the named executive officer's employment agreements contain a definition of cause for which we may terminate the executive's employment. If we terminate the executive's employment for cause, he will receive only his base salary or other compensation earned through the date of termination and retain the rights to any vested benefits subject to the terms of the plan or agreement under which those benefits are provided.

The SERPs for Messrs. Middleton, Pasenelli and Cockerham contain a definition of cause for which we may terminate the executive's employment. If the executive's employment is terminated for cause, they will not be entitled to any benefits under the terms of the SERPs.

Under the 1995 Stock Option and Incentive Plan, if we terminate an executive for just cause (as defined in the plan), any stock option granted under the plan and held by the terminated employee is cancelled upon the date of termination.

Pursuant to the 2005 Equity Compensation Plan, if an executive is terminated for cause, all rights to any restricted stock and long-term restricted stock units award granted under the plan and held by the terminated employee will expire as of the effective date of termination.

**Payments Made Upon Termination Without Cause.** If we terminate Mr. Middleton's employment without cause, he will receive (1) his base salary or other compensation earned through the date of termination, a pro rata share of the average bonus or other cash compensation for the three years preceding the termination and retain the rights to any vested benefits subject to the terms of the plan or agreement under which those benefits are provided, and (2) a lump sum payment equal to his base salary for the remaining term of the agreement and five times his most recent annual incentive compensation payment. We would also continue Mr. Middleton's medical, dental and life insurance benefits for 60 months.

Under his employment agreement, if we terminate the employment of Mr. Pasenelli without cause, he would receive a lump sum payment equal to three times his base salary and three times his most recent annual incentive compensation payment. Under Mr. Cockerham's employment agreement, if we terminate his employment without cause, he would receive a lump sum payment equal to two times his base salary and two times his most recent annual incentive compensation payment. We would also continue both executives' medical, dental and life insurance benefits for 36 months.



Pursuant to the 2005 Equity Compensation Plan, if we terminate an executive without cause and unless otherwise determined by the Compensation Committee, all unvested shares of restricted stock and interests under long-term restricted stock units are forfeited as of the termination date of the executive.

**Payments Made Upon Termination by Executive with Good Reason.** If Mr. Middleton voluntarily terminates his employment under circumstances that would constitute good reason (as defined in his employment agreement), he will receive (1) his base salary or other compensation earned through the date of termination, a pro rata share of the average bonus or other cash compensation for the three years preceding the termination and retain the rights to any vested benefits subject to the terms of the plan or agreement under which those benefits are provided, and (2) a lump sum payment equal to his base salary for the remaining term of the agreement and five times his most recent annual incentive compensation payment. We would also continue Mr. Middleton's medical, dental and life insurance benefits for 60 months.

Pursuant to the 2005 Equity Compensation Plan, if an executive voluntarily terminates his or her employment and unless otherwise determined by the Compensation Committee, all unvested shares of common stock and interests under long-term restricted stock units are forfeited as of the termination date of the executive.

**Payments Made Upon Disability.** Under Mr. Middleton's employment agreement, if he becomes disabled and we terminate his employment pursuant to the terms of the agreement, he will receive his base salary or other compensation earned through the date of termination and retain the rights to any vested benefits subject to the terms of the plan or agreement under which those benefits are provided. In addition, Mr. Middleton will be entitled to disability pay equal to 100% of his base salary in effect at the date of termination. He would continue to receive disability payments until the earlier of (1) 180 days after his termination of employment, (2) the date on which long-term disability insurance benefits are first paid to him, (3) his death, or (4) the date his employment agreement would have terminated had his employment not terminated because of disability. If the disability benefits terminate because 180 days have lapsed or because the date his employment agreement would have terminated had his employment not terminated because of disability is reached, Mr. Middleton will receive disability pay equal to 60% of his base salary during an additional period ending on the earliest of (1) the date on which long-term disability insurance benefits are first paid to him, (2) his death, or (3) the date his employment agreement would have terminated had his employment not terminated because of disability. While receiving benefits under any long-term disability insurance plan, the Company will supplement any disability benefits received by Mr. Middleton to ensure that the aggregate amount received by Mr. Middleton equals 60% of his base salary. Mr. Middleton would continue to participate in our benefit plans until the date his employment agreement would have terminated had his employment not terminated because of disability.

Under Mr. Pasenelli's and Mr. Cockerham's employment agreements, if we terminate an executive due to disability pursuant to the terms of the agreement, the executive will receive the compensation and benefits provided for under the agreement for (1) any period during the term of the agreement and before the establishment of the executive's disability; or (2) any period of disability before the executive's termination of employment due to disability.

The SERPs for Messrs. Middleton, Pasenelli and Cockerham provide for a disability benefit equal to the executive's accrued benefit, calculated as of the date of determination of disability. Payment of the disability benefit will commence on the first day of the month following the earlier of the executive's 65<sup>th</sup> birthday or death and shall be paid in 15 equal annual installments.

Under the salary continuation agreements dated September 6, 2003, as amended, upon termination of employment as a result of disability, Messrs. Middleton, Pasenelli and Cockerham are entitled to an annual benefit for a period of 15 years of \$128,048, \$74,112 and \$72,235, respectively, commencing with the month following the executive attaining age 65, or in Mr. Middleton's case, age 62. Under the salary continuation agreements dated August 21, 2006, as amended, Messrs. Pasenelli and Cockerham are entitled to an annual disability benefit ranging from \$10,637 to \$18,100 and \$3,282 to \$4,800, respectively, depending on the date of termination, commencing with the month following the executive attaining age 65.

Under the 1995 Stock Option and Incentive Plan, if we terminate an executive's employment due to a disability, outstanding stock options will vest and remain exercisable until the earlier of one year from the date of termination or the expiration date of the stock options.

Pursuant to the 2005 Equity Compensation Plan, if we terminate an executive's employment due to a disability, outstanding restricted stock and long-term restricted stock unit awards will immediately vest as of the date of termination.

**Payments Made Upon Death.** Under Mr. Middleton's employment agreement, upon Mr. Middleton's death, Mr. Middleton's beneficiary will receive any base salary compensation earned through the date of death, plus any other compensation or benefits to be provided in accordance with the terms and provisions of the Company's benefit plans and programs.

Under Mr. Pasenelli's and Mr. Cockerham's employment agreements, upon the executive's death, the Company will pay his or her beneficiary or estate any compensation due to the executive through the end of the month in which death occurred, plus any other compensation or benefits to be provided in accordance with the terms and provisions of the Company's benefit plans and programs.

Mr. Middleton's, Mr. Pasenelli's and Mr. Cockerham's SERPs provide for a death benefit equal to the executive's accrued benefit, payable to the executive's beneficiary in 15 equal annual installments beginning the second month following the death of the executive if the executive dies before reaching normal retirement age. If the executive dies after the commencement of the SERP benefit payments, the executive's beneficiary is entitled to the unpaid balance of the executive's 15 annual benefit payments.

Under their salary continuation agreements, if the executive dies while in active service with the Bank, Mr. Middleton's, Mr. Pasenelli's and Mr. Cockerham's designated beneficiaries will receive an annual benefit, for a period of 15 years, of \$128,048, \$92,212 and \$77,035, respectively, commencing with the month following the executive's death. If the executive dies after his employment has terminated but before payments under the agreement have commenced, their designated beneficiary will be entitled to the same payments beginning on the first day of the month after the executive's death.

Under the 1995 Stock Option and Incentive Plan, if an executive dies, outstanding stock options will vest and remain exercisable until the earlier of two years from the date of death or the expiration date of the stock options.

Pursuant to the 2005 Equity Compensation Plan, if an executive dies, outstanding awards vest immediately.

**Payments Made Upon a Change in Control.** Mr. Middleton's employment agreement provides that if during the two-year period following a change in control (as defined in the agreement), Mr. Middleton terminates employment

for any reason, he will be entitled to (1) his base salary or other compensation earned through the date of termination, a pro rata share of the average bonus or other cash compensation for the three years preceding the termination and retain the rights to any vested benefits subject to the terms of the plan or agreement under which those benefits are provided, and (2) a lump sum payment equal to his base salary for the remaining term of the agreement and five times his most recent annual incentive compensation payment. We would also continue Mr. Middleton's medical, dental and life insurance benefits for 60 months. Mr. Middleton would also be entitled to these payments and benefits if Mr. Middleton's employment is terminated due to death or disability and (1) the termination occurs within one year after a change in control, or (2) the termination occurs within one year after a preliminary change in control (as defined in the agreement) and a change in control occurs within two years after such termination. Section 280G of the Internal Revenue Code provides that payments related to a change in control that equal or exceed three times the individual's "base amount" (defined as average annual taxable compensation over the five preceding calendar years) constitute "excess parachute payments." Individuals who receive excess parachute payments are subject to a 20% excise tax on the amount that exceeds the base amount, and the employer may not deduct such amounts. Mr. Middleton's employment agreement provides for an additional tax indemnification payment if payments under the agreement exceed three times his base amount ("280G Limit"). The indemnification payment provides the executive with a net amount sufficient to pay the excise tax and related taxes to place Mr. Middleton in the same economic position in which he would have been had the 280G Limit not applied.

Mr. Pasenelli's employment agreement provides that if (1) the executive's employment is terminated without cause or without the executive's consent and for a reason other than cause in connection with or within 12 months after a change in control (as defined in the agreement); or (2) the executive voluntarily terminates employment within 12 months following a change in control upon the occurrence of events described in the agreement, he will receive a lump sum payment equal to three times his annual base salary and three times his most recent annual incentive compensation payment, plus continued health and welfare benefits for 36 months following termination. Under Mr. Cockerham's employment agreement, he will receive a lump sum payment equal to two times his annual base salary and two times his most recent annual incentive compensation payment, plus continued health and welfare benefits for 36 months following termination. Mr. Pasenelli's and Mr. Cockerham's employment agreements provide that if the value of the benefits provided under the agreements in connection with a change in control exceed his 280G Limit, his payment will be reduced or revised so that the aggregate payments do not exceed his 280G Limit.

Mr. Middleton's, Mr. Pasenelli's and Mr. Cockerham's SERPs provide that if the executives experience a separation from service within 24 months following a change in control, the executives are entitled to an annual benefit for a period of 15 years of \$28,348, \$66,373 and \$10,484, respectively. The executives will receive the benefit payment in the form of (1) a lump sum, (2) equal annual installments over two years, or (3) equal annual installments over five years, as previously elected by each executive.

Under the salary continuation agreements dated September 6, 2003, as amended, upon the termination of employment within 12 months (24 months in the case of Mr. Middleton) subsequent to a change in control and before age 65 (62 in the case of Mr. Middleton), Mr. Middleton, Mr. Pasenelli and Mr. Cockerham are entitled to an annual benefit for a period of 15 years of \$128,048, \$74,112 and \$72,235, respectively, commencing with the month following the executive attaining age 65 (62 in the case of Mr. Middleton). As with his employment agreement, Mr. Middleton's salary continuation agreement provides for an additional tax indemnification payment if payments under the agreement exceed his 280G Limit. Each of Mr. Pasenelli's and Mr. Cockerham's salary continuation agreements dated September 6, 2003, as amended, provide that if the value of the benefits provided in connection with a change in control exceed his 280G Limit, his payment will be reduced or revised so that the aggregate payments do not exceed his 280G Limit. Under the salary continuation agreement dated August 21, 2006, as amended, Mr. Pasenelli is entitled to an additional annual benefit ranging from \$11,314 to \$18,100 (based on the date of termination) if his employment is terminated within 12 months subsequent to a change in control and before age 65. Under the salary continuation agreement dated August 21, 2006, as amended, Mr. Cockerham is entitled to an additional annual benefit equal to the present value of \$4,800 using an interest factor of 5% upon the termination of employment within 12 months subsequent to a change in control and before age 65.

In the event of a change in control of The Community Financial or Community Bank of the Chesapeake, outstanding stock options granted pursuant to our 1995 Stock Option and Incentive Plan automatically vest and, unless otherwise provided for by the committee administering the plan, the option holder will receive in cash an amount equal to the difference between the fair market price of the securities and the exercise price of the option for each option held. Under the Company's 2005 Equity Compensation Plan, a change in control accelerates the vesting of all outstanding stock options, restricted stock awards and long-term restricted stock units. The value of the accelerated options count toward the executive's 280G Limit.



## OTHER INFORMATION RELATING TO

### DIRECTORS AND EXECUTIVE OFFICERS

**Section 16(a) Beneficial Ownership Reporting Compliance.** Pursuant to federal securities laws, the Company's officers, directors and persons who own more than 10% of the outstanding common stock are required to file reports detailing their ownership and changes of ownership in such common stock, and to furnish the Company with copies of all such reports. Based solely on its review of the copies of such reports received during the past fiscal year and written representations from such persons that no additional reports of changes in beneficial ownership were required, the Company believes that during 2013, all of its officers, directors and all of its stockholders owning in excess of 10% of the outstanding common stock of the Company, have complied with the reporting requirements, except for two late reports filed by Todd L. Capitani, Executive Vice President and Senior Financial Officer of the Company, with regard to awards of restricted stock and one late report filed by Mr. Pasenelli with regard to the exercise of stock options and the tendering of shares for tax withholding purposes.

**Policies and Procedures for Approval of Related Persons Transactions.** We maintain a Policy and Procedures Governing Related Person Transactions, which is a written policy and set of procedures for the review and approval or ratification of transactions involving related persons. Under the policy, related persons consist of directors, director nominees, executive officers, persons or entities known to us to be the beneficial owner of more than five percent of any outstanding class of the voting securities of the Company, or immediate family members or certain affiliated entities of any of the foregoing persons.

Transactions covered by the policy consist of any financial transaction, arrangement or relationship or series of similar transactions, arrangements or relationships, in which:

- the aggregate amount involved will or may be expected to exceed \$50,000 in any calendar year;
- the Company is, will or may be expected to be a participant; and
- any related person has or will have a direct or indirect material interest.

The policy excludes certain transactions, including:

- any compensation paid to an executive officer of the Company if the Governance Committee of the Board approved (or recommended that the Board approve) such compensation;
- any compensation paid to a director of the Company if the Board or an authorized committee of the Board approved such compensation; and
- any transaction with a related person involving consumer and investor financial products and services provided in the ordinary course of the Company's business and on substantially the same terms as those prevailing at the time for



comparable services provided to unrelated third parties or to the Company's employees on a broad basis (and, in the case of loans, in compliance with the Sarbanes-Oxley Act of 2002).

Related person transactions will be approved or ratified by the Audit Committee. In determining whether to approve or ratify a related person transaction, the Audit Committee will consider all relevant factors, including:

- whether the terms of the proposed transaction are at least as favorable to the Company as those that might be achieved with an unaffiliated third party;
- the size of the transaction and the amount of consideration payable to the related person;
- the nature of the interest of the related person;
- whether the transaction may involve a conflict of interest; and
- whether the transaction involves the provision of goods and services to the Company that are available from unaffiliated third parties.

A member of the Audit Committee who has an interest in the transaction will abstain from voting on approval of the transaction, but may, if so requested by the chair of the Audit Committee, participate in some or all of the discussion.

**Relationships and Transactions with the Company and the Bank.** The Sarbanes-Oxley Act of 2002 generally prohibits loans by the Company to its executive officers and directors. However, the Sarbanes-Oxley Act contains a specific exemption from such prohibition for loans by the Bank to its executive officers and directors in compliance with federal banking regulations. Federal regulations require that all loans or extensions of credit to executive officers and directors of insured financial institutions must be made on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with other persons not related to the Bank and must not involve more than the normal risk of repayment or present other unfavorable features. The Bank is therefore prohibited from making any new loans or extensions of credit to executive officers and directors at different rates or terms than those offered to the general public. Notwithstanding this rule, federal regulations permit the Bank to make loans to executive officers and directors at reduced interest rates if the loan is made under a benefit program generally available to all other employees and does not give preference to any executive officer or director over any other employee. The Bank does not currently have such a program in place. From time to time, the Bank makes loans and extensions of credit to its executive officers and directors, and members of their immediate families. The outstanding loans made to our directors and executive officers, and members of their immediate families, were made in the ordinary course of business, were made on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable loans with persons not related to the Bank, and did not involve more than the normal risk of collectibility or present other unfavorable features. As of December 31, 2013, these loans were performing according to their original terms.

In accordance with banking regulations, the Board of Directors reviews all loans made to a director or executive officer in an amount that, when aggregated with the amount of all other loans to such person and his or her related interests, exceed the greater of \$25,000 or 5% of the Company's capital and surplus (up to a maximum of \$500,000), and such loan must be approved in advance by a majority of the disinterested members of the Board of Directors.

## **STOCKHOLDER PROPOSALS AND NOMINATIONS**

To be eligible for inclusion in the Company's proxy materials for next year's annual meeting of stockholders, any stockholder proposal to take action at such meeting must be received at the Company's main office at 3035 Leonardtown Road, Waldorf, Maryland 20601 no later than November 25, 2014. If next year's annual meeting is held on a date more than 30 calendar days from May 5, 2015, a stockholder proposal must be received by a reasonable time before the Company begins to print and mail its proxy solicitation materials. Any stockholder proposals will be subject to the requirements of the proxy rules adopted by the Securities and Exchange Commission.

Stockholder proposals, other than those submitted above, and nominations must be submitted in writing, delivered or mailed by first class United States mail, postage pre-paid, to the Secretary of the Company not fewer than 30 days nor

more than 60 days before any such meeting; provided, however, that if notice or public disclosure of the meeting is given fewer than 40 days before the meeting, such written notice shall be delivered or mailed to the Secretary of the Company not later than the close of the 10<sup>th</sup> day following the day on which notice of the meeting was mailed to stockholders.

## **BOARD POLICIES REGARDING COMMUNICATIONS**

### **WITH THE BOARD OF DIRECTORS**

The Board of Directors maintains a process for stockholders to communicate with the Board of Directors. Stockholders wishing to communicate with the Board of Directors should send any communication to the Secretary, The Community Financial Corporation, 3035 Leonardtown Road, Waldorf, Maryland 20601. Any communication must state the number of shares beneficially owned by the stockholder making the communication. The Secretary will forward such communication to the full Board of Directors or to any individual director or directors to whom the communication is addressed unless the communication is unduly hostile, threatening, illegal or similarly inappropriate, in which case the Secretary has the authority to discard the communication or take appropriate legal action regarding the communication.

### **MISCELLANEOUS**

The Company will pay the cost of this proxy solicitation. The Company will reimburse brokerage firms and other custodians, nominees and fiduciaries for reasonable expenses incurred by them in sending proxy materials to the beneficial owners of the common stock. In addition to conducting solicitations by mail, directors, officers and regular employees of the Company may solicit proxies personally or by telephone without additional compensation.

The Company's 2013 Annual Report to Stockholders, including financial statements, accompanies this proxy statement. Such Annual Report is not to be treated as a part of the proxy solicitation material nor as having been incorporated herein by reference. **A copy of the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2013, as filed with the Securities and Exchange Commission, will be furnished without charge to stockholders as of March 7, 2014, upon written request to the Secretary, The Community Financial Corporation, 3035 Leonardtown Road, Waldorf, Maryland 20601.**

[The Community Financial Corporation Letterhead]

Dear ESOP Participant:

On behalf of the Board of Directors, I am forwarding to you the attached vote authorization form to convey your voting instructions to Joseph V. Stone, Jr. and H. Beaman Smith, Trustees for the Community Bank of the Chesapeake Employee Stock Ownership Plan and Trust (the "ESOP") on the proposals presented at the Annual Meeting of Stockholders of The Community Financial Corporation (the "Company") on May 5, 2014. Also enclosed is a Notice of Annual Meeting and Proxy Statement for the Company's Annual Meeting of Stockholders and a The Community Financial Corporation 2013 Annual Report to Stockholders.

As an ESOP participant, you are entitled to instruct the ESOP Trustees how to vote the shares of Company common stock allocated to your ESOP account as of March 7, 2014, the record date for the Annual Meeting. The Trustees will vote all allocated shares of Company common stock as directed by ESOP participants. The Trustees will vote unallocated shares of common stock held in the ESOP Trust and the shares for which timely instructions are not received in a manner calculated to most accurately reflect the instructions received from ESOP participants, subject to the exercise of their fiduciary duties.

To direct the ESOP Trustees how to vote the shares of common stock allocated to your ESOP account, please complete and sign the enclosed vote authorization form and return it to the attention of Marlene Smith at the address indicated on the vote authorization form no later than **April 28, 2014**.

Sincerely,

/s/ Michael L. Middleton  
Michael L. Middleton  
*Chairman of the Board and Chief Executive Officer*

**VOTE AUTHORIZATION FORM**

**COMMUNITY BANK OF THE CHESAPEAKE**

**EMPLOYEE STOCK OWNERSHIP PLAN AND TRUST**

**THE COMMUNITY FINANCIAL CORPORATION**

**Annual Meeting of Stockholders – May 5, 2014**

With respect to all shares of common stock of The Community Financial Corporation (the “Company”) that are allocated to the account of the undersigned pursuant to the Community Bank of the Chesapeake Employee Stock Ownership Plan and Trust (the “ESOP”), the undersigned hereby directs Joseph V. Stone, Jr. and H. Beaman Smith, as Trustees of the Trust established under the ESOP, to vote such shares at the Annual Meeting of Stockholders (the “Meeting”) to be held at the Community Bank of the Chesapeake, Waldorf, Maryland, on Monday, May 5, 2014 at 10:00 a.m., local time, and at any and all adjournments thereof as follows:

**The Board of Directors recommends a vote “FOR” all of the nominees and “FOR” Proposals 2 and 3.**

You are to vote my shares as follows:

x PLEASE MARK VOTES AS IN THIS EXAMPLE

**1. ELECTION OF DIRECTORS**

**FOR** all nominees “ **WITHHOLD AUTHORITY** to vote “ **\*EXCEPTIONS\***  
listed below for all nominees listed below

Philip T. Goldstein, James R. Shepherd and M. Arshed Javaid

**(INSTRUCTIONS: To withhold authority to vote for any individual nominee, mark the “Exceptions” box and write that nominee’s name in the space provided below).**

\*Exceptions: \_\_\_\_\_

**2. THE RATIFICATION OF THE APPOINTMENT OF STEGMAN & COMPANY AS THE INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM FOR THE FISCAL YEAR ENDING DECEMBER 31, 2014**

FOR AGAINST ABSTAIN

.. .. .

**3. THE APPROVAL OF A NON-BINDING RESOLUTION ON THE COMPENSATION OF THE NAMED EXECUTIVE OFFICERS.**

FOR AGAINST ABSTAIN

.. .. .

The undersigned acknowledges receipt from the Company prior to the execution of this vote authorization form of the Notice of Annual Meeting, a Proxy Statement for the Annual Meeting and the Company's 2013 Annual Report.

PARTICIPANT'S NAME

Dated: \_\_\_\_\_, 2014

SIGNATURE OF PARTICIPANT

**Please complete this direction form, sign, date and return it to the Company, Attn: Marlene Smith, The Community Financial Corporation, 3035 Leonardtown Road, Waldorf, Maryland 20601 by April 28, 2014.**





