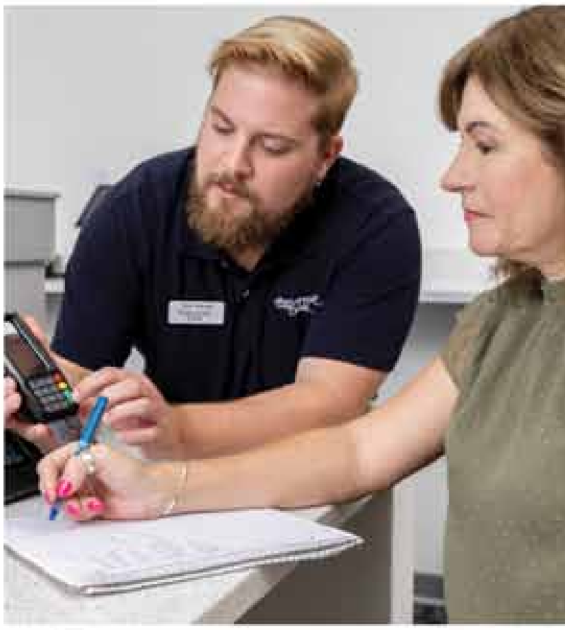
CHESAPEAKE FINANCIAL SHARES INC.

Beyond Banking



2022 by the Numbers

155

Organizations Served by Our Volunteers

124

Employees Volunteered

31 of those held officer positions

$3.73 Earnings Per Share

20.89% Return on Equity

Top 50 Best Banks to Work For

and

TOP 200 Community Banks

(based on three-year average ROE)

2022 designation by

AMERICAN BANKER

Over

4,200

Small Businesses

Served

Our customers rated our service 4.78 out of 5 based on 2022 surveys.

4,847

Volunteer Hours in 2022

Over

35,000

Customers Served

DEAR SHAREHOLDER

"Wow, what a year 2022 was! Coming off over a decade of relatively low-interest rate volatility, the Federal Reserve raised interest rates 4.25% in the last 10 months of the year in an effort to curb inflation. Despite the "active" rate market, Chesapeake Financial Shares was able to have a sixth straight record-breaking year. Attraction and retention of good employees has been a decades-long effort and pays off for us on a daily basis in the form of good customer service and being nimble. 2022 is a great example of this.

Our net income for 2022 was $17,628,587 representing a 17.4% increase over 2021. We welcomed a slight total asset contraction of 4.1% coming off of total asset increases in the prior two years of 26% and 13%, respectively, resulting in total assets of $1,328,997,182 on December 31. We maintained an 11% net loan growth during 2022 even with interest rates rising precipitously. All three of our specialty lines of business, Chesapeake Payment Systems, Flexent, and Chesapeake Wealth Management, added significantly to our consolidated net earnings.

2022 also marked the passing of significant contributors to our collective tapestry. Queen Elizabeth, Mikhail Gorbachev, Hershel "Woody" Williams (last remaining WWII Medal of Honor recipient), Bill Russell, Angela Lansbury, Barbara Walters, and Pelé all added to our world, and their contributions will be missed.

Our Annual Report cover highlights people, both employees and customers, emphasizing financial services goes far beyond banking. Financial services is meeting human and community needs with human solutions in an increasingly digital world. Thank you for being a shareholder and participating in this common mission. Please join us Friday, April 7th, for our Annual Shareholders Meeting.

I look forward to seeing you there.

Sincerely,

Jeffrey M. Szyperski

Jeffrey M. Szyperski
Chairman, CEO & President
Chesapeake Financial Shares, Inc.

	2022	2021	2020	2019	2018
	(Dollars in thousands except ratios and per share amounts)				
Results of Operations					
Interest income	$ 47,276	$ 44,901	$ 38,563	$ 37,673	$ 32,546
Interest expense	3,191	3,346	5,051	8,140	4,975
Net interest income	44,085	41,555	33,512	29,533	27,571
Provision for (reversal of) loan losses	700	(400)	1,950	525	525
Net interest income after provision for loan losses	43,385	41,955	31,562	29,008	27,046
Noninterest income	22,192	19,312	19,624	20,584	18,508
Noninterest expense	45,124	43,954	37,391	36,288	33,356
Income before income taxes	20,453	17,313	13,795	13,304	12,198
Income tax expense	2,824	2,303	2,046	1,905	1,378
Net income	$ 17,629	$ 15,010	$ 11,749	$ 11,399	$ 10,820
Financial Condition					
Total assets	$ 1,328,997	$ 1,385,816	$ 1,204,733	$ 958,306	$ 854,766
Total deposits	1,166,240	1,124,972	1,019,501	839,116	749,181
Net loans	733,300	656,786	544,439	531,113	506,204
Subordinated notes	20,000	20,000	–	–	–
Short-term debt	45,979	99,046	50,000	–	–
Trust preferred capital notes	5,155	5,155	5,155	5,155	5,155
Shareholders' equity	79,067	126,137	122,666	105,443	92,726
Average assets	1,337,782	1,311,403	1,112,051	932,397	820,677
Average shareholders' equity	84,377	126,454	114,443	102,821	89,659
Key Financial Ratios					
Return on average assets	1.32%	1.14%	1.06%	1.22%	1.32%
Return on average equity	20.89%	11.87%	10.27%	11.09%	12.07%
Cash dividends paid as a percent of net income	15.52%	16.99%	20.77%	21.09%	20.79%
Per Share Data**					
Net income, diluted	$ 3.73	$ 3.11	$ 2.40	$ 2.29	$ 2.18
Cash dividends declared	$ 0.58	$ 0.53	$ 0.50	$ 0.49	$ 0.46
Book value	$ 16.78	$ 26.66	$ 25.40	$ 21.36	$ 18.86

***On July 19, 2019, the Board of Directors approved a 6-for-5 stock dividend of CFS's common stock paid on October 15, 2019. All per share information for all periods presented has been retroactively restated to reflect the stock dividend.*

To the Board of Directors and Shareholders
Chesapeake Financial Shares, Inc.
Kilmarnock, Virginia

Opinion

We have audited the consolidated financial statements of Chesapeake Financial Shares, Inc. and its subsidiaries (the "Company"), which comprise the consolidated balance sheets as of December 31, 2022 and 2021, the related consolidated statements of income, comprehensive income (loss), changes in shareholders' equity, and cash flows for the years then ended, and the related notes to the consolidated financial statements (collectively, the financial statements).

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2022 and 2021, and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

We have also audited, in accordance with auditing standards generally accepted in the United States of America (GAAS), the Company's internal control over financial reporting as of December 31, 2022, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission in 2013, and our report dated February 14, 2023 expressed an unmodified opinion on the effectiveness of the Company's internal control over financial reporting.

Basis for Opinion

We conducted our audits in accordance with auditing standards generally accepted in the United States of America (GAAS). Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report. We are required to be independent of the Company and to meet our other ethical responsibilities, in accordance with the relevant ethical requirements relating to our audits. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Responsibilities of Management for the Financial Statements

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

In preparing the financial statements, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the Company's ability to continue as a going concern within one year after the date that the financial statements are issued or available to be issued.

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with GAAS will always detect a material misstatement when it exists. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Misstatements are considered material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the financial statements.

In performing an audit in accordance with GAAS, we:

- Exercise professional judgment and maintain professional skepticism throughout the audit.
- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances.
- Evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the financial statements.
- Conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about the Company's ability to continue as a going concern for a reasonable period of time.

Other Information Included in the Annual Report

Management is responsible for the other information included in the annual report. The other information comprises the information included in the annual report but does not include the financial statements and our auditor's report thereon. Our opinion on the financial statements does not cover the other information, and we do not express an opinion or any form of assurance thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and consider whether a material inconsistency exists between the other information and the financial statements, or the other information otherwise appears to be materially misstated. If, based on the work performed, we conclude that an uncorrected material misstatement of the other information exists, we are required to describe it in our report.

We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings, and certain internal control–related matters that we identified during the audit.

Elliott Davis, PLLC

Raleigh, North Carolina
February 14, 2023

	December 31, 2022	2021
Assets		
Cash and due from banks	$ 24,843,967	$ 18,600,125
Interest-bearing deposits in banks and federal funds sold	1,551,378	2,189,615
Securities available for sale, at fair value	446,449,281	600,644,067
Other investments, at cost	3,222,100	5,547,600
Loans held for sale	–	618,000
Small Business Administration Payroll Protection Program ("SBA-PPP") loans receivable, net of fees	6,450	2,642,603
Loans, net of allowance for loan losses of $7,512,577 in 2022 and $6,793,400 in 2021	733,300,380	656,785,773
Cash management accounts, net of allowance of $1,898,616 in 2022 and $1,426,204 in 2021	27,243,315	26,377,378
Commercial mortgage loan repurchasing facilities	8,128,060	5,084,305
Premises and equipment, net	23,863,901	22,779,715
Accrued interest receivable	5,856,331	6,253,845
Bank-owned life insurance	17,751,505	17,331,209
Bank-owned annuity contract	3,592,671	3,616,990
Foreclosed assets	970,812	1,278,062
Other assets	32,217,031	16,066,888
Total assets	$ 1,328,997,182	$ 1,385,816,175
Liabilities and Shareholders' Equity		
Deposits:		
Demand accounts	$ 343,930,336	$ 313,857,448
Savings and interest-bearing demand deposits	702,647,684	671,804,955
Certificates of deposit		
Denominations less than $250,000	97,887,337	115,942,075
Denominations of $250,000 or more	21,774,631	23,367,029
Total deposits	1,166,239,988	1,124,971,507
Trust preferred capital notes	5,155,000	5,155,000
Short-term debt	45,979,000	99,046,000
Subordinated notes	20,000,000	20,000,000
Accrued interest payable	144,003	112,818
Accrued expenses and other liabilities	12,412,042	10,393,963
Total liabilities	$ 1,249,930,033	$ 1,259,679,288
Shareholders' equity:		
Preferred stock, par value $1 per share; authorized 50,000 shares; no shares outstanding	$ –	$ –
Common stock, voting, par value $5 per share; authorized 5,760,000 shares; 4,713,265 and 4,729,475 issued and outstanding at December 31, 2022 and 2021, respectively	23,417,910	23,484,300
Common stock, nonvoting, par value $5 per share; authorized 635,000 shares; no shares outstanding	–	–
Additional paid-in capital	14,072,355	14,806,975
Retained earnings	91,707,848	76,815,064
Accumulated other comprehensive (loss) income	(50,130,964)	11,030,548
Total shareholders' equity	79,067,149	126,136,887
Total liabilities and shareholders' equity	$ 1,328,997,182	$ 1,385,816,175

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

	Years Ended December 31, 2022	2021
Interest and Dividend Income		
Interest and fees on loans	$ 33,175,365	$ 32,935,384
Interest on interest-bearing deposits and federal funds sold	66,225	35,643
Interest and dividends on securities available for sale:		
Taxable	8,960,471	7,142,319
Nontaxable	4,837,281	4,604,841
Dividends	237,015	182,396
Total interest and dividend income	47,276,357	44,900,583
Interest Expense		
Savings and interest-bearing demand deposits	1,037,977	566,309
Certificates of deposit	708,573	2,000,037
Short-term debt	608,522	147,867
Subordinated notes and trust preferred capital notes	836,534	631,600
Total interest expense	3,191,606	3,345,813
Net interest income	44,084,751	41,554,770
Provision for (reversal of) loan losses	699,996	(400,004)
Net interest income after provision for loan losses	43,384,755	41,954,774
Noninterest Income		
Trust and wealth management income	4,074,761	4,391,806
Service charges	972,320	770,347
Net (loss) gain on sales of securities available for sale	(3,303,287)	730,035
Mortgage banking income	1,678,833	2,776,845
Merchant services income, net	4,934,928	4,061,549
Cash management fee income	3,196,595	2,025,501
Other income	10,637,771	4,556,125
Total noninterest income	22,191,921	19,312,208
Noninterest Expenses		
Salaries and benefits	25,627,048	23,760,395
Occupancy expenses	3,483,084	3,717,489
Net loss on foreclosed assets	69,778	399,989
Provision for cash management account losses	240,000	1,845,000
Other expenses	15,704,575	14,231,308
Total noninterest expenses	45,124,485	43,954,181
Income before income taxes	20,452,191	17,312,801
Income tax expense	2,823,604	2,303,287
Net income	$ 17,628,587	$ 15,009,514
Earnings per common share, basic	$ 3.74	$ 3.12
Earnings per common share, diluted	$ 3.73	$ 3.11

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

	Years Ended December 31, 2022	2021
Net income	$ 17,628,587	$ 15,009,514
Other comprehensive income:		
Gross unrealized losses on securities available for sale	(75,798,041)	(8,116,650)
Deferred tax benefit	15,917,589	1,704,497
	(59,880,452)	(6,412,153)
Unrealized (losses) gains on cash flow hedge	(4,924,882)	1,726,449
Deferred tax benefit (expense)	1,034,225	(362,555)
	(3,890,657)	1,363,894
Less:		
Reclassification of losses (gains) recognized in net income	3,303,287	(730,035)
Deferred tax (benefit) expense	(693,690)	153,307
	2,609,597	(576,728)
Total other comprehensive loss, net of tax	(61,161,512)	(5,624,987)
Comprehensive (loss) income	$ (43,532,925)	$ 9,384,527

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

Years Ended December 31, 2022 and 2021

	Common Stock, Voting	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
Balance, December 31, 2020	$ 23,988,220	$ 17,667,342	$ 64,355,386	$ 16,655,535	$122,666,483
Net income	–	–	15,009,514	–	15,009,514
Other comprehensive income	–	–	–	(5,624,987)	(5,624,987)
Exercise of stock options	84,670	71,150	–	–	155,820
Issuance of restricted stock	76,940	(76,940)	–	–	–
Stock awards surrendered in cashless exercise	(54,600)	(213,300)	–	–	(267,900)
Issuance of common stock for services	43,515	151,519	–	–	195,034
Repurchase of common stock	(654,445)	(3,142,212)	–	–	(3,796,657)
Stock-based compensation	–	349,416	–	–	349,416
Cash dividends ($0.53 per share)	–	–	(2,549,836)	–	(2,549,836)
Balance, December 31, 2021	$ 23,484,300	$ 14,806,975	$ 76,815,064	$ 11,030,548	$126,136,887
Net income	–	–	17,628,587	–	17,628,587
Other comprehensive loss	–	–	–	(61,161,512)	(61,161,512)
Exercise of stock options	84,960	77,290	–	–	162,250
Issuance of restricted stock	94,410	(94,410)	–	–	–
Stock awards surrendered in cashless exercise	(49,900)	(237,626)	–	–	(287,526)
Issuance of common stock for services	34,215	167,654	–	–	201,869
Repurchase of common stock	(230,075)	(1,059,158)	–	–	(1,289,233)
Stock-based compensation	–	411,630	–	–	411,630
Cash dividends ($0.58 per share)	–	–	(2,735,803)	–	(2,735,803)
Balance, December 31, 2022	$ 23,417,910	$ 14,072,355	$ 91,707,848	$ (50,130,964)	$ 79,067,149

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

	Years Ended December 31, 2022	2021
Cash Flows from Operating Activities		
Net income	$ 17,628,587	$ 15,009,514
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	1,876,243	1,588,646
Provision for (reversal of) loan losses	699,996	(400,004)
Provision for cash management account losses	240,000	1,845,000
Deferred income tax (benefit) expense	(387,678)	122,755
Amortization of investment securities, net	3,921,017	3,750,820
Net loss (gain) on sales of securities available for sale	3,303,287	(730,035)
Net loss on foreclosed assets	69,778	399,989
Stock-based compensation	411,630	349,416
Origination of loans held for sale	(35,189,753)	(71,839,370)
Proceeds from sale of loans	36,723,501	75,794,642
Gain on sale of loans	(915,748)	(2,040,272)
(Increase) decrease in bank-owned life insurance	(420,296)	344,959
Decrease (increase) in bank-owned annuities	24,319	(3,221)
Changes in other assets and liabilities:		
Decrease in accrued interest receivable	397,514	6,436
(Decrease) increase in other assets	1,369,497	(2,987,237)
Increase (decrease) in accrued interest payable	31,185	(84,760)
(Decrease) increase in accrued expenses and other liabilities	(1,670,709)	4,552,930
Net cash provided by operating activities	$ 28,139,370	$ 25,680,208
Cash Flows from Investing Activities		
Purchases of securities available for sale	$ (56,719,813)	$ (213,903,215)
Proceeds from sales and calls of securities available for sale	83,181,399	4,384,105
Proceeds from maturities and paydowns of securities available for sale	48,011,205	51,182,592
Redemption (purchase) of other investments, net	2,325,500	(1,332,600)
Proceeds from sale of foreclosed assets	237,472	2,533,811
Decrease in SBA-PPP loans receivable, net	2,636,153	49,294,935
Net increase in loans	(77,214,603)	(111,946,676)
Net increase in cash management accounts	(1,105,937)	(11,341,440)
Purchase of residual portfolio	–	(2,057,786)
Capital calls of small business investment company funds and other investments	(2,003,813)	(820,600)
Net increase of commercial mortgage loan repurchase facility	(3,043,755)	(5,084,305)
Purchase of premises and equipment	(2,888,742)	(3,509,240)
Net cash used in investing activities	$ (6,584,934)	$ (242,600,419)

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

	Years Ended December 31, 2022	2021
Cash Flows from Financing Activities		
Net increase in demand accounts, interest-bearing demand accounts and savings accounts	$ 60,915,617	$ 139,968,780
Net decrease in certificates of deposits	(19,647,136)	(34,497,818)
Exercise of stock options	162,250	155,820
Repurchase/surrender of common stock	(1,576,759)	(4,064,557)
Cash dividends	(2,735,803)	(2,549,836)
Proceeds from issuance of subordinated notes	–	20,000,000
Purchase of federal funds	13,933,000	12,046,000
(Decrease) Increase in short-term debt	(67,000,000)	37,000,000
Net cash (used in) provided by financing activities	$ (15,948,831)	$ 168,058,389
Net increase (decrease) in cash and cash equivalents	$ 5,605,605	$ (48,861,822)
Cash and cash equivalents at beginning of year	20,789,740	69,651,562
Cash and cash equivalents at end of year	$ 26,395,345	$ 20,789,740
Supplemental Disclosures of Cash Flow Information		
Cash paid during the year for:		
Interest	$ 2,794,092	$ 3,430,573
Income taxes	$ 2,885,000	$ 2,137,000
Supplemental Schedule of Noncash Investing and Financing Activities		
Unrealized loss on securities available for sale	$ (72,494,754)	$ (8,846,685)
Unrealized (loss) gain on cash flow hedge	(4,924,882)	1,726,449
Issuance of common stock for services	$ 201,869	$ 195,034

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

Note 1. Summary of Significant Accounting Policies

General

Chesapeake Financial Shares, Inc. ("CFS" or "Company") is a bank holding company whose principal business activity consists of ownership in Chesapeake Bank (the "Bank") and Chesapeake Wealth Management, Inc. ("CWM"). The consolidated financial statements include the accounts of CFS and its wholly-owned subsidiaries, except for CFS Capital Trust II (the "Trust"), which is not a consolidated subsidiary of the Company. The subordinated debt payable to the Trust by the Company is reported as a liability of the Company. All significant intercompany accounts have been eliminated.

Subsequent Events

Subsequent events have been considered through February 14, 2023, the same date on which these consolidated financial statements were issued.

Significant Accounting Policies

The accounting and reporting policies of CFS are in accordance with accounting principles generally accepted in the United States of America and conform to general practices within the banking industry. The more significant of these policies are summarized below.

Securities

Debt securities that management has the positive intent and ability to hold to maturity are classified as "held to maturity" and recorded at amortized cost. Equity securities are recorded at fair value with changes in fair value included in earnings. Debt securities not classified as held to maturity or trading are classified as "available for sale" and recorded at fair value, with unrealized gains and losses excluded from earnings and reported in other comprehensive income. Purchase premiums and discounts are recognized in interest income using the interest method over the terms of the securities. Gains and losses on the sale of securities are recorded on the trade date and are determined using the specific identification method. CFS classifies all debt securities as available for sale.

Impairment of securities occurs when the fair value of a security is less than its amortized cost. For debt securities, impairment is considered other-than-temporary ("OTTI") and recognized in its entirety in net income if either (a) the intent is to sell the security or (b) it is more-likely-than-not that it will be necessary to sell the security prior to recovery of its amortized cost. If, however, management's intent is not to sell the security and it is not more than likely that management will be required to sell the security before recovery, management must determine what portion of the impairment is attributable to credit loss, which occurs when the amortized cost of the security exceeds the present value of the cash flows expected to be collected from the security. If there is no credit loss, there is no other-than-temporary impairment. If there is a credit loss, other-than-temporary impairment exists and the credit loss must be recognized in net income and the remaining portion of impairment must be recognized in other comprehensive income. Equity securities are reported at fair value and changes in fair value are included in consolidated earnings. Management regularly reviews each security for other-than-temporary impairment based on criteria that includes the extent to which cost exceeds market price, the duration of that market decline, the financial health of and specific prospects for the issuer, the best estimate of the present value of cash flows expected to be collected from debt securities, the intention with regards to holding the security to maturity, and the likelihood that CFS would be required to sell the security before recovery.

Small Business Administration Paycheck Protection Program

The Small Business Administration Paycheck Protection Program ("SBA-PPP") is one of the centerpieces of the Coronavirus Aid, Relief, and Economic Security Act (the "CARES Act"), which was passed on March 27, 2020 in response to the outbreak of coronavirus ("COVID-19") and was supplemented with subsequent legislation. Overseen by the United States Treasury Department, the SBA-PPP offered cash flow assistance to nonprofit and small business employers through guaranteed loans for expenses incurred between February 15, 2020 and August 8, 2020. A third round of SBA-PPP loans were authorized on December 27, 2020 with applications accepted between January 11 and May 31, 2021. Borrowers are eligible for forgiveness of principal and accrued interest on SBA-PPP loans to the extent that the proceeds are used to cover eligible payroll cost, interest cost, rent and utility cost over a period between 8 and 24 weeks after the loan is made as long as the borrower retains its employees and their compensation levels. The CARES Act authorizes the SBA to fully guarantee these loans.

Due to the unique nature of these provisions, SBA-PPP loans have been disclosed as a separate balance sheet item. Origination fees received by the SBA are capitalized into the carrying amount of the loans. The deferred fee income, net of origination costs, is recognized over the life of the loan as an adjustment to yield using the effective interest method. SBA-PPP loans receivable as of December 31, 2022 totaled $6 thousand with $0 in net unearned fees and generated $97 thousand of interest income during the year ended December 31, 2022. SBA-PPP loans receivable as of December 31, 2021 totaled $2.7 million with $97 thousand in net unearned fees and generated $4 million of interest income during the year ended December 31, 2021.

Loans

The Bank grants mortgage, commercial, and consumer loans to customers. A substantial portion of the loan portfolio is represented by mortgage loans and commercial real estate throughout the Northern Neck, Middle Peninsula, Williamsburg, James City County, and Richmond areas of Virginia. The ability of the Bank's debtors to honor their contracts is dependent upon the real estate and general economic conditions in these areas.

The Bank's recorded investments in loans are stated at face value, net of unamortized premiums and discounts and charge-offs. Interest is computed by methods which result in level rates of return on principal. Nonrefundable loan fees and direct loan origination costs are recognized in operations when received and incurred. The impact of this methodology is not significantly different from recognizing the net of the fees and costs over the contractual life of the related loan.

The Bank analyzes its loan portfolio by segment. Segments are based on the level at which the allowance for loan losses is calculated and monitored. The Bank's loan segments are commercial, commercial – real estate, consumer – non real estate, and residential – real estate. The Bank further segregates each segment of the loan portfolio into classes based on how each loan was initially recorded. Classes are a level of detail that appropriately exhibit the risks inherent in the loan portfolio.

The loan portfolio is segmented based on risk characteristics. Particular characteristics associated with each segment are detailed below:

Commercial: Commercial loans include both secured and unsecured loans for working capital, expansion, and other business purposes. Short-term working capital loans are secured by business assets. The Bank also makes term commercial loans secured by equipment and real estate. Lending decisions are based on an evaluation of the financial strength, cash flow, management and credit history of the borrower, and the quality of the collateral securing the loan. With few exceptions, the Bank requires personal guarantees and secondary sources of repayment. Commercial loans generally provide greater yields and re-price more frequently than other types of loans, such as real estate loans.

Commercial – Real Estate: Loans secured by commercial real estate also carry risks associated with the success of the business and ability to generate a positive cash flow sufficient to service debts. Real estate security diminishes risks only to the extent that a market exists for the subject collateral. Some real estate secured construction loans carry risks that a project will not be completed as scheduled and budgeted and that the value of the collateral may, at any point, be less than the principal amount of the loan.

Consumer – Non Real Estate: Consumer non real estate loans carry risks associated with the continued creditworthiness of the borrower and the value of the collateral, such as automobiles which may depreciate more rapidly than other assets. In addition, these loans may be unsecured. Consumer loans are more likely than real estate loans to be immediately affected in an adverse manner by job loss, divorce, illness, personal bankruptcy, or other life events.

Residential – Real Estate: Consumer real estate loans carry risks associated with the continued creditworthiness of the borrower and changes in the value of the collateral.

Loans of each class are placed on nonaccrual status when a loan is specifically determined to be impaired or when principal or interest is delinquent for 90 days or more. Any unpaid interest previously accrued on those loans is reversed from income. Interest income generally is not recognized on specific impaired loans unless the likelihood of further loss is remote. Interest payments received on such loans are applied as a reduction of the loan principal balance. Generally, the

Bank will return a loan to accrual status when all delinquent interest and principal become current and remain current for six consecutive months under the terms of the loan agreement or the loan is well-secured and in the process of collection.

Mortgage loans held for resale are stated at the lower of cost or market on an individual loan basis. Loan discounts and origination fees received on loans held for resale are deferred until the related loans are sold to third party investors. Gains are recognized at the time of sale.

Allowance for Loan Losses

The allowance for loan losses is established as losses are estimated to have occurred through a provision for loan losses charged to earnings. Loans of each segment are fully or partially charged off against the allowance when the Bank deems the amount to be uncollectible. General conditions for charge-off include repayment schedules that are deemed to be protracted beyond a reasonable timeframe, the loan has been classified as a loss either internally or by regulators, or the loan is 180 days past due unless well-secured and in the process of collection. Subsequent recoveries, if any, are credited to the allowance.

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

The allowance consists of allocated and general components. The allocated component relates to loans that are classified as impaired. For those loans that are classified as impaired, an allowance is established when the discounted cash flows (or the collateral value or observable market price less costs to liquidate) of the impaired loan are lower than the carrying value of that loan. The general component covers non-classified loans and is based on historical charge-off by segment and expected default derived from the Bank's loss experience by loan type. Other adjustments may be made to the allowance based on an assessment of internal or external influences on credit quality that are not fully reflected in the historical loss or risk rating data. Adjustments to the general component of the allowance are made for each segment based on management's assessment of the state of the economy, delinquencies, exceptions to loan underwriting, monitoring policies, various trends, and local unemployment. There were no significant changes to the Bank's allowance methodology during the current year.

A loan in each class is considered impaired when, based on current information and events, it is probable that the Bank 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. Impairment is measured on a loan-by-loan basis by either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's observable market price, or the fair value of the collateral.

Troubled Debt Restructurings

In situations where, for economic or legal reasons related to a borrower's financial condition, management may grant a concession to the borrower that it would not otherwise consider, the related loan is classified as a troubled debt restructuring (TDR). Management strives to identify borrowers in financial difficulty early and work with them to modify their loan to more affordable terms before the loan reaches nonaccrual status. These modified terms may include rate reductions, principal forgiveness, payment forbearance and other actions intended to minimize the economic loss and to avoid foreclosure or repossession of the collateral. In cases where borrowers are granted new terms that provide for a reduction of either interest or principal, management measures any impairment on the restructuring as noted above for impaired loans.

Commercial Mortgage Loan Repurchase Facilities

Commercial mortgage loan repurchase facilities are accounted for as collateralized financing transactions as the terms of purchase agreements do not qualify for sale accounting and are therefore recorded at the amount of cash advanced.

Interest earned is recorded in interest income. Commercial mortgage loan repurchase facilities are collateralized by commercial mortgage loans. The fair value of collateral is monitored daily and additional collateral is obtained or excess collateral is returned for margin maintenance purposes. Collateral accepted under commercial mortgage loan repurchase facilities transactions is not permitted by contract to be sold or repledged.

Premises and Equipment

Land is carried at cost. Premises and equipment are stated at cost less accumulated depreciation. Depreciation is computed using both straight-line and accelerated methods over the assets' estimated useful lives. Estimated useful lives range from 10 to 39 years for buildings and leasehold improvements and 3 to 7 years for furniture, fixtures, and equipment.

The Company determines if an arrangement is a lease at inception. Operating leases are included in operating lease right-of-use (“ROU”) assets and other liabilities on our consolidated balance sheets. Finance leases are included in premises and equipment and other liabilities on our consolidated balance sheets. The amortization of the finance leases are included in occupancy expense on the consolidated income statement. The interest expense on finance leases is included in short-term debt on the consolidated income statement

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 liabilities are recognized at commencement date based on the present value of lease payments over the lease term. Most of the Company’s leases do not provide an implicit rate, as such an incremental borrowing rate is developed based on the information available at commencement date in determining the present value of lease payments has been used. The operating 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 option will be exercised. 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. For certain leases, the lease and non-lease components are accounted for as a single lease component. Additionally, for certain equipment leases, a portfolio approach is applied to effectively account for the operating lease ROU assets and liabilities.

Foreclosed Assets

Foreclosed assets are recorded at the time of foreclosure at their fair value, net of estimated costs to sell. At foreclosure, any excess of the loan balance over the fair value of the property, less cost to sell, is charged to the allowance for loan losses. Such carrying value is periodically reevaluated and written down as a direct expense if there is an indicated decline in the net realizable value. Costs to bring a property to salable condition are capitalized up to the fair value of the property, while costs to maintain a property in salable condition are expensed as incurred.

Transfers of Financial Assets

Transfers of financial assets are accounted for as sales, when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when (a) the assets have been isolated from CFS – put presumptively beyond the reach of the transferor and its creditors, even in bankruptcy or other receivership, (b) 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 (c) CFS does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity or the ability to unilaterally cause the holder to return specific assets.

Derivative Instruments and Hedging Activities

The Company records all derivatives on the balance sheet at fair value. The accounting for changes in the fair value of derivatives depends on the intended use of the derivative and the resulting designation. Derivatives used to hedge the exposure to changes in the fair value of an asset, liability, or firm commitment attributable to a particular risk, such as interest rate risk, are considered fair value hedges. Derivatives used to hedge the exposure to variability in expected future cash flows, or other types of forecasted transactions, are considered cash flow hedges.

For derivatives designated as cash flow hedges, the effective portion of changes in the fair value of the derivative is initially reported in other comprehensive income (outside of earnings) and subsequently reclassified to earnings when the hedged transaction affects earnings, and the ineffective portion of the change in the fair value of the derivative is recognized directly in earnings. The Company assesses the effectiveness of the hedging relationship by comparing the changes in cash flows of the derivative hedging instrument with the changes in cash flows of the designated hedged transactions. The Company does not have any derivatives designated as fair value hedges.

The Company's objective in using derivatives is to add stability to net interest income and to manage its exposure to adverse changes in interest rates.

Income Taxes

The income tax accounting guidance results in two components of income tax expense: current and deferred. Current income tax expense reflects taxes to be paid or refunded for the current period by applying provisions of the enacted tax law to the taxable income or excess deductions over revenues. CFS determines deferred income taxes using the liability (or balance sheet) method. Under this method, the net deferred tax asset or liability is based on the tax effects of the differences between book and tax bases of assets and liabilities, and enacted changes in tax rates and laws are recognized in the period in which they occur.

Deferred income tax expense results from changes in deferred tax assets and liabilities between periods. Deferred tax assets are recognized if it is more-likely-than-not, based on the technical merits, that the tax position will be realized or sustained under examination. The term more-likely-than-not means a likelihood of more than 50 percent; the terms examined and upon examination also include resolution of the related appeals or litigation processes, if any. A tax position that meets the more-likely-than-not recognition threshold is initially and subsequently measured as the largest amount of tax benefit that has a greater than 50 percent likelihood of being realized upon settlement with a taxing authority that has full knowledge of all relevant information. The determination of whether or not a tax position has met the more-likely-than-not threshold considers the facts, circumstances, and information available at the reporting date and is subject to management's judgment. Deferred tax assets are reduced by a valuation allowance if, based on the weight of the evidence available, it is more-likely-than-not that some portion or all of a deferred tax asset will not be realized.

CFS accounts for income taxes in accordance with the accounting guidance related to uncertainty in income taxes, which sets out a consistent framework to determine the appropriate level of tax reserves to maintain for uncertain tax positions.

Consolidated Statements of Cash Flows

For purposes of the consolidated statement of cash flows, CFS considers cash equivalents to include cash on hand, amounts due from banks, interest-bearing deposits, and federal funds sold.

Advertising Costs

CFS follows the policy of charging the production costs of advertising to expense as incurred.

Use of Estimates

In preparing consolidated financial statements in conformity with accounting principles generally accepted in the United States of America, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the balance sheet and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses, the valuation of deferred tax assets, other-than-temporary impairments of securities, and the valuation of foreclosed assets.

Earnings Per Common Share

Basic earnings per common share represents income available to common shareholders divided by the weighted-average number of common shares outstanding during the period. Diluted earnings per common share reflects additional common shares that would have been outstanding if dilutive potential common shares had been issued, as well as any adjustment to income that would result from the assumed issuance. Potential common shares that may be issued by CFS related solely to outstanding stock options and restricted stock, are determined using the treasury stock method.

Cash Management Accounts

CFS purchases trade accounts receivable from customers. These receivables are stated at face value, net of discounts and an allowance for losses. CFS retains reserves against these customer balances in a separate liability account to cover unpaid receivables, returns, allowances and other adjustments.

Stock-Based Compensation

Stock-based compensation accounting requires that the compensation cost relating to stock-based payment transactions be recognized in financial statements. That cost will be measured based on the grant date fair value of the equity or liability instruments issued. The stock compensation accounting guidance covers a wide range of stock-based compensation arrangements including stock options, restricted share plans, and performance-based awards.

The stock-based compensation accounting guidance requires that compensation cost for all stock awards be calculated and recognized over the employees' service periods, generally defined as the vesting period. Compensation cost is recognized on a straight-line basis over the requisite service period for the award. A Black-Scholes model is used to estimate the fair value of stock options, while the fair value of the Company's common stock at the date of grant is used for restricted awards. There were no options granted in 2021 or 2022.

Fair Value of Financial Instruments

Fair values of financial instruments are estimated using relevant market information and other assumptions, as more fully discussed in Note 20. Fair value estimates involve uncertainties and matters of significant judgment. Changes in assumptions or in market conditions significantly affect the estimates.

Assets Under Management

Securities and other property held by Chesapeake Wealth Management in a fiduciary or agency capacity are not assets of CFS and are not included in the accompanying consolidated financial statements.

Recent Accounting Pronouncements

ASU 2016-13:

Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments ("ASU 2016-13"). ASU 2016-13 significantly changes how entities will measure credit losses for most financial assets and certain other instruments that are not measured at fair value through net income. The standard will replace the current incurred loss approach with an expected loss model, referred to as the current expected credit loss ("CECL") model. The new standard will apply to financial assets subject to credit losses and measured at amortized cost and certain off-balance-sheet credit exposures, which include, but are not limited to, loans, leases, held-to-maturity securities, loan commitments and financial guarantees. ASU 2016-13 simplifies the accounting for purchased credit-impaired debt securities and loans and expands the disclosure requirements regarding an entity's assumptions, models and methods for estimating the allowance for loan and lease losses. In addition, entities will need to disclose the amortized cost balance for each class of financial asset by credit quality indicator, disaggregated by the year of origination. For public business entities that meet the definition of a smaller reporting company, such as the Company, the ASU 2016-13 is effective for interim and annual reporting periods beginning after December 15, 2022. Early adoption is permitted in any interim period as long as the Company has adopted to the amendments in ASU 2016-13. Upon adoption, ASU 2016-13 provides for a modified retrospective transition by means of a cumulative effect adjustment to equity as of the beginning of the period in which the guidance is effective.

The Company is finalizing its evaluation of the adoption of this ASU and plans to adopt as of January 1, 2023. The Company to date has selected the software vendor of choice for implementation, sourced and tested required data from the Company's loan systems, tested data feeds to the model, contracted for and received results from independent third parties of model validation of the CECL model and process, determined appropriate segmentations of its portfolio, selected a preliminary forecast period for reasonable and supportable forecasts, and has performed parallel runs of the model. The Company is currently finalizing its assessment of current and forecasted macroeconomic factors and assumptions and testing and finalization of internal controls. The Company currently estimates the allowance for loan losses will increase by a range of $0 and $300 thousand. In addition, the Company expects to recognize a liability for unfunded commitments between $400 thousand and $500 thousand upon adoption. The Company will finalize the adoption during the first quarter of 2023.

Reclassification

Certain items for prior years have been reclassified to conform to the current year presentation. Such reclassifications had no effect on net income, total assets or shareholders' equity as previously reported.

Note 2. Securities

Amortized cost and fair values of securities available for sale as of December 31, 2022 and 2021, are as follows:

2022	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
US Treasury	$ 488,714	$ –	$ (56,507)	$ 432,207
Securities of state and political subdivisions	283,305,105	95,285	(45,795,490)	237,604,900
SBA loan pooled securities	2,295,558	6,107	–	2,301,665
Mortgage-backed securities				
Agency	54,097,779	18,591	(3,860,091)	50,256,279
Non-agency	119,737,078	21,851	(8,190,604)	111,568,325
Other debt securities	47,064,746	2,541	(2,781,382)	44,285,905
Total	$ 506,988,980	$ 144,375	$ (60,684,074)	$ 446,449,281

2021	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
US Treasury	$ 11,892,333	$ 74,346	$ (29,176)	$ 11,937,503
Securities of state and political subdivisions	361,291,152	14,654,427	(2,649,585)	373,295,994
SBA loan pooled securities	2,863,069	8,729	–	2,871,798
Mortgage-backed securities				
Agency	62,691,282	868,719	(612,374)	62,947,627
Non-agency	99,858,493	506,272	(873,165)	99,491,600
Other debt securities	50,092,683	306,537	(299,675)	50,099,545
Total	$ 588,689,012	$ 16,419,030	$ (4,463,975)	$ 600,644,067

The amortized cost and fair value of securities available for sale as of December 31, 2022, by contractual maturity are shown below. Expected maturities may differ from contractual maturities because issuers may have the right to call or prepay obligations without penalties.

	Amortized Cost	Fair Value
Due in one year or less	$ 14,807,896	$ 14,407,948
Due after one year through five years	135,371,466	129,028,992
Due after five years through ten years	209,805,102	186,800,800
Due after ten years	147,004,516	116,211,541
Total	$ 506,988,980	$ 446,449,281

Proceeds from sales of securities available for sale during 2022 and 2021 were $83,181,399 and $4,384,105, respectively. Gross realized gains amounted to $409,140 and $730,035 in 2022 and 2021, respectively. Gross realized losses amounted to $3,712,427 and $0 in 2022 and 2021, respectively.

The amortized cost of securities pledged to secure public deposits, borrowings from the Federal Home Loan Bank, fiduciary powers and for other purposes required or permitted by law amounted to $308,763,670 and $290,480,855 at December 31, 2022 and 2021, respectively.

Temporarily Impaired Securities

Information pertaining to securities with gross unrealized losses at December 31, 2022 and 2021, aggregated by investment category and length of time that individual securities have been in a continuous loss position, follows:

	2022					
	Less Than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Gross Unrealized Losses
US Treasury	$ 432,207	$ 56,507	$ –	$ –	$ 432,207	$ 56,507
Securities of state and political subdivisions	109,190,002	12,407,454	120,949,242	33,388,036	230,139,244	45,795,490
Mortgage-backed securities						
Agency	27,075,590	1,148,776	22,620,808	2,711,315	49,696,398	3,860,091
Non-agency	62,470,676	3,216,781	43,334,723	4,973,823	105,805,399	8,190,604
Other debt securities	18,829,691	829,148	23,983,364	1,952,234	42,813,055	2,781,382
	$ 217,998,166	$ 17,658,666	$ 210,888,137	$ 43,025,408	$ 428,886,303	$ 60,684,074

	2021					
	Less Than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Gross Unrealized Losses
US Treasury	$ 5,312,305	$ 29,176	$ –	$ –	$ 5,312,305	$ 29,176
Securities of state and political subdivisions	104,705,420	2,181,467	10,728,129	468,118	115,433,549	2,649,585
Mortgage-backed securities						
Agency	25,032,197	587,267	2,620,859	25,108	27,653,056	612,375
Non-agency	49,531,641	583,028	13,874,146	290,137	63,405,787	873,165
Other debt securities	23,849,396	221,181	7,544,241	78,493	31,393,637	299,674
	$ 208,430,959	$ 3,602,119	$ 34,767,375	$ 861,856	$ 243,198,334	$ 4,463,975

U.S. Treasury

The unrealized loss on CFS's investment in one U.S. Treasury security is primarily due to changes in interest rates. This security is backed by the full faith and credit of the U.S. government and therefore CFS does not consider the investment to be other-than-temporarily impaired at December 31, 2022.

Securities of State and Political Subdivisions

CFS's unrealized losses on investments in 114 municipal bonds relate to investments in longer-term securities of municipalities throughout the U.S. The unrealized losses are primarily caused by the trend in interest rates. CFS currently does not believe it is probable that it will be unable to collect all amounts due according to the contractual terms of the investments. Because CFS does not intend to sell the investments and it is not more-likely-than-not that CFS will be required to sell the investments before recovery of its par value, which may be maturity, it does not consider these investments to be other-than-temporarily impaired at December 31, 2022.

Mortgage-Backed Securities

The unrealized losses on CFS's investment in 95 government-sponsored enterprise mortgage-backed securities were caused by interest rate movements. CFS purchased those investments at a premium relative to their face amount, and the contractual cash flows of those investments are guaranteed by an agency of the U.S. government. Accordingly, it is expected that the securities would not be settled at a price less than the amortized cost of CFS's investments. CFS does not consider these investments to be OTTI at December 31, 2022 due to the following:

- The decline in the market value is attributable to changes in interest rates and not credit quality;
- CFS does not intend to sell the investments;
- It is not more-likely-than-not that CFS will be required to sell the investments before recovery of their amortized cost basis, which may be maturity.

The unrealized losses associated with 146 private-label residential mortgage-backed securities are primarily driven by higher projected collateral losses, wider credit spreads and changes in interest rates. CFS assessed credit impairment using an economic cash flow model. There was no OTTI impairment recognized as of December 31, 2022.

Management continuously monitors the mortgage-backed securities portfolio for potential permanent impairment. Analytical tools used include robust credit risk analysis. CFS strives to maintain exposure only to securities that have credit support in excess of original issue levels. Generally, it is CFS's intent to hold the securities for the time necessary to recover the amortized cost unless prudent business decisions warrant otherwise.

Other Debt Securities

The 67 investments in this category are primarily made up of student loan backed investments under the Federal Family Education Loan Program (FFELP). These loans are generally insured by the Federal Government at 97% or more of their balances. The investments have investment grade ratings by credible rating agencies. Management determined that the unrealized losses in other debt securities is a result of movements in interest rates and market conditions. There was no OTTI impairment recognized as of December 31, 2022.

Other-Than-Temporary Impairment

CFS routinely conducts periodic reviews to identify and evaluate each investment security to determine whether an OTTI has occurred. The initial indicator of OTTI is a decline in market value (unrealized loss) below the amount recorded for an investment as well as the severity and duration of the decline. If the decline in fair value is below amortized cost, CFS recognizes OTTI if (1) CFS has the intent to sell the security, (2) it is more-likely-than-not that CFS will be required to sell the security before recovery of its amortized cost basis, or (3) CFS does not expect to recover the entire amortized cost of the security. CFS uses various economic data points and models to aid in its determination of OTTI. Various inputs into the economic models are used to determine if OTTI exists. The most significant inputs in determining OTTI are:

- Length of time and extent to which fair value has been less than amortized cost;
- Cause of the decline, such as interest rates or adverse conditions in the market;
- Payment structure of the security;

- Credit performance of the underlying collateral, including delinquency rates, nonperforming collateral/defaults, severities of losses, collateral values and expected credit losses;
- Current rating of security; and
- Independent analysts' reports and forecasts.

Other inputs may include the actual collateral attributes and other performance indicators of the underlying asset.

If CFS determines that a given security is subject to an OTTI write-down or loss, CFS records the expected credit portion of the loss as a charge to earnings. The measurement of the credit loss component is equal to the difference between the security's cost basis and the present value of its expected future cash flows, using the economic models, discounted at the security's purchase yield assumption. The remaining non-credit portion is recorded in other comprehensive income.

As of December 31, 2022 there were no investment securities where an OTTI had occurred.

Note 3. SBA-PPP Loans Receivable

Pursuant to the CARES Act, the SBA-PPP provides forgivable loans to small businesses to enable them to maintain payroll, hire back employees who have been laid off, and cover applicable overhead. SBA-PPP loans have an interest rate of 1.0%, have 2 and 5 year terms, and carry a 100% guarantee of the SBA.

The allowance for loan losses for SBA-PPP loans was separately evaluated given the explicit government guarantee. This analysis, which incorporated historical experience with similar SBA guarantees and underwriting, concluded the likelihood of loss was remote and therefore no allowance for loan losses was assigned to these loans.

SBA-PPP loans receivable totaled $6 thousand and $2.7 million as of December 31, 2022 and 2021, respectively. All were rated as pass credits, not past due, nonaccrual, TDR, or otherwise impaired. Unearned net fees associated with the SBA-PPP loans amount to $0 and $97 thousand at December 31, 2022 and 2021, respectively. There were no outstanding commitments to extend additional SBA-PPP loans at December 31, 2022.

Note 4. Loans

A summary of the balances of loans by segment follows:

	December 31,	
	2022	2021
Commercial	$ 300,678,213	$ 246,096,810
Commercial - Real Estate	325,542,635	316,736,538
Consumer - Non Real Estate	9,367,673	8,285,369
Residential - Real Estate	105,224,436	92,460,456
Gross loans	$ 740,812,957	$ 663,579,173
Less: Allowance for loan losses	(7,512,577)	(6,793,400)
Loans, net	$ 733,300,380	$ 656,785,773

Overdrafts totaling $122,007 and $299,900 at December 31, 2022 and 2021, respectively, were reclassified from deposits to Consumer – Non Real Estate loans.

The following tables represent a summary of changes in the allowance for loan losses by segment:

	Commercial	Commercial - Real Estate	Consumer - Non Real Estate	Residential - Real Estate	Unallocated	Total
Year Ended December 31, 2022						
Balance beginning of year	$ 2,704,129	$ 3,099,983	$ 80,530	$ 882,903	$ 25,855	$ 6,793,400
Provision for loan losses	220,903	188,657	85,473	128,374	76,589	699,996
Charge-offs	(24,958)	–	(131,459)	–	–	(156,417)
Recoveries	2,049	98,766	65,383	9,400	–	175,598
Total allowance for loan losses	$ 2,902,123	$ 3,387,406	$ 99,927	$ 1,020,677	$ 102,444	$ 7,512,577
Individually evaluated for impairment	$ 4,057	$ 218,546	$ 9,271	$ –	$ –	$ 231,874
Collectively evaluated for impairment	2,898,066	3,168,860	90,656	1,020,677	102,444	7,280,703
Total allowance for loan losses	$ 2,902,123	$ 3,387,406	$ 99,927	$ 1,020,677	$ 102,444	$ 7,512,577
Individually evaluated for impairment	$ 1,908,515	$ 2,247,548	$ 21,671	$ –	$ –	$ 4,177,734
Collectively evaluated for impairment	298,769,698	323,295,087	9,346,002	105,224,436	–	736,635,223
Total loans	$ 300,678,213	$ 325,542,635	$ 9,367,673	$ 105,224,436	$ –	$ 740,812,957

	Commercial	Commercial - Real Estate	Consumer - Non Real Estate	Residential - Real Estate	Unallocated	Total
Year Ended December 31, 2021						
Balance beginning of year	$ 3,077,712	$ 2,813,553	$ 211,581	$ 974,347	$ 202,571	$ 7,279,764
Provision for (reversal of) loan losses	(466,549)	425,356	(82,251)	(99,844)	(176,716)	(400,004)
Charge-offs	(14,167)	(138,926)	(110,407)	–	–	(263,500)
Recoveries	107,133	–	61,607	8,400	–	177,140
Total allowance for loan losses	$ 2,704,129	$ 3,099,983	$ 80,530	$ 882,903	$ 25,855	$ 6,793,400
Individually evaluated for impairment	$ 217,418	$ 171,294	$ –	$ –	$ –	$ 388,712
Collectively evaluated for impairment	2,486,711	2,928,689	80,530	882,903	25,855	6,404,688
Total allowance for loan losses	$ 2,704,129	$ 3,099,983	$ 80,530	$ 882,903	$ 25,855	$ 6,793,400
Individually evaluated for impairment	$ 1,615,758	$ 1,823,775	$ –	$ –	$ –	$ 3,439,533
Collectively evaluated for impairment	244,481,052	314,912,763	8,285,369	92,460,456	–	660,139,640
Total loans	$ 246,096,810	$ 316,736,538	$ 8,285,369	$ 92,460,456	$ –	$ 663,579,173

The following table presents additional impaired loan information at yearend. Unpaid principal balance represents the contractual principal balance of the loan.

	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
December 31, 2022					
With no related allowance:					
Commercial					
Secured	$ 1,254,565	$ 1,254,565	$ –	$ 817,277	$ 65,215
Commercial - Real Estate					
Non-owner occupied	517,097	517,097	–	258,548	19,761
Owner occupied	571,906	571,906	–	578,835	16,191
With an allowance recorded:					
Commercial					
Secured	$ 653,950	$ 653,950	$ 4,057	$ 905,117	$ 28,525
Commercial - Real Estate					
Owner occupied	1,158,545	1,158,545	218,546	1,172,330	51,241
Consumer Non-Real Estate					
Consumer Installment	21,671	21,671	9,271	11,012	979
Total:					
Commercial	$ 1,908,515	$ 1,908,515	$ 4,057	$ 1,722,394	$ 93,740
Commercial - Real Estate	2,247,548	2,247,548	218,546	2,009,713	87,193
Consumer Installment	21,671	21,671	9,271	11,012	979
	$ 4,177,734	$ 4,177,734	$ 231,874	$ 3,743,119	$ 181,912

	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
December 31, 2021					
With no related allowance:					
Commercial					
Secured	$ 582,311	$ 582,311	$ –	$ 842,124	$ 45,780
Commercial - Real Estate					
Non-owner occupied	599,481	599,481	–	626,980	46,932
With an allowance recorded:					
Commercial					
Secured	$ 1,033,447	$ 1,033,447	$ 217,418	$ 1,365,167	$ 58,158
Consumer - Real Estate					
Owner occupied	1,224,294	1,224,294	171,294	1,251,761	66,925
Total:					
Commercial	$ 1,615,758	$ 1,615,758	$ 217,418	$ 2,207,291	$ 103,938
Commercial - Real Estate	1,823,775	1,823,775	171,294	1,878,741	113,857
	$ 3,439,533	$ 3,439,533	$ 388,712	$ 4,086,032	$ 217,795

Included in impaired loans are troubled debt restructurings. At December 31, 2022 and 2021, $3,222,174 and $3,439,533 in loans were classified as troubled debt restructurings where concessions have been granted to borrowers experiencing financial difficulties. These concessions could include a reduction in the loan interest rate, payment extensions, or other actions intended to maximize collection.

Information regarding loans modified as troubled debt restructurings by class during 2022 are as follows:

	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Consumer Non-Real Estate			
Consumer Installment	1	$ 21,671	$ 21,671

The restructured loans have been classified as a troubled debt restructuring due to being modified to interest only payments for 12 months.

Information regarding loans modified as troubled debt restructuring by class during 2021 are as follows

	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Commercial - Secured	3	$ 947,077	$ 947,077

The 2021 restructured loans have been classified as a troubled debt restructuring due to being modified to interest only payments for greater than 12 months along with debt service coverage.

There were no troubled debt restructurings that subsequently defaulted (more than 90 days past due or charged-off) within the first year of modification during 2022 and 2021.

At December 31, 2022, no additional funds were committed to be advanced in connection with impaired loans.

The Bank's internal risk rating definitions are:

Pass/Watch: These include satisfactory loans which may have elements of risk that the Bank has chosen to monitor formally. The objective of monitoring is to assure that no weaknesses develop in these loans.

Special Mention: These loans have a potential weakness that requires management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the asset or in the Bank's credit position at some future date. These credits do not expose the Bank to sufficient risk to warrant further adverse classification.

Substandard: A substandard asset is inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any. Loans classified as such must have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the Bank will sustain some loss if the deficiencies are not corrected.

Doubtful: Loans classified doubtful have all the weaknesses inherent in a substandard asset with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable.

Loss: Loans classified loss are considered uncollectible and of such little value that their continuance as a bankable asset is not warranted. This classification does not mean that the asset has absolutely no recovery or salvage value, but rather it is not practical or desirable to defer writing off this basically worthless asset even though partial recovery may be received in the future.

The Bank's credit quality information, which is based on internal risk grades is as follows:

	Pass	Watch	Special Mention	Substandard	Doubtful	Total
December 31, 2022						
Commercial						
Secured	$ 275,268,471	$ 965,152	$ 7,300	$ 438,462	$ –	$ 276,679,385
Unsecured	23,772,719	226,109	–	–	–	23,998,828
Commercial - Real Estate						
Acquisition and development	12,182,914	–	–	–	–	12,182,914
Non-owner occupied	185,956,862	4,206,385	–	517,097	–	190,680,344
Owner occupied	94,957,450	1,925,176	–	1,799,624	–	98,682,250
Multifamily	23,997,127	–	–	–	–	23,997,127
Consumer - Non Real Estate						
Installment	8,399,071	–	–	22,099	–	8,421,170
Revolving	824,496	–	–	–	–	824,496
Other	122,007	–	–	–	–	122,007
Residential - Real Estate						
First lien 1-4 family	43,459,578	372,799	281,131	58,300	–	44,171,808
Junior lien 1-4 family	11,150,521	–	–	–	–	11,150,521
Construction	12,421,084	–	–	–	–	12,421,084
Land	14,196,486	108,730	–	–	–	14,305,216
Revolving	22,925,507	150,010	100,290	–	–	23,175,807
Total	$ 729,634,293	$ 7,954,361	$ 388,721	$ 2,835,582	$ –	$ 740,812,957

	Pass	Watch	Special Mention	Substandard	Doubtful	Total
December 31, 2021						
Commercial						
Secured	$ 229,725,280	$ 1,493,341	$ –	$ 957,862	$ –	$ 232,176,483
Unsecured	13,903,754	–	–	16,573	–	13,920,327
Commercial - Real Estate						
Acquisition and development	13,947,022	–	–	–	–	13,947,022
Non-owner occupied	183,765,233	713,259	1,320,448	–	–	185,798,940
Owner occupied	92,389,847	1,623,586	–	1,823,775	–	95,837,208
Multifamily	21,153,368	–	–	–	–	21,153,368
Consumer - Non Real Estate						
Installment	6,136,403	–	–	4,297	–	6,140,700
Revolving	1,844,769	–	–	–	–	1,844,769
Other	299,900	–	–	–	–	299,900
Residential - Real Estate						
First lien 1-4 family	32,100,953	481,924	468,747	7,495	–	33,059,119
Junior lien 1-4 family	10,493,888	–	–	–	–	10,493,888
Construction	15,286,976	–	–	–	–	15,286,976
Land	12,033,249	23,859	–	–	–	12,057,108
Revolving	21,379,485	149,139	34,741	–	–	21,563,365
Total	$ 654,460,127	$ 4,485,108	$ 1,823,936	$ 2,810,002	$ –	$ 663,579,173

The following is a summary of information pertaining to nonaccrual and past due loans by class:

	30-59 Days Past Due	60-89 Days Past Due	90 Days or More Past Due	Total Past Due	Nonaccruals	Current	Total Loans
December 31, 2022							
Commercial							
Secured	$ –	$ –	$ –	$ –	$ 438,462	$ 276,240,923	$ 276,679,385
Unsecured	226,109	–	–	226,109	–	23,772,719	23,998,828
Commercial Real Estate							
Acquisition and development	–	–	–	–	–	12,182,914	12,182,914
Non-owner occupied	–	–	–	–	517,097	190,163,247	190,680,344
Owner occupied	–	–	–	–	1,799,624	96,882,626	98,682,250
Multifamily	–	–	–	–	–	23,997,127	23,997,127
Consumer - Non Real Estate							
Installment	6,951	–	–	6,951	22,481	8,391,738	8,421,170
Revolving	–	–	–	–	–	824,496	824,496
Other	18,547	–	–	18,547	–	103,460	122,007
Residential - Real Estate							
First lien 1-4 family	75,577	–	–	75,577	234,856	43,861,375	44,171,808
Junior lien 1-4 family	–	–	–	–	40,554	11,109,967	11,150,521
Construction	–	–	–	–	–	12,421,084	12,421,084
Land	–	–	–	–	–	14,305,216	14,305,216
Revolving	39,513	–	–	39,513	24,827	23,111,467	23,175,807
Total	$ 366,697	$ –	$ –	$ 366,697	$ 3,077,901	$ 737,368,359	$ 740,812,957

	30-59 Days Past Due	60-89 Days Past Due	90 Days or More Past Due	Total Past Due	Nonaccruals	Current	Total Loans
December 31, 2021							
Commercial							
Secured	$ –	$ –	$ –	$ –	$ 10,785	$ 232,165,698	$ 232,176,483
Unsecured	55,622	–	–	55,622	–	13,864,705	13,920,327
Commercial Real Estate							
Acquisition and development	–	–	–	–	–	13,947,022	13,947,022
Non-owner occupied	185,109	–	–	185,109	–	185,613,831	185,798,940
Owner occupied	204,002	241,036	–	445,038	1,823,775	93,568,395	95,837,208
Multifamily	–	–	–	–	–	21,153,368	21,153,368
Consumer - Non Real Estate							
Installment	18,234	–	–	18,234	741	6,121,725	6,140,700
Revolving	14,329	–	–	14,329	–	1,830,440	1,844,769
Other	12,212	–	–	12,212	–	287,688	299,900
Residential - Real Estate							
First lien 1-4 family	21,577	86,627	–	108,204	137,354	32,813,561	33,059,119
Junior lien 1-4 family	–	–	–	–	46,256	10,447,632	10,493,888
Construction	–	–	–	–	–	15,286,976	15,286,976
Land	18,371	–	–	18,371	–	12,038,737	12,057,108
Revolving	286,111	–	–	286,111	–	21,277,254	21,563,365
Total	$ 815,567	$ 327,663	$ –	$ 1,143,230	$ 2,018,911	$ 660,417,032	$ 663,579,173

There were no loans 90+ days past due and still accruing at December 31, 2022 and 2021, respectively.

Note 5. Premises and Equipment

A summary of the cost and accumulated depreciation of premises and equipment follows:

	December 31,	
	2022	2021
Land	$ 4,917,999	$ 5,115,379
Buildings	27,863,990	25,434,153
Furniture, fixtures and improvements	3,164,035	2,861,724
Equipment	6,025,144	5,773,385
Leasehold improvements	4,353,380	4,251,165
	$ 46,324,548	$ 43,435,806
Less accumulated depreciation	(23,123,129)	(21,403,944)
Total	$ 23,201,419	$ 22,031,862

For the years ended December 31, 2022 and 2021, depreciation expense was $1,719,184 and $1,407,466, respectively.

Included in the consolidated balance sheet presentation of these financial statements, premises and equipment also includes the right-of-use asset for leases totaling $662,482 and $747,853 as of December 31, 2022 and 2021. Refer to Note 13 for additional disclosure on the right-of-use asset.

Note 6. Time Deposits

Remaining maturities on certificates of deposit are as follows:

2023	$ 83,016,841
2024	23,924,349
2025	10,241,708
2026	1,105,795
2027	1,373,275
Thereafter	–
Total	$ 119,661,968

Note 7. Trust Preferred Capital Notes

On July 2, 2007, CFS Capital Trust II was formed by the Company for the purpose of issuing redeemable capital securities. Trust II is not a consolidated subsidiary of the Company. On July 5, 2007, $15.5 million of trust preferred securities which have a LIBOR-indexed floating rate of interest were issued. The weighted-average interest rate for the year ended December 31, 2022 was 3.18%. The interest rate as of December 31, 2022 was 5.12%. The securities have a mandatory redemption date of October 1, 2037, and became subject to varying call provisions beginning on September 6, 2012.

In August 2014, CFS was notified that $5.0 million of the $15.0 million in trust preferred securities of Trust II would be auctioned off as part of a larger pooled collateralized debt obligation liquidation. CFS placed a bid of $3.9 million for the securities which was accepted by the trustee and the transaction closed on September 5, 2014. In January 2015, CFS was notified that $5.0 million of the $10.0 million remaining in trust preferred securities of Trust II would be auctioned off as part of a larger pooled collateralized debt obligation liquidation. CFS placed bids totaling $3.9 million for the securities which were accepted by the trustee and the transactions closed on February 5, 2015 and February 13, 2015.

As of December 31, 2022, $5.0 million in preferred stock and $155,000 in common stock of Trust II were still outstanding.

The trust preferred securities may be included in Tier 1 capital for regulatory capital adequacy determination purposes up to 25% of Tier 1 capital after its inclusion. The portion of the trust preferred not considered as Tier 1 capital may be included in Tier 2 capital.

The obligations of CFS with respect to the issuance of the capital securities constitute a full and unconditional guarantee by CFS of the Trust's obligations with respect to the capital securities.

Subject to certain exceptions and limitations, CFS may elect from time to time to defer interest payments on the junior subordinated debt securities, which would result in a deferral of distribution payments on the related capital securities.

Note 8. Borrowings

The Bank has lines of credit with the FHLB that can equal up to 25% of total assets of the Bank. As of December 31, 2022, loans with a carrying value of $27,229,517 and securities with an amortized cost of $155,092,187 were pledged to the FHLB as collateral for borrowings. The FHLB lines of credit totaled $116.3 million with an outstanding balance of $20 million as of December 31, 2022. At December 31, 2021 the FHLB line of credit totaled $147.7 million with an outstanding balance of $87 million. Additional loans are available that can be pledged as collateral for future borrowings from the FHLB above the current lendable collateral value.

The Bank also maintains an additional secured line of credit with another correspondent bank totaling $20 million, which had an outstanding balance of $11 million as of December 31, 2022. In addition to the available credit from the FHLB, the Bank also has unsecured lines of credit with correspondent banks totaling $98.5 million available for overnight borrowings, which had an outstanding balance of $15 million as of December 31, 2022. The Company has a line of credit secured by 400,000 shares of Chesapeake Bank common stock with a correspondent bank totaling $10.0 million available for borrowing as of December 31, 2022. There was no outstanding balance as of December 31, 2022 and 2021.

On June 15, 2021, the Company entered into a Subordinated Note Purchase Agreement with 32 institutional accredited investors under which the Company issued an aggregate of $20 million of subordinated notes (the "2021 Notes") to institutional accredited investors. The 2021 Notes have a maturity date of June 15, 2031. The 2021 Notes bear interest, payable on the 15th of June and December of each year, commencing December 15, 2021, at a fixed rate of 3.25% per year for the first 5 years, and thereafter will bear a floating interest rate of 3-Month Term SOFR plus 260 basis points. The 2021 Notes are not convertible into common stock or preferred stock and are not callable by the holders. The Company has the right to redeem the 2021 Notes, in whole or in part, without premium or penalty, at any interest payment date on or after December 15, 2026 and prior to the maturity date, but in all cases in a principal amount with integral multiples of $1,000, plus interest accrued and unpaid through the date of redemption. If an event of default occurs, such as the bankruptcy of the Company, the holder of a 2021 Note may declare the principal amount of the note to be due and immediately payable. The 2021 Notes are unsecured, subordinated obligations of the Company, and rank junior in right of payment to the Company's existing and future senior indebtedness. The 2021 Notes qualify as Tier 2 capital for regulatory reporting; though, Tier 2 capital treatment is reduced by 20% in each year subsequent to the first date of the redemption right.

Note 9. Income Taxes

The income tax provision differs from the amount of income tax determined by applying the U.S. federal income tax rate to pretax income for the years ended December 31, 2022 and 2021, due to the following:

	2022	2021
Income tax at federal statutory rate	$ 4,294,960	$ 3,635,688
Increase (decrease) in income taxes resulting from:		
State and local taxes	5,146	15,694
Tax exempt income	(1,128,793)	(1,101,505)
Other	(347,709)	(246,590)
Total	$ 2,823,604	$ 2,303,287

The provision for income taxes charged to operations for the years ended December 31, 2022 and 2021, consists of the following:

	2022	2021
Current tax expense		
Federal	$ 3,204,768	$ 2,192,761
State	6,514	23,779
Deferred tax (benefit) expense	(387,678)	86,747
Total	$ 2,823,604	$ 2,303,287

The components of the net deferred tax asset, included in other assets, are as follows:

	December 31,	
	2022	2021
Deferred tax assets:		
Allowance for loan and cash management account losses	$ 1,976,350	$ 1,726,117
Foreclosed assets	63,380	157,765
Deferred compensation	403,935	304,025
Premises and equipment	(237,229)	(97,008)
Restricted stock	(113,881)	(118,969)
Unrealized loss on securities	12,713,336	–
Other	404,877	137,824
Total deferred tax assets	$ 15,210,768	$ 2,109,754
Deferred tax liabilities:		
Securities available for sale	–	$ 2,510,563
Net deferred tax assets (liabilities)	$ 15,210,768	$ (400,809)

CFS, on a consolidated basis, files income tax returns in the U.S. federal jurisdiction, the Commonwealth of Virginia and other states where income is generated. With few exceptions, CFS is no longer subject to U.S. federal or state income tax examinations by tax authorities for years before 2019.

The Company has analyzed the tax positions taken or expected to be taken in its tax returns and concluded it has no liability related to uncertain tax positions.

Note 10. Employee Benefit Plans

Employee Stock Ownership Plan

CFS sponsors an employee stock ownership plan (ESOP) that generally covers full-time employees who have completed one calendar year of service. CFS makes annual contributions to the ESOP at the discretion of the Board of Directors. ESOP compensation expense was $500,000 and $450,000 for the years ended December 31, 2022 and 2021.

401(k) Plan

CFS has adopted a contributory 401(k) plan that covers substantially all employees. Under the plan, employees may elect to defer up to 100% of their salary, subject to Internal Revenue Service limits. CFS will make a matching contribution of 100% of the first 3% and 50% of the second 3% of the employee's salary deferred. CFS may also make a discretionary contribution to the plan. Total expense related to the plan was $758,473 and $683,113 for 2022 and 2021, respectively.

Post-retirement benefits

The Company has entered into deferred compensation arrangements with certain key personnel, which call for the payment of benefits upon the retirement or death of the individuals. The agreements provide that a retirement benefit is payable upon a defined normal retirement age while in service to the Company and a lesser benefit is payable upon early retirement. Other benefits are payable upon disability, death or change in control.

These agreements are unfunded arrangements maintained primarily to provide supplemental retirement benefits and comply with Section 409A of the Internal Revenue Code.

The Company has elected to finance the retirement benefits by purchasing annuities that have been designed to provide a future source of funds for the lifetime retirement benefits of the agreements. The liabilities associated with these deferred compensation arrangements were $1,627,929 and $1,208,171 for the years ended December 31, 2022 and 2021, respectively. The annuity had a balance of $3,592,671 and $3,616,990 as of December 31, 2022 and 2021, respectively, and is recorded at amortized cost. Salaries and employee benefits expense included $419,758 and $460,075 of expense related to these arrangements for 2022 and 2021, respectively.

Note 11. Stock Option Plans

On April 1, 2005, CFS's shareholders approved a stock incentive plan under which options or restricted stock may be granted to certain key employees. The plan reserved 269,568 shares of voting common stock for issuance and expired on January 21, 2015. There was no compensation cost charged to income for those plans related to stock options for 2022.

On April 4, 2014, CFS's shareholders approved a stock incentive plan under which options or restricted stock may be granted to certain key employees. The plan reserved 504,000 shares of voting common stock for issuance and expires on January 16, 2024. There was no compensation cost charged to income for those plans related to stock options for 2022.

The incentive stock option plans require that options be granted at an exercise price equal to at least 100% of the fair market value of the common stock on the date of the grant; however, for those individuals who own more than 10% of the stock of CFS, the option price must be at least 110% of the fair market value on the date of grant. Such options are generally not exercisable until 3 years from the date of issuance and require continuous employment during the period prior to exercise. The options will expire in no more than 10 years after the date of grant. The fair value of each option grant is estimated on the date of the grant using the Black-Scholes option-pricing model. Expected volatility is based on the historic volatility of CFS's stock price over the expected life of the options. The expected term is estimated as the average of the contractual life and vesting schedule for the respective options. The risk-free interest rate is the U.S. Treasury zero-coupon issue with a remaining term equal to the expected term of the options granted. The dividend yield is estimated as the ratio of CFS's historical dividends paid per share of common stock to the stock price on the date of grant. There were no options granted during the years ended December 31, 2022 and 2021.

A summary of the option activity under the plans at December 31, 2022 and changes during the year then ended are as follows:

	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value
Outstanding at December 31, 2021	19,152	$ 9.55		
Granted	–	–		
Exercised	(16,992)	9.55		
Expired	(2,160)	9.55		
Forfeited	–	–		
Outstanding at December 31, 2022	–	$ –	–	$ –
Options exercisable, end of year	–	$ –	–	$ –

Aggregate intrinsic value of stock options represents the total pre-tax intrinsic value (the amount by which the current market value of the underlying stock exceeds the exercise price of the option) that would have been received by the option holders had all the option holders exercised their options on December 31, 2022. This amount changes based on changes in the market value of CFS's stock.

The total intrinsic value of options exercised during the year ended December 31, 2022 and 2021 was $348,271 and $234,443, respectively. As of December 31, 2022 and December 31, 2021 there are no unrecognized compensation costs related to nonvested stock options granted under the plans.

Restricted Stock

The Company grants shares of restricted stock to key employees. These awards help align the interests of these employees with the interests of the shareholders of the Company by providing economic value directly related to increases in the value of the Company's common stock. The value of the stock awarded is established as the fair market value of the stock at the time of grant. The Company recognizes expense, equal to the total value of such awards, ratably over the vesting period of the stock grants. Restricted stock vests over 36 months based on the term of the award.

Nonvested restricted stock activity for the year ended December 31, 2022 is summarized in the following table:

	Shares	Weighted Average Grant Date Value
Nonvested at December 31, 2021	32,615	$ 22.96
Granted	15,950	28.75
Vested	(18,882)	22.61
Forfeited	–	–
Nonvested at December 31, 2022	29,683	$ 26.19

At December 31, 2022, there were no unrecognized compensation costs related to nonvested restricted stock granted under the 2005 Plan. At December 31, 2022, there was $543,036 in unrecognized compensation cost related to nonvested restricted stock granted under the 2014 Plan. This cost is expected to be recognized over the next 28 months. Stock based compensation expense for nonvested restricted stock totaled $411,630 and $349,416 during 2022 and 2021, respectively.

Note 12. Shareholders' Equity

During 2022 and 2021, CFS issued 6,843 and 8,703 shares, respectively, of common stock to its directors for partial compensation. Also, during 2022 and 2021, the Company purchased and retired 46,015 and 130,889 shares, respectively of common stock.

Note 13. Leases

The Company's long-term lease agreements are classified as finance leases. These leases offer the option to extend the lease term and the Company has included such extensions in its calculation of the lease liabilities to the extent the options are reasonably assured of being exercised.

The components of lease expense are as follows:

	2022	2021
Finance lease expense		
Amortization of right-of-use asset	$ 85,371	$ 84,672
Interest on lease liabilities	32,064	34,785
Total finance lease expense	$ 117,435	$ 119,457

Cash paid for amounts included in the measurement of lease liabilities are as follows:

	2022	2021
Operating cash flows from finance leases	$ 112,156	$ 109,141

Supplemental balance sheet information related to leases are as follows:

	2022	2021
Finance Leases:		
Premises and equipment	$ 747,853	$ 832,525
Accumulated depreciation	85,371	84,672
Premises and equipment, net	$ 662,482	$ 747,853
Other long-term liabilities	853,272	933,363
Total finance lease liabilities	$ 853,272	$ 933,363
Weighted Average Remaining Lease Term:	8 Years	9 Years
Weighted Average Discount Rate:	3.6%	3.6%

Maturities of lease liabilities are as follows:

For the year ending December 31,	2022
2023	$ 115,489
2024	118,920
2025	122,452
2026	126,090
2027	129,835
Thereafter	370,763
Lease payments	$ 983,549
Amounts representing interest	(130,277)
Present value of net future minimum lease payments	$ 853,272

Rent expense under operating leases totaled $80,093 and $74,356 for the years ended December 31, 2022 and 2021, respectively.

Note 14. Related Party Transactions

Officers, directors and their affiliates had loans of $17,751,998 and $17,755,481 at December 31, 2022 and 2021, respectively, with the Bank.

Changes in related party loans during 2022 were as follows:

Balance, December 31, 2021	$ 17,755,481
Additions	645,646
Payments	(649,129)
Balance, December 31, 2022	$ 17,751,998

These transactions occurred in the ordinary course of business on substantially the same terms as those prevailing at the time for comparable transactions with unrelated persons.

Related parties had deposits of $12,095,550 and $12,210,640 as of December 31, 2022 and 2021, respectively.

Note 15. Other Income and Expenses

The principal components of "Other income" in the consolidated statements of income are:

	2022	2021
ATM fee income	$ 2,396,683	$ 2,182,927
Gain on termination of interest rate cap	3,468,395	–
Gain on investment buyback	2,163,342	–
Other	2,609,351	2,373,198
Total	$ 10,637,771	$ 4,556,125

The principal components of "Other expenses" in the consolidated statements of income are:

	2022	2021
Advertising	$ 1,881,565	$ 1,412,661
Software	3,320,629	3,007,784
Professional fees	2,040,685	1,836,116
Debit card expense	947,279	802,989
Franchise tax	1,072,053	866,471
Contributions	461,016	614,038
Exam and audit	273,741	298,318
Legal fees	163,823	508,080
FDIC assessments	369,568	349,753
Delivery and transportation	319,108	286,960
Stationery and supplies	292,292	233,766
Other	4,562,816	4,014,372
Total	$ 15,704,575	$ 14,231,308

Note 16. Revenue from Contracts with Customers

During the years ended December 31, 2022 and 2021, the Company recognized revenues from contracts with customers totaling $17,804,976 and $16,342,293, respectively. There were no impairment losses recognized on any receivables or contract assets arising from the Company's contracts with customers during the years ended December 31, 2022 and 2021. While the Company does have noninterest income related to changes in cash surrender value of life insurance, sales of investments, and income from government sponsored entities, these are not within the scope of ASC 606.

All of the Company's revenue from contracts with customers in the scope of ASC 606 is recognized within noninterest income. The following table represents the Company's sources of noninterest income for the years ended December 31, 2022 and 2021. Items outside the scope of ASC 606 are noted as such.

	2022	2021
Noninterest income		
Service charges	$ 972,320	$ 770,347
ATM fee income	2,396,683	2,182,927
Trust and wealth management income	4,074,761	4,391,806
Merchant services income, net	4,934,928	4,061,549
Cash management fee income	3,196,595	2,025,501
Mortgage banking income	1,678,833	2,776,845
Other[(a)]	4,937,801	3,103,233
Total	$ 22,191,921	$ 19,312,208

(a) The Other category includes $500,551 and $133,318 of income sources that are within the scope of ASC 606 but determined immaterial as of December 31, 2022 and 2021, respectively; the remaining balance of $4,437,250 and $2,969,915 is outside of the scope of ASC 606 as of December 31, 2022 and 2021, respectively.

A description of the Company's revenue streams accounted for under ASC 606 follows:

Service Charges on Deposit Accounts: The Company earns fees from its deposit customers for transaction-based, account maintenance, and overdraft services. Transaction-based fees are recognized at the time the transaction is executed as that is the point in time the Company fulfills the customer's request. Account maintenance fees are earned over the course of a month, representing the period over which the Company satisfies the performance obligation. Overdraft fees are recognized at the point in time that the overdraft occurs. Service charges on deposits are withdrawn from the customer's account balance.

ATM Fee Income: The Company earns interchange fees from debit cardholder transactions conducted through the VISA payment network. Interchange fees from cardholder transactions represent a percentage of the underlying transaction value and are recognized daily, concurrently with the transaction processing services provided to the cardholder.

Merchant Services: The Company earns interchange fees from customer debit and credit card transactions that are earned at the time a cardholder engages in a transaction with a merchant as well as fees charged to merchants for providing them the ability to accept and process the debit and credit card transactions. Revenue is recognized when the performance obligation has been met as it is satisfied upon the completion of the card transaction. Additionally, revenue recognition guidance requires costs associated with cardholder and merchant services transactions to be netted against the fee income from such transactions when an entity is acting as an agent in providing services to customer.

Wealth Management Services: The Company earns wealth management fees from its contracts with trust and brokerage customers to manage assets for investment, and/or to transact on their accounts. These fees are earned as the Company provides the contracted monthly or quarterly services and are generally assessed based on a tiered scale of the market value of assets under management at month-end. Fees that are transaction based, including trade execution services, are recognized at the point in time that the transaction is executed, i.e. the "trade date". Other related services provided include financial planning services, which are based on a fixed fee schedule, and are recognized when the services are rendered.

Cash Management: The Company earns fee income on accounts receivable financing relationships. The Company recognizes the fee income when the invoices are funded.

Mortgage Banking Income: The Company earns revenues from both selling and servicing of consumer 1-4 family mortgages sold to Freddie Mac. The origination revenues are recognized when the loan is sold and funded by Freddie Mac. Servicing revenues are earned for maintaining the payment processing of the loan and are recognized each month when the loan payment is processed.

Gains/Losses on Sales of OREO: The Company records a gain or loss from the sale of OREO when control of the property transfers to the buyer, which generally occurs at the time of an executed deed. When the Company finances the sale of OREO to the buyer, the Company assesses whether the buyer is committed to perform their obligations under the contract and whether collectability of the transaction price is probable. Once these criteria are met, the OREO asset is derecognized and the gain or loss on sale is recorded upon the transfer of control of the property to the buyer. In determining the gain or loss on the sale, the Company adjusts the transaction price and related gain (loss) on sale if a significant financing component is present.

Based on the Company's analysis, none of the contracts discussed above required a material cost to obtain or fulfill the contract, which resulted in no capitalized assets associated with these contracts as of December 31, 2022 and 2021.

Note 17. Earnings Per Common Share

The following data shows the amounts used in computing earnings per common share and the effect on the weighted average number of shares of dilutive potential common stock. The potential common stock did not have an impact on net income. Shares related to unvested restricted stock grants are included in the weighted average number of common shares outstanding because the holders participate in non-refundable dividends and have voting rights during the vesting period.

	2022	2021
Weighted average number of common shares, basic	4,717,918	4,818,926
Effect of dilutive stock options	8,412	14,289
Weighted average number of common shares and dilutive potential common stock used in diluted EPS	4,726,330	4,833,215

There were no antidilutive options for the years ended December 31, 2022 and 2021.

Note 18. Financial Instruments with Off-Balance-Sheet Risk

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

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

At December 31, 2022 and 2021, the following financial instruments were outstanding whose contract amounts represent credit risk:

	Contract Amount	
	2022	2021
	(in thousands)	
Commitments to grant loans	$ 8,836	$ 6,779
Unfunded commitments under lines of credit	196,747	173,525
Commercial and standby letters of credit	5,325	6,312
Cash management unfunded commitments	35,383	29,722

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. The commitments for lines of credit may expire without being drawn upon. Therefore, the total commitment amounts do not necessarily represent future cash requirements. The amount of collateral obtained, if it is deemed necessary by the Bank, is based on management's credit evaluation of the customer.

Unfunded commitments under commercial lines of credit, revolving credit lines and overdraft protection agreements are commitments for possible future extensions of credit to existing customers. These lines of credit usually do not contain a specified maturity date and may not be drawn upon to the total extent to which the Bank is committed. The amount of collateral obtained, if it is deemed necessary by the Bank, is based on management's credit evaluation of the customer.

Commercial and standby letters of credit are conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. Those letters of credit are primarily issued to support public and private borrowing arrangements. Essentially all letters of credit issued have expiration dates within one year. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. The Bank generally holds collateral supporting those commitments, if deemed necessary.

The Company had no reserve for unfunded commitments recorded at December 31, 2022 and 2021.

The Company has invested in several funds primarily consisting of Small Business Investment Companies (SBIC) and housing equity funds. The unfunded commitment remaining on these funds totaled $4,927,400 and $6,136,400 as of December 31, 2022 and 2021, respectively. In 2022, the Company invested in two Fintech investment funds. The unfunded commitment remaining on these funds totaled $3,296,684 as of December 31, 2022.

CFS maintains its cash accounts in several correspondent banks. The total amount by which cash on deposit in those banks exceeded the federally insured limits was $1,695,861 at December 31, 2022.

Note 19. Derivatives

To mitigate exposure to interest costs, in May 2020, the Company purchased an interest rate cap with a rate of 0.75% and a 10-year term. The instrument's hedge was $50 million of FHLB borrowings maturing quarterly with similar reset dates. These borrowings were expected to be rolled quarterly, with its fixed rate set based on 3-month LIBOR. In February 2022, the Company terminated this interest rate cap and recognized a gain of $3.5 million, which is included in other noninterest income on the consolidated statements of income. In connection with the termination of the interest rate cap, the Company repaid the $50 million of FHLB borrowings that were associated with these hedges.

In March 2022, the Company entered into a receive fixed/pay variable interest rate swap agreement. The Company mitigates the interest rate risk entering into these swap agreements by entering into equal and offsetting swap agreements with a highly rated third-party financial institution. These back-to-back swap agreements are freestanding derivatives and are recorded at fair value in the Company's consolidated balance sheets (asset positions are included in other assets and liability positions are included in other liabilities).

The following table presents the notional and fair values of the derivative agreements for December 31, 2022.

	December 31, 2022	
	Notational Amount	**Fair Value**
	(in thousands)	
Interest rate swap agreement		
Receive fixed/pay variable swap	$ 50,000	$ (2,917)

The Company does not use derivatives for trading or speculative purposes.

Note 20. Fair Value of Assets and Liabilities

Determination of Fair Value

CFS uses fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. The fair value of a financial instrument is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value is best determined based upon quoted market prices. However, in many instances, there are not quoted market prices for CFS's various financial instruments. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. Accordingly, the fair value estimates may not be realized in an immediate settlement of the instrument.

Fair value guidance provides a consistent definition of fair value, which focuses on exit price in an orderly transaction (that is, not a forced liquidation or distressed sale) between market participants at the measurement date under current market conditions. If there has been a significant decrease in volume and level of activity for the asset or liability, a change in valuation technique or the use of multiple valuation techniques may be appropriate. In such instances, determining the price at which willing market participants would transact at the measurement date under current market conditions depends on the facts and circumstances and requires the use of significant judgment. The fair value is a reasonable point within the range that is most representative of fair value under current market conditions.

Fair Value Hierarchy

In accordance with this guidance, CFS groups its financial assets and financial liabilities generally measured at fair value in three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value.

Level 1 - Valuation is based on quoted prices in active markets for identical assets and liabilities and generally includes debt and equity securities that are traded in an active exchange market. Valuations are obtained from readily available pricing sources for market transactions involving identical assets or liabilities.

Level 2 - Valuation is based on inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. The valuation may be based on quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the asset or liability.

Level 3 - Valuation is based on unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement.

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

Cash and Cash Equivalents and Interest-Bearing Deposits in Banks

The carrying amounts of cash and short-term instruments approximate fair values based on the short-term nature of the assets.

Securities

Securities available for sale are recorded at fair value on a recurring basis. Fair value measurement is based upon quoted market prices, when available (Level 1). If quoted market prices are not available, fair values are measured utilizing independent valuation techniques of identical or similar securities for which significant assumptions are derived primarily from or corroborated by observable market data (Level 2). If the inputs used to provide the evaluation for certain securities are unobservable and/or there is little, if any, market activity then the security would fall to the lowest level of the hierarchy (Level 3).

The Company's investment portfolio is primarily valued using fair value measurements that are considered to be Level 2. The Company has contracted with a third-party portfolio accounting service vendor for valuation of its securities portfolio. The vendor's primary source for security valuation is Interactive Data Corporation ("IDC"), which evaluates securities based on market data. IDC utilizes evaluated pricing models that vary by asset class and include available trade, bid, and other market information. Generally, the methodology includes broker quotes, proprietary modes, vast descriptive terms and conditions databases, as well as extensive quality control programs.

The vendor utilizes proprietary valuation matrices for valuing all municipal securities. The initial curves for determining the price, movement, and yield relationships within the municipal matrices are derived from industry benchmark curves or sourced from a municipal trading desk. The securities are further broken down according to issuer, credit support, state of issuance and rating to incorporate additional spreads to the industry benchmark curves.

The Company uses an independent valuation information source that draws on quantitative models and market data contributed from over 4,000 market participants, to validate third party valuations. Any material differences between valuation sources are researched by further analyzing the various inputs that are utilized by each pricing source.

The carrying value of other investments, which include FRB and FHLB stock, approximates fair value based upon the redemption provisions of each entity.

Loans Held For Sale

Loans held for sale include mortgage loans and are carried at the lower of cost or market value. The fair values of mortgage loans held for sale are based on current market rates from investors within the secondary market for loans with similar characteristics. Carrying value approximates fair value.

Loans Receivable

Fair values for loans are estimated using discounted cash flow analyses, using market interest rates for comparable loans. Also included in the fair values for loans is a credit component adjustment. Fair values for nonperforming loans are estimated using discounted cash flow analyses or underlying collateral values, where applicable.

Cash Management Accounts

The carrying value of cash management accounts approximates their fair value. The future cash flows from these accounts are short-term in nature (less than 90 days) and the rate of return approximates current market rates.

Commercial Mortgage Loan Repurchase Facilities

The fair value of commercial mortgage loan repurchase facilities was determined using a discount cash flow technique. Interest rates appropriate to the maturity and underlying collateral are used for discounting the estimated cash flows. As observable market interest rates are used, the fair value of commercial mortgage loan repurchase facilities was classified as Level 2.

Deposits

The fair values disclosed for demand deposits (for example, interest and noninterest checking, savings, and certain types of money market accounts) are, by definition, equal to the amount payable on demand at the reporting date (that is, their carrying amounts). The carrying amounts of variable-rate, fixed-term money market accounts and certificates of deposit, if any, approximate their fair values at the reporting date. Fair values for fixed-rate certificates of deposit are estimated using a discounted cash flow calculation that applies market interest rates on comparable instruments to a schedule of aggregated expected monthly maturities on time deposits.

Short-Term Debt

The carrying amounts of short-term debt maturing within 90 days approximate their fair values. Fair values of short-term debt are estimated using discounted cash flow analyses based on current market rates and similar types of borrowing arrangements.

Subordinated Notes and Trust Preferred Capital Notes

Current market rates for debt with similar terms and remaining maturities are used to estimate fair value of existing debt. Fair value of long-term debt is based on quoted market prices or dealer quotes for the identical liability when traded as an asset in an active market. If a quoted market price is not available, an expected present value technique is used to estimate fair value.

The fair value of the Company's subordinated notes is estimated by utilizing recent issuance rates for subordinated debt offerings of similar issuer size.

Accrued Interest

The carrying amounts of accrued interest approximate fair value.

Off-Balance-Sheet Credit-Related Instruments

Fair values for off-balance-sheet, credit-related financial instruments are based on fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the counterparties' credit standings.

Derivative Asset

Derivative instruments held or issued by the Company for risk management purposes are traded in over-the-counter markets. For those derivatives, the Company measures fair value using models that use primarily market observable inputs, such as yield curves and option volatilities, and include the value associated with counterparty credit risk. The Company classifies derivative instruments held or issued for risk management purposes as Level 2. As of December 31, 2022, the Company's derivative instrument consists solely of an interest rate swap.

Assets Measured at Fair Value on a Recurring Basis

The following table presents the balances of financial assets measured at fair value on a recurring basis as of December 31, 2022 and 2021:

		Fair Value Measurements Using		
Description	Carrying Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
		(in thousands)		
December 31, 2022				
Securitites available-for-sale:				
US Treasury	$ 432	$ –	$ 432	$ –
Securities of state and political subdivisions	237,605	–	237,605	–
SBA loan pooled securities	2,302	–	2,302	–
Mortgage-backed securities				
Agency	50,256	–	50,256	–
Non-agency	111,568	–	111,568	–
Other debt securities	44,286	–	44,286	–
Total assets at fair value	$ 446,449	$ –	$ 446,449	$ –
December 31, 2021				
Securitites available-for-sale:				
US Treasury	$ 11,937	$ –	$ 11,937	$ –
Securities of state and political subdivisions	373,296	–	373,296	–
SBA loan pooled securities	2,872	–	2,872	–
Mortgage-backed securities				
Agency	62,948	–	62,948	–
Non-agency	99,492	–	99,492	–
Other debt securities	50,099	–	50,099	–
	600,644	–	600,644	–
Interest rate cap	3,868	–	3,868	–
Total assets at fair value	$ 604,512	$ –	$ 604,512	$ –

As of December 31, 2022, there were no assets classified as Level 3 to be measured at fair value on a recurring basis. The following tables present the changes in Level 3 assets that are measured at fair value for the year ended December 31, 2021:

	Fair Value Measurements Using Significant Unobservable Inputs (Level 3)					
		Total Realized/Unrealized Gains (Losses) Included in				
	Balance as of December 31, 2020	Net Income	Other Comprehensive Loss	Purchases, Sales, Issuances, and Settlements, Net	Transfers in and/or out of Level 3	Balance as of December 31, 2021
	(in thousands)					
Mortgage-backed securities non-agency	$ 3,208	$ —	$ —	$ (3,208)	$ —	$ —

Assets Measured at Fair Value on a Nonrecurring Basis

Under certain circumstances, CFS makes adjustments to the fair value of certain assets and liabilities although they are not measured at fair value on a recurring basis. The following table presents assets carried on the consolidated balance sheet by caption and by level in the fair value hierarchy at December 31, 2022 and 2021, for which a nonrecurring change in fair value has been recorded:

	Fair Value Measurements at December 31, 2022 Using (in thousands)		
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Impaired loans	$ –	$ –	$ 1,602
Foreclosed assets	–	–	971

	Fair Value Measurements at December 31, 2021 Using (in thousands)		
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Impaired loans	$ –	$ –	$ 1,869
Foreclosed assets	–	–	1,278

	Fair Value Measurements at December 31, 2022			
	Fair Value (in thousands)	Valuation Techniques	Unobservable Inputs	Weighted Average
Assets:				
Impaired loans	$ 1,602	Market comparables	Discount applied to market comparables [1]	12.6%
Foreclosed assets	971	Market comparables	Discount applied to market comparables [1]	41.3%
Total	$ 2,573			

[1] *A discount percentage is applied based on age of independent appraisals, selling costs, current market conditions, and experience within the local market.*

	Fair Value Measurements at December 31, 2021			
	Fair Value (in thousands)	Valuation Techniques	Unobservable Inputs	Weighted Average
Assets:				
Impaired loans	$ 1,869	Market comparables	Discount applied to market comparables (1)	17.2%
Foreclosed assets	1,278	Market comparables	Discount applied to market comparables (1)	35.6%
Total	$ 3,147			

(1) *A discount percentage is applied based on age of independent appraisals, selling costs, current market conditions, and experience within the local market.*

Impaired Loans

Loans are designated as impaired when, in the judgment of management based on current information and events, it is probable that all amounts due according to the contractual terms of the loan agreements will not be collected. The measurement of loss associated with impaired loans can be based on either the observable market price of the loan or the fair value of the collateral. Collateral may be in the form of real estate or business assets including equipment, inventory, and accounts receivable. The vast majority of the Company's collateral is real estate. The value of real estate is determined utilizing an income or market valuation approach based on an appraisal, of one year or less, conducted by an independent, licensed appraiser using observable market data (Level 2). However, if the collateral is a house or building in the process of construction or if an appraisal of the property is more than one year old and not solely based on observable market comparables, or management determines the fair value of the collateral is further impaired below the appraised value, then a Level 3 valuation is considered to measure the fair value. The value of business equipment is based upon an outside appraisal, of one year or less, if deemed significant, or the net book value on the applicable business's financial statements if not considered significant using observable market data. Likewise, values for inventory and accounts receivables collateral are based on financial statement balances or aging reports (Level 3). Impaired loans allocated to the allowance for loan losses are measured at fair value on a nonrecurring basis. Any fair value adjustments are recorded in the period incurred as provision for loan losses on the Consolidated Statements of Income.

Foreclosed Assets

Fair values of foreclosed assets are carried at the lower of carrying value or fair value less selling costs. Fair value is based upon independent market prices, appraised values of the collateral, or management's estimation of the value of the collateral. When the fair value of the collateral is based on an observable market price or a current appraised value, the Company records the foreclosed asset as Level 2 valuation. When an appraised value is not available or management determines the fair value of the collateral is further impaired below the appraised value and there is no observable market price, the Company records the foreclosed asset as Level 3 valuation. Any fair value adjustments are recorded in the period incurred as a foreclosed asset expense on the Consolidated Statements of Income.

The estimated fair values, and related carrying or notional amounts, of CFS's financial instruments are as follows:

	Carrying Value	Quoted Prices in Active Markets for Identical Assets Level 1	Significant Other Observable Inputs Level 2	Significant Unobservable Inputs Level 3	Total Fair Value
		Fair Value Measurements at December 31, 2022			
			(in thousands)		
Financial assets:					
Cash and cash equivalents	$ 26,395	$ 26,395	$ –	$ –	$ 26,395
Securities available for sale	446,449	–	446,449	–	446,449
Other investments	3,322	–	–	3,222	3,222
Loans	740,813	–	728,448	1,602	730,050
Cash management accounts	29,142	–	30,055	–	30,055
Commercial mortgage loan repurchasing facilities	8,128	–	8,020	–	8,020
Accrued interest receivable	5,856	–	5,856	–	5,856
Financial liabilities:					
Deposits	$ 1,166,240	$ –	$ 1,007,767	$ –	$ 1,007,767
Trust preferred capital notes	5,155	–	4,375	–	4,375
Short-term debt	45,979	–	45,692	–	45,692
Subordinated notes	20,000	–	–	19,378	19,378
Accrued interest payable	144	–	144	–	144
Interest rate swap	2,917	–	2,917	–	2,917

	Carrying Value	Quoted Prices in Active Markets for Identical Assets Level 1	Significant Other Observable Inputs Level 2	Significant Unobservable Inputs Level 3	Total Fair Value
		Fair Value Measurements at December 31, 2021			
			(in thousands)		
Financial assets:					
Cash and cash equivalents	$ 20,790	$ 20,790	$ –	$ –	$ 20,790
Securities available for sale	600,644	–	600,644	–	600,644
Other investments	5,548	–	–	5,548	5,548
Loans	666,222	–	650,965	1,869	652,834
Cash management accounts	27,804	–	31,594	–	31,594
Commercial mortgage loan repurchase facilities	5,084	–	5,066	–	5,066
Accrued interest receivable	6,254	–	6,254	–	6,254
Interest rate caps	3,868	–	3,868	–	3,868
Financial liabilities:					
Deposits	$ 1,124,972	$ –	$ 1,127,198	$ –	$ 1,127,198
Trust preferred capital notes	5,155	–	4,201	–	4,201
Short-term debt	99,046	–	99,037	–	99,037
Subordinated notes	20,000	–	–	21,408	21,408
Accrued interest payable	113	–	113	–	113

CFS assumes interest rate risk (the risk that general interest rate levels will change) as a result of its normal operations. As a result, the fair values of CFS's financial instruments will change when interest rate levels change and that change may be either favorable or unfavorable to CFS. Management attempts to match maturities of assets and liabilities to the extent believed necessary to minimize interest rate risk. However, borrowers with fixed rate obligations are less likely to prepay in a rising rate environment and more likely to prepay in a falling rate environment. Conversely, depositors who are receiving fixed rates are more likely to withdraw funds before maturity in a rising rate environment and less likely to do so in a falling rate environment. Management monitors rates and maturities of assets and liabilities and attempts to minimize interest rate risk by adjusting terms of new loans and deposits and by investing in securities with terms that mitigate CFS's overall interest rate risk.

Note 21. Minimum Regulatory Capital Requirements

CFS and the Bank are subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory, possibly additional discretionary, actions by regulators that, if undertaken, could have a direct material effect on CFS's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, financial institutions must meet specific capital guidelines that involve quantitative measures of assets, liabilities, and certain off-balance-sheet items as calculated under regulatory accounting practices. A financial institution's capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors. Prompt corrective action provisions are not applicable to bank holding companies.

The final rules implementing Basel Committee on Banking Supervision's capital guidelines for U.S. banks (Basel III rules) became effective for the Company on January 1, 2015 with full compliance of all requirements being phased in over a multi-year schedule, and fully phased in by January 1, 2019. The net unrealized gain or loss on available for sale securities is not included in computing regulatory capital. Management believes, as of December 31, 2022, the Company and Bank meet all capital adequacy requirements to which they are subject.

	Actual		For Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2022:						
Total Capital (to Risk-Weighted Assets):						
Company	$ 163,610	15.9%	$ 82,361	8.0%	N/A	
Bank	$ 155,764	14.9%	$ 83,674	8.0%	$104,593	10.0%
Tier 1 Capital (to Risk-Weighted Assets):						
Company	$ 134,199	13.0%	$ 61,770	6.0%	N/A	
Bank	$ 146,353	14.0%	$ 62,756	6.0%	$ 83,674	8.0%
Tier 1 Capital (to Average Assets):						
Company	$ 134,199	9.6%	$ 55,878	4.0%	N/A	
Bank	$ 146,353	10.5%	$ 55,537	4.0%	$ 69,421	5.0%
Common Equity Tier 1 Capital (to Risk-Weighted Assets)						
Company	$ 129,199	12.5%	$ 46,328	4.5%	N/A	
Bank	$ 146,353	14.0%	$ 47,067	4.5%	$ 67,985	6.5%
As of December 31, 2021:						
Total Capital (to Risk-Weighted Assets):						
Company	$ 148,327	15.2%	$ 78,256	8.0%	N/A	
Bank	$ 142,525	14.6%	$ 78,041	8.0%	$ 97,552	10.0%
Tier 1 Capital (to Risk-Weighted Assets):						
Company	$ 120,107	12.3%	$ 58,692	6.0%	N/A	
Bank	$ 134,305	13.8%	$ 58,530	6.0%	$ 78,041	8.0%
Tier 1 Capital (to Average Assets):						
Company	$ 120,107	8.9%	$ 53,924	4.0%	N/A	
Bank	$ 134,305	10.0%	$ 53,616	4.0%	$ 67,019	5.0%
Common Equity Tier 1 Capital (to Risk-Weighted Assets)						
Company	$ 115,107	11.8%	$ 44,019	4.5%	N/A	
Bank	$ 134,305	13.8%	$ 43,898	4.5%	$ 63,408	6.5%

Note 22. Accumulated Other Comprehensive Income

Changes in each component of accumulated other comprehensive income for the years ended December 31, 2022 and 2021 were as follows:

	Unrealized Gains on Available-for-Sale Securities	Unpaid Unrealized Gains on Cash Flow Hedges	Total
Balance at December 31, 2021	$ 9,444,494	$ 1,586,054	$ 11,030,548
Other comprehensive income before reclassification	(60,574,142)	(3,890,657)	(64,464,799)
Amounts reclassified from accumulated other comprehensive income	3,303,287	–	3,303,287
Net current-period other comprehensive income	(57,270,855)	(3,890,657)	(61,161,512)
Balance at December 31, 2022	$ (47,826,361)	$ (2,304,603)	$ (50,130,964)
Balance at December 31, 2020	$ 16,433,375	$ 222,160	$ 16,655,535
Other comprehensive income before reclassification	(6,258,846)	1,363,894	(4,894,952)
Amounts reclassified from accumulated other comprehensive income	(730,035)	–	(730,035)
Net current-period other comprehensive income	(6,988,881)	1,363,894	(5,624,987)
Balance at December 31, 2021	$ 9,444,494	$ 1,586,054	$ 11,030,548

Details regarding reclassifications out of accumulated other comprehensive income for the years ended December 31, 2022 and 2021 were as follows:

Reclassifications Out of Accumulated Other Comprehensive Income for the Year Ended December 31, 2022:

Details about AOCI Components	Amount Reclassified from AOCI	Affected Line Item in the Consolidated Income Statement
Realized loss on sale of securities	$ (3,303,287)	Net loss on sales of securities available for sale
Income tax benefit	693,690	Income tax benefit
Total reclassifications	$ (2,609,597)	Net of tax

Reclassifications Out of Accumulated Other Comprehensive Income for the Year Ended December 31, 2021:

Details about AOCI Components	Amount Reclassified from AOCI	Affected Line Item in the Consolidated Income Statement
Realized gain on sale of securities	$ 730,035	Net gain on sales of securities available for sale
Income tax expense	(153,307)	Income tax expense
Total reclassifications	$ 576,728	Net of tax

Note 23. Condensed Parent Company Financial Statements

The following parent company accounting policies should be read in conjunction with the related condensed balance sheets, statements of income, and statements of cash flows.

Investments in subsidiaries are accounted for using the equity method of accounting. The parent company and its subsidiaries file a consolidated federal income tax return. The subsidiaries' individual tax provisions and liabilities are stated as if they filed separate returns and any benefits or detriments of filing the consolidated tax return are absorbed by the parent company.

The parent company's principal assets are its investments in its wholly-owned subsidiaries. Dividends from the Bank are the primary source of funds for the parent company. The payment of dividends by the Bank is restricted by various statutory limitations. Banking regulations also prohibit extensions of credit by the Bank to the parent company unless appropriately secured by assets. As of December 31, 2022, the amount available for payment of additional dividends without prior regulatory approval from the Bank to the parent company is $31,676,545 or 40.06% of consolidated net assets.

Balance Sheets (Condensed)

	December 31, 2022	December 31, 2021
Assets		
Cash	$ 516,121	$ 947,704
Investment in subsidiaries	101,337,915	148,242,862
Premises and equipment, net	1,269,486	1,349,837
Other assets	1,730,471	1,161,597
Total assets	$ 104,853,993	$ 151,702,000
Liabilities and Shareholders' Equity		
Trust preferred capital notes	$ 5,155,000	$ 5,155,000
Subordinated notes	20,000,000	20,000,000
Other liabilities	512,412	410,113
Shareholders' equity	79,186,581	126,136,887
Total liabilities and shareholders' equity	$ 104,853,993	$ 151,702,000

Statements of Income (Condensed)

	2022	2021
Income: Dividends from subsidiaries	$ 5,103,615	$ 2,402,486
Other	406,342	759,087
Total income	$ 5,509,957	$ 3,161,573
Expenses: Interest expense	$ 817,389	$ 406,186
Other expenses	1,637,390	1,654,079
Total expenses	$ 2,454,779	$ 2,060,265
Income before income taxes and equity in undistributed earnings of subsidiaries	$ 3,055,178	$ 1,101,308
Allocated income tax benefit	434,859	293,376
Income before equity in undistributed earnings of subsidiaries	$ 3,490,037	$ 1,394,684
Equity in undistributed earnings of subsidiaries	14,138,550	13,614,830
Net income	$ 17,628,587	$ 15,009,514

Statements of Cash Flows (Condensed)

	2022	2021
Cash Flows from Operating Activities		
Net income	$ 17,628,587	$ 15,009,514
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	80,351	82,041
Equity in distributed earnings of subsidiaries	(14,138,550)	(13,614,830)
Stock-based compensation	411,630	349,416
Issuance of common stock for services	201,869	195,034
Changes in other assets and liabilities:		
Increase in other assets	(567,457)	(202,779)
Increase (decrease) in other liabilities	102,299	(22,385)
Net cash provided by operating activities	$ 3,718,729	$ 1,796,011
Cash Flows from Investing Activities		
Capital contribution to the Bank	$ –	$ (15,000,000)
Net cash used in investing activities	$ –	$ (15,000,000)
Cash Flows from Financing Activities		
Issuance of subordinated notes	$ –	$ 20,000,000
Dividends paid	(2,735,803)	(2,549,836)
Repurchase of common stock	(1,576,759)	(4,064,557)
Exercise of stock options	162,250	155,820
Net cash provided by (used in) financing activities	$ (4,150,312)	$ 13,541,427
Net (decrease) increase in cash	$ (431,583)	$ 337,438
Cash at beginning of year	947,704	610,266
Cash at end of year	$ 516,121	$ 947,704

Financial Overview: Chesapeake Financial Shares, Inc. (CFS or the "Company") recorded net income of $17,628,587 for 2022. The return on average equity in 2022 was 20.89% and return on average assets was 1.32% compared to 11.87% and 1.14%, respectively, in 2021. At December 31, 2022, CFS had total assets of $1.329 billion, which was a decrease of 4.10% when compared to December 31, 2021. The Company ended 2022 with total gross loans of $740.8 million, and total deposits of $1.17 billion, an increase of 11.6% and 3.7%, respectively.

The current economic environment continued to cause competitive pricing pressures on loans. Despite the pressures mentioned, loan volume was up $77 million for 2022, which brought the average annual loan growth rate for the last five years to 8.8%. Total past due and nonaccrual loans increased by $1.1 million from December 31, 2021 to December 31, 2022. The loan loss reserve to non-PPP gross loans less unearned discounts remained at 1.0% as of December 31, 2022 and December 31, 2021. The deposit increase of 3.7% for 2022 brought the average annual deposit growth rate for the last five years to 11.7%.

With the passage of the Paycheck Protection Program ("PPP"), administered by the Small Business Administration ("SBA"), the Company was able to originate 968 loans totaling $76.9 million in 2020 and 473 loans totaling $36 million in 2021. In total, the Company received $4.9 million in fees from the SBA for originating the loans of which $777,003 were recognized into income in 2020, $4,043,657 in 2021 and $97,433 in 2022. Loans funded through this program are guaranteed by the SBA and loans that meet regulatory criteria are subject to forgiveness. As of December 31, 2022, one loan totaling $6 thousand remains that was not forgiven by the SBA. Data in the following discussion excludes this PPP loan unless otherwise stated.

Summary of Results of Operations: Net income for 2022 was $17,628,587, or $3.73 per share (fully diluted) compared to $15,009,514 or $3.11 per share in 2021, an increase of $2,619,073. Net interest income before the provision for loan losses was up 6.1% from 2021. There was a 14.9% or $2,879,713 increase in noninterest income, primarily due to the gain on sale of an investment held at cost totaling $2,163,342 along with the cash management program rebounding from the impact of COVID-19. Cash management income increased from 2021 by $1,171,094, or 57.8%. Merchant services income increased from 2021 by $873,379, or 21.5% while, due to the volatile markets, trust income and wealth management fees decreased $317,045 in 2022 from 2021, or 7.2%. In March 2022, the Company terminated the interest rate cap entered into in June of 2020 which resulted in a gain of $3,468,395. During 2022, the Company recognized net losses on sale of securities totaling $3,303,287. Noninterest expense increased by 2.7% or $1,170,304 in 2022 over 2021.

Assets

Loan Portfolio: The loan portfolio is the largest component of earning assets for the Company and accounts for the greatest portion of total interest income. The gross loan portfolio totaled $740.8 million and $663.6 million as of December 31, 2022 and 2021, respectively, representing an increase of 11.6% year over year. Commercial loans (including real estate and non-real estate combined) were up 11.3% or $63.4 million while residential and consumer loan balances were up 13.8% or $12.8 million and 13.1% or $1.1 million, respectively, at December 31, 2022 compared to December 31, 2021.

On December 31, 2022, the loan portfolio consisted of 84.5% commercial loans, 14.2% single-family residential and residential construction loans, and 1.3% consumer and other loans. Commercial loans consisted primarily of business loans such as owner-occupied commercial development, retail, builders/contractors, medical, service and professional, hospitality, nonprofits, marine industry, and a small portion of agricultural and seafood loans.

Total nonperforming assets consisted of nonaccrual loans, performing restructured loans, repossessed and foreclosed properties, and other real estate owned. Nonperforming assets were $5,518,766 at December 31, 2022, which represented a 18.1% decrease from $6,736,507 at December 31, 2021. Past due loans over 30 days, excluding nonaccrual, totaled $366,697 and $1,143,230 as of December 31, 2022 and 2021, respectively. Nonaccrual loans were $3.1 million or 0.4% of total loans at December 31, 2022. On December 31, 2021, nonaccrual loans totaled $2.0 million or 0.3% of total loans.

Investment Securities: All of CFS's debt securities are classified as securities available for sale and are carried at fair market value. Debt securities may be classified as investment securities (held to maturity) when management has the intent and CFS has the ability at the time of purchase to hold the securities to maturity. Securities available for sale include securities that may be sold in response to changes in market interest rates, changes in the securities option or credit risk, increases in loan demand, general liquidity needs and other similar factors.

The fair market value of the portfolio was $60,539,699 less than amortized cost at December 31, 2022, and was $11,955,055 greater than amortized cost at December 31, 2021. Investments are reviewed quarterly for potential other-than-temporary impairment (OTTI) and subsequent write-down. There were no impaired investments as of December 31, 2022. All decreases in fair market value were as a result of the current rate and economic environment.

At December 31, 2022, total securities at fair market value were $446.4 million, down $154.2 million from $600.6 million on December 31, 2021. The below table represents the investment mix for the years ended December 31, 2022 and 2021.

	2022	2021	Change	Percent Change
US Treasury	$ 432,207	$ 11,937,503	$ (11,505,296)	(96.4%)
Securities of state and political subdivisions	237,604,900	373,295,994	(135,691,094)	(36.3%)
SBA loan pooled securities	2,301,665	2,871,798	(570,133)	(19.9%)
Mortgage-backed securities	161,824,604	162,439,227	(614,623)	(0.4%)
Other debt securities	44,285,905	50,099,545	(5,813,640)	(11.6%)
	$ 446,449,281	$ 600,644,067	$ (154,194,786)	(25.7%)

Asset Quality-Provision/Allowance for Loan Losses: The provision for loan losses is a charge against earnings necessary to maintain the allowance for loan losses at a level consistent with management's evaluation of the credit quality and risk adverseness of the loan portfolio. The allowance for loan losses represents management's estimate of the amount adequate to provide for potential losses inherent in the loan portfolio. To achieve this goal, the loan loss provision must be sufficient to cover loans charged off plus any growth in the loan portfolio and recognition of specific loan impairments. In determining the adequacy of the allowance for loan losses, management uses a methodology which specifically identifies and reserves for higher risk loans. Loans in a nonaccrual status and over 90 days past due are considered in this evaluation as well as other loans, which may be a potential loss. The status of nonaccrual and past due loans varies from quarter to quarter based on seasonality, local economic conditions, and the cash flow of customers. A general reserve is established for nonspecifically reserved loans.

The allowance for loan losses was $7,512,577, or 1.0%, of non-PPP gross loans at December 31, 2022. This ratio was 1.0% on December 31, 2021, and 1.3% at December 31, 2020. The table below represents the provision for loan losses taken in years 2022 and 2021 as well as loans charged off and subsequent recoveries.

	2022	2021
Provision for (reversal of) loan losses	$ 699,996	$ (400,004)
Loans charged off	156,417	153,850
Recoveries	175,598	115,533

Management and the Board of Directors believe that the total allowance at December 31, 2022 was adequate relative to current levels of risk in the portfolio. However, continued loan growth or increases in specific problem loans may warrant additional provisions in the future. Management has also assessed the allowance for loan and lease losses under the Current Expected Credit Loss (CECL) model. The Company currently estimates the allowance for loan losses will increase by a range of $0 and $300 thousand. In addition, the Company expects to recognize a liability for unfunded commitments between $400 thousand and $500 thousand upon adoption.

Foreclosed Assets: As of December 31, 2022, the Bank held $970,812 in foreclosed assets. These assets are being actively marketed through real estate channels and represent near term secondary sources of liquidity. The Company was able to dispose of three other real estate owned properties during 2022.

Liabilities

Deposits: CFS depends on deposits to fund most of its lending activities, generate fee income opportunities, and create a market for other financial service products. Deposits are also the largest component of CFS's liabilities and account for the greatest portion of interest expense.

Deposits totaled $1.2 billion and $1.1 billion, as of December 31, 2022 and 2021, respectively, and represented an increase of 3.7% for December 31, 2022 over December 31, 2021. The below table represents a breakdown of total deposits.

	2022	2021	Change	Percent Change
Demand accounts	$ 343,930,336	$ 313,857,448	$ 30,072,888	9.6%
Savings and interest bearing deposits	702,647,684	671,804,955	30,842,729	4.6%
Certificates of deposit	119,661,968	139,309,104	(19,647,136)	(14.10%)
Total deposits	$ 1,166,239,988	$ 1,124,971,507	$ 41,268,481	3.67%

Net Interest Income: The principal source of earnings for CFS is net interest income. Net interest income is the difference between interest plus fees generated by earning assets and interest expense paid to fund those assets. As such, net interest income represents the gross profit from the Bank's lending, investment, and funding activities.

A large number of variables interact to affect net interest income. Included are variables such as changes in the mix and volume of earning assets and interest bearing liabilities, market interest rates, and the statutory federal tax rate. It is management's ongoing policy to maximize net interest income through the development of balance sheet and pricing strategies while maintaining appropriate risk levels as set by the Board of Directors.

Net interest income totaled $44.1 million and $41.6 million, for 2022 and 2021, respectively, representing an increase of 6.1% for 2022 over 2021. Total interest income was $47.3 million and $44.9 million for 2022 and 2021, respectively. Total interest expense was $3.2 million and $3.3 million for 2022 and 2021, respectively. On a consolidated tax equivalent annualized basis, the 2022 net interest margin was 3.7%.

Noninterest Income: Noninterest income represented 32.0% of the total gross revenue for the Company. Sources of noninterest income include the Company's merchant processing services (Chesapeake Payment Systems), accounts receivable financing (Flexent), wealth management and trust services (Chesapeake Wealth Management) and mortgage banking income.

For the year ended December 31, 2022, noninterest income was $22.2 million. This represents an increase in noninterest income of $2,879,713 for the year. The contributors to the increase in noninterest income was a gain on sale of an investment held at cost totaling $2,163,342, gain received on the termination of interest rate cap totaling $3,468,395 and the cash management program recovering from the negative impact the COVID-19 pandemic had on the program in 2020 and 2021. Along with that, CFS had an increase in merchant services income and interchange income. Changes in noninterest income categories are highlighted below.

	2022	2021	Change	Percent Change
Trust and wealth management income	$ 4,074,761	$ 4,391,806	$ (317,045)	(7.2%)
Service charge income	972,320	770,347	201,973	26.2%
Net (loss) gain on sales of securities available for sale	(3,303,287)	730,035	(4,033,322)	(552.5%)
Mortgage banking income	1,678,833	2,776,845	(1,098,012)	(39.5%)
Merchant services income, net	4,934,928	4,061,549	873,379	21.5%
Cash management fee income	3,196,595	2,025,501	1,171,094	57.8%
Interchange income	2,396,683	2,182,927	213,756	9.8%
Gain on termination of interest rate cap	3,468,395	–	3,468,395	100.0%
Gain on sale of investment held at cost	2,163,342	–	2,163,342	100.0%
Other income	2,609,351	2,373,198	236,153	10.0%
Total noninterest income	$ 22,191,921	$ 19,312,208	$ 2,879,713	14.9%

Noninterest Expenses: Total noninterest expenses increased 2.7%, or $1.2 million in 2022 over 2021. Comparing 2022 to 2021, provision for cash management account losses decreased $1.6 million. In 2021, there was an additional provision taken to replenish the reserve after charging off a $2.3 million relationship. Advertising expense and other expense increased $0.5 million each. Software expense increased $0.3 million due to investments in technology and the adopted multi-year human + digital strategy. Below is a breakdown of other expenses for 2022 over 2021.

	2022	2021	Change	Percent Change
Provision for cash management account losses	$ 240,000	$ 1,845,000	$ (1,605,000)	(87.0%)
Advertising	1,881,565	1,412,661	468,904	33.2%
Software	3,320,629	3,007,784	312,845	10.4%
Professional fees	2,040,685	1,836,116	204,569	11.1%
Debit card expense	947,279	802,989	144,290	18.0%
Franchise tax	1,072,053	866,471	205,582	23.7%
Contributions	461,016	614,038	(153,022)	(24.9%)
Exam and audit	273,741	298,318	(24,577)	(8.2%)
Legal fees	163,823	508,080	(344,257)	(67.8%)
FDIC assessments	369,568	349,753	19,815	5.7%
Delivery and transportation	319,108	286,960	32,148	11.2%
Stationery and supplies	292,292	233,766	58,526	25.0%
Other	4,562,816	4,014,372	548,444	13.7%
Total noninterest expenses	$ 15,944,575	$ 16,076,308	$ (131,733)	(0.8%)

Liquidity, Interest Rate Sensitivity, and Inflation: The objectives of CFS's liquidity management policy include providing adequate funds to meet the needs of depositors and borrowers at all times, as well as providing funds to meet the basic needs for ongoing operations of CFS, and to allow funding of longer-term investment opportunities and regulatory requirements. The objective of providing adequate funding should be accomplished at reasonable costs and on a timely basis. At December 31, 2022, management considers CFS's liquidity to be more than adequate.

The Company obtains funding from a variety of sources, including customer deposits and certificates of deposit, and payments on our loans and investments. In addition, the Company maintains lines of credit with the FHLB of Atlanta and various other correspondent banks. Bank management maintains overnight borrowing relationships with correspondent banks for up to $234.8 million, secured and unsecured. CFS has access to an additional secured borrowing relationship of $10.0 million.

Since the assets and liabilities of a bank are primarily monetary in nature (payable in fixed, determinable amounts), the performance of a bank is affected more by changes in interest rates than by inflation. Interest rate sensitivity refers to the difference between assets and liabilities subject to repricing, maturity, or volatility during a specified period. Management's objective in controlling interest rate sensitivity is to reprice loans and deposits and make investments that will maintain a profitable net interest margin (see "Net Interest Income"). The Company's Asset-Liability Committee ("ALCO") meets regularly and is responsible for reviewing the interest rate sensitivity position and establishing policies and strategies to monitor and limit exposure. From time-to-time CFS will enter into derivative contracts to aid in the asset liability management of its balance sheet. During 2022 the Company unwound an interest rate cap that resulted in a gain of $3.5 million, which was offset by the sale of investments with a loss of $3.5 million. Also, during 2022, the Company entered into a receive-fixed, pay-variable interest rate swap.

While the effect of inflation is normally not as significant as its influence on those businesses that have large investments in plant and inventories, it does have an effect. There are normally corresponding increases in the money supply, and banks will normally experience above average growth in assets, loans and deposits. Also, general increases in the prices of goods and services will result in increased operating expenses.

Shareholders' Equity: Capital represents funds, earned or obtained, over which management can exercise greater control in comparison with deposits and borrowed funds. Future growth and expansion of CFS is dictated by the ability to produce capital. The adequacy of CFS's capital is reviewed by management and the Board of Directors on an ongoing basis with reference to the size, composition and quality of CFS's asset and liability levels and consistent with regulatory requirements and industry standards. Management seeks to maintain a capital structure that assures an adequate level to support anticipated asset growth and absorb potential losses.

The Company's capital position as of December 31, 2022 is consistent with being well-capitalized under the regulatory framework for prompt corrective action. The table below represents CFS's capital ratios as of December 31, 2022 and December 31, 2021.

	2022	2021
Total capital to risk-weighted assets	15.9%	15.2%
Tier 1 capital to risk-weighted assets	13.0%	12.3%
Tier 1 capital to average assets	9.6%	8.9%
Common equity tier 1 capital to risk-weighted assets	12.5%	11.8%

Dividend and Market Information: The Company's stock trades on the "OTC" (Over the Counter) market under the symbol "CPKF". The Company has increased its dividend payment annually for more than 30 years. The Company raised its dividend to $0.58 per share in 2022, an increase of $0.05 over 2021. Trades in the Company's common stock occurred infrequently and generally involved a relatively small number of shares. Based on information available, the selling price for the Company's common stock during 2022 ranged from $19.15 to $31.00, and during 2021, from $21.50 to $30.20. Such transactions may not be representative of all transactions during the indicated periods of the fair value of the stock at the time of such transactions due to the infrequency of trades and the limited market for the stock. At December 31, 2022, there were 4,713,265 shares of the Company's common stock outstanding held by approximately 242 holders of record. During 2022 CFS purchased and retired 46,015 shares of CPKF.

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