Dogwood State Bank

Report on Financial Statements

For the years ended December 31, 2022 and 2021

Page

Independent Auditor's Report

Board of Directors
Dogwood State Bank

Report on the Financial Statements

We have audited the financial statements of Dogwood State Bank (the "Company"), which comprise the balance sheets as of December 31, 2022 and 2021, the related statements of income, comprehensive income, changes in shareholders' equity, and cash flows for the years then ended, and the related notes to the 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 its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

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.

Auditor's Responsibilities for the Audit of the Financial Statements, Continued

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, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control. Accordingly, no such opinion is expressed.

- 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.

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
March 30, 2023

Dogwood State Bank

Balance Sheets

As of December 31, 2022 and 2021

(dollars in thousands, except share information)

	2022	2021
Assets		
Cash and cash equivalents		
Cash and due from banks	$ 3,149	$ 2,705
Interest-earning deposits with banks	36,734	92,402
Total cash and cash equivalents	39,883	95,107
Investment securities available for sale (amortized cost of $45,533 and $69,453 at December 31, 2022 and 2021)	41,043	68,821
Investment securities held to maturity (fair value of $69,500 and $42,063 at December 31, 2022 and 2021)	81,512	42,449
Marketable equity securities	252	243
Loans held for sale	11,545	9,330
Paycheck Protection Program (PPP) loans	6,656	61,327
Loans, excluding PPP loans	876,122	591,679
Allowance for loan losses	(8,728)	(6,625)
Loans, net	867,394	585,054
Premises and equipment, net	17,377	16,360
Bank-owned life insurance	26,707	26,268
Goodwill	7,016	7,016
Other intangible assets, net	126	343
Accrued interest receivable and other assets	18,745	12,771
Total assets	$ 1,118,256	$ 925,089
Liabilities and Shareholders' Equity		
Liabilities		
Deposits:		
Non-interest bearing demand	$ 315,804	$ 236,162
Interest-bearing demand	96,895	111,598
Money market and savings	339,872	340,726
Time	151,345	99,228
Total deposits	903,916	787,714
FHLB advances	60,000	4,000
Lease liability	9,730	8,584
Accrued interest payable and other liabilities	6,693	5,834
Total liabilities	980,339	806,132
Commitments and contingencies (Note 11)		
Shareholders' Equity		
Preferred stock (1,000,000 shares authorized; no shares outstanding in any period)	-	-
Voting common stock, par value $1 (20,000,000 shares authorized; 8,382,996 and 7,677,680 shares issued and outstanding at December 31, 2022 and 2021, respectively)	8,383	7,678
Non-voting common stock, par value $1 (9,000,000 shares authorized; 5,444,920 shares issued and outstanding at December 31, 2022 and 2021, respectively)	5,445	5,445
Additional paid-in-capital	116,129	103,869
Accumulated earnings	13,199	2,604
Accumulated other comprehensive loss	(5,239)	(639)
Total shareholders' equity	137,917	118,957
Total liabilities and shareholders' equity	$ 1,118,256	$ 925,089

See Notes to Financial Statements

Dogwood State Bank

Statements of Income

For the years ended December 31, 2022 and 2021

(dollars in thousands, except share information)

	2022	2021
Interest Income		
Loans	$ 35,857	$ 26,407
Investment securities	3,706	1,187
Federal funds sold and interest-earning deposits	733	102
Total interest income	40,296	27,696
Interest Expense		
Deposits	3,141	1,428
FHLB advances	463	98
PPPLF borrowings	-	53
Lease liability	199	179
Total interest expense	3,803	1,758
Net interest income	36,493	25,938
Provision for loan losses	2,710	2,868
Net interest income after provision for loan losses	33,783	23,070
Non-interest income		
Government-guaranteed lending	9,841	13,279
Service charges and fees on deposit accounts	1,311	878
Bank-owned life insurance	696	580
Gain on sale of marketable equity securities	9	4
Other	215	265
Total non-interest income	12,072	15,006
Non-interest expense		
Salaries, employee benefits, and other compensation	21,632	25,829
Occupancy and equipment	2,210	2,010
Data processing	1,144	1,020
Loss on sale of portfolio loans	331	-
Amortization of other intangible assets	217	323
Other	6,669	5,218
Total non-interest expense	32,203	34,400
Income before income taxes	13,652	3,676
Income tax expense (benefit)	3,057	(717)
Net income	$ 10,595	$ 4,393

See Notes to Financial Statements

Dogwood State Bank

Statements of Comprehensive Income

For the years ended December 31, 2022 and 2021

(dollars in thousands, except share information)

	2022	2021
Net income	$ 10,595	$ 4,393
Other comprehensive loss		
Unrealized losses on investment securities available for sale:		
Net unrealized losses on investment securities available for sale	(4,332)	(1,585)
Tax effect	1,017	372
Reclassification adjustment for net realized gains on investment securities	-	(4)
Tax effect	-	1
Total change in unrealized losses on investment securities available for sale, net of tax	(3,315)	(1,216)
Unrealized losses on investment securities available for sale transferred to held to maturity:		
Unrealized losses on investment securities available for sale transferred to held to maturity	(2,154)	(203)
Tax effect	506	48
Accretion of unrealized losses on investment securities held to maturity previously recognized in other comprehensive income	474	17
Tax effect	(111)	(4)
Total change in unrealized losses on investment securities available for sale transferred to held to maturity, net of tax	(1,285)	(142)
Other comprehensive loss, net of tax	(4,600)	(1,358)
Total comprehensive income	$ 5,995	$ 3,035

See Notes to Financial Statements

Dogwood State Bank

Statements of Changes in Shareholders' Equity

For the years ended December 31, 2022 and 2021

(dollars in thousands, except share information)

	Number of voting shares	Number of non-voting shares	Voting common stock	Non-voting common stock	Additional paid-in capital	Accumulated earnings (deficit)	Accumulated other comprehensive income (loss)	Total shareholders' equity
Balance, December 31, 2020	5,597,126	5,444,920	$ 5,597	$ 5,445	$ 77,603	$ (1,789)	$ 719	$ 87,575
Net income	-	-	-	-	-	4,393	-	4,393
Other comprehensive loss	-	-	-	-	-	-	(1,358)	(1,358)
Common stock issued	2,326,839	-	2,327	-	25,493	-	-	27,820
Restricted stock awards issued	117,500	-	118	-	(118)	-	-	-
Restricted stock awards forfeited	(10,000)	-	(10)	-	10	-	-	-
Vesting restricted stock tax withholding	(353,785)	-	(354)	-	(6,223)	-	-	(6,577)
Stock warrant repurchased	-	-	-		(170)			(170)
Stock-based compensation	-	-	-	-	7,274	-	-	7,274
Balance, December 31, 2021	7,677,680	5,444,920	7,678	5,445	103,869	2,604	(639)	118,957
Net income	-	-	-	-	-	10,595	-	10,595
Other comprehensive loss	-	-	-	-	-	-	(4,600)	(4,600)
Common stock issued	664,316	-	664	-	11,280	-	-	11,944
Restricted stock awards issued	58,500	-	59	-	(59)	-	-	-
Restricted stock awards forfeited	(17,500)	-	(18)	-	18	-	-	-
Stock-based compensation	-	-	-	-	1,021	-	-	1,021
Balance, December 31, 2022	8,382,996	5,444,920	$ 8,383	$ 5,445	$ 116,129	$ 13,199	$ (5,239)	$ 137,917

See Notes to Financial Statements

Dogwood State Bank

Statements of Cash Flows

For the years ended December 31, 2022 and 2021

(dollars in thousands, except share information)

	2022	2021
Operating activities		
Net income	$ 10,595	$ 4,393
Adjustments to reconcile net income to cash provided by operating activities:		
Provision for loan losses	2,710	2,868
Deferred tax benefit	(779)	(694)
Depreciation and amortization	1,841	2,152
Stock-based compensation	1,021	7,274
Vesting restricted stock - tax witholding	-	(6,577)
Origination of loans held for sale	(148,318)	(114,246)
Proceeds from sale of loans held for sale	155,320	128,191
Gains on sale of loans	(9,217)	(13,279)
Net increase (decrease) in accrued interest payable	492	(195)
Net (increase) decrease in accrued interest receivable	(1,276)	42
Gain on sale of investment securities available for sale, net	-	12
Gain on marketable equity securities	(9)	(16)
Change in cash surrender value of bank owned life insurance	(439)	(580)
Net change in other assets	(4,661)	(6,910)
Net change in other liabilities	1,513	4,497
Net cash provided by operating activities	8,793	6,932
Investing activities		
Net increase in loans outstanding	(285,050)	(218,390)
Net decrease in PPP loans	54,671	39,783
Purchases of investment securities available for sale	(14,400)	(83,319)
Purchases of investment securities held to maturity	(12,413)	(6,355)
Purchase of marketable equity securities	-	(243)
Proceeds from maturities, calls, and principal repayments of Investment securities available for sale	3,888	12,417
Proceeds from maturities, calls, and principal repayments of Investment securities held to maturity	7,497	3,484
Proceeds from sales of investment securities available for sale	-	19,769
Purchases of bank owned life insurance	-	(10,780)
Proceeds from sales of premises and equipment	558	270
Purchases of premises and equipment	(2,914)	(422)
Net cash used in investing activities	(248,163)	(243,786)
Financing activities		
Net increase in demand, money market, and savings deposits	64,085	345,641
Net increase in time deposits	52,117	29,941
Net increase (decrease) in FHLB advances	56,000	(31,000)
Net increase (decrease) in PPPLF borrowings	-	(66,711)
Proceeds from issuance of common stock, net	11,944	27,820
Repurchase of common stock warrants	-	(170)
Net cash provided by financing activities	184,146	305,521
Change in cash and cash equivalents	(55,224)	68,667
Cash and cash equivalents, beginning of period	95,107	26,440
Cash and cash equivalents, end of period	$ 39,883	$ 95,107
Cash paid for:		
Interest	$ 3,311	$ 1,953
Income taxes	$ 983,303	$ 1,690
Supplemental disclosure of non-cash transactions		
Transfers of investment securities available for sale to investment securities held to maturity	$ 32,212	$ 37,750
Initial recognition of right-of-use asset	$ 1,796	$ 2,597
Initial recognition of lease obligation	$ 1,796	$ 2,597

See Notes to Financial Statements

Note 1. Nature of Operations and Basis of Presentation

Nature of operations:

Dogwood State Bank (the "Company") is a state-chartered bank organized under the laws of North Carolina. The Company is headquartered in Raleigh, North Carolina, and provides a wide range of banking services and products through its seven branch offices in Charlotte, Fayetteville, Greenville, Morehead City, Raleigh, Sanford and Wilmington, North Carolina. The Company also supports various guaranteed government lending (GGL) programs of the Small Business Administration (SBA) through its small business lending division.

Basis of presentation:

The accompanying financial statements include the accounts and transactions of the Company. The preparation of the Company's financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Note 2. Summary of Significant Accounting Policies

Cash and cash equivalents:

Cash and cash equivalents include cash and due from banks, interest-earning deposits with banks, and federal funds sold. Cash and cash equivalents have original maturities of three months or less. The carrying amount of such instruments is considered a reasonable estimate of fair value.

Investment securities:

The Company classifies investment securities as held to maturity, available for sale, or trading at the time of purchase. Premiums and discounts are recognized in interest income using the interest method over the period to maturity. Debt securities are classified as held to maturity where the Company has both the intent and ability to hold the securities to maturity. These securities are reported at amortized cost.

Investment securities available for sale are carried at fair value and consist of debt securities not classified as trading or held to maturity. Unrealized holding gains and losses on investment securities available for sale are reported in other comprehensive income, net of related tax effects. Gains and losses on the sale of investment securities available for sale are determined using the specific identification method recorded on a trade date basis.

Note 2. Summary of Significant Accounting Policies, continued

Investment securities, continued:

Each investment security held to maturity and available for sale in a loss position is evaluated for other-than-temporary impairment. The review includes an analysis of the facts and circumstances of each individual investment such as (1) the length of time and the extent to which the fair value has been below amortized cost, (2) changes in the earnings performance, credit rating, asset quality, or business prospects of the issuer, (3) the ability of the issuer to make principal and interest payments, (4) changes in the regulatory, economic, or technological environment of the issuer, and (5) changes in the general market condition of either the geographic area or industry in which the issuer operates.

Regardless of these factors, if the Company has developed a plan to sell the security or it is more likely than not that the Company will be forced to sell the security in the near future, then the impairment is considered other-than-temporary and the carrying value of the security is permanently written down to the current fair value with the difference between the new carrying value and the amortized cost charged to earnings. If the Company does not intend to sell the security and it is not more likely than not that it will be required to sell the security before recovery of its amortized cost basis less any current period credit loss, the other-than-temporary impairment is separated into the following: (1) the amount representing the credit loss and (2) the amount related to all other factors. The amount of the total other-than-temporary impairment related to the credit loss is recognized in earnings, and the amount of the total other-than-temporary impairment related to other factors is recognized in other comprehensive income, net of applicable taxes.

Marketable equity securities:

Investments in equity securities having readily determinable fair values are stated at fair value. Realized and unrealized gains and losses on these securities are determined by specific identification and are included in noninterest income.

Loans held for sale:

Loans held for sale include the guaranteed portion of loans originated through the small business lending division that are expected to be sold in the secondary market to investors. Loans held for sale are carried at fair value.

Paycheck Protection Program (PPP) loans:

Loans originated by the Company under the PPP represent the outstanding balance of loans to assist small businesses and non-profit organizations affected by the COVID-19 pandemic. PPP loans are fully guaranteed by the SBA, and management believes the Company will fully collect the outstanding balance of all of these loans. As of December 31, 2022 and 2021, PPP loans totaled $6,656 and $61,327, respectively. None of these loans are past due or otherwise impaired. As of December 31, 2022 and 2021, there was no allowance for PPP loans due to the full SBA guarantee.

Note 2. Summary of Significant Accounting Policies, continued

Loans, excluding PPP loans:

Loans that the Company has the intent and ability to hold for the foreseeable future, or until maturity, are reported at their outstanding principal balance, adjusted for any charge-offs, deferred fees or costs on originated loans and unamortized premiums or discounts on acquired loans. Loan origination fees and certain direct origination costs are capitalized and recognized as an adjustment to the yield of the related loan. Interest on loans is recorded based on the principal amount outstanding.

The accrual of interest on impaired loans is discontinued when the future collectability of the recorded loan balance is in doubt. When the future collectability of the recorded impaired loan balance is not in doubt, interest income may be recognized on the cash basis. Generally, loans are placed on nonaccrual status when they are past due 90 days or more. When a loan is placed in nonaccrual status, all unpaid accrued interest is reversed, and subsequent collections of interest and principal payments are generally applied as a reduction to the principal outstanding. Should the credit quality of a nonaccrual loan improve, the loan may be returned to an accrual status after demonstrating consistent payment history for at least six months.

A loan is classified as a troubled debt restructuring (TDR) when certain modifications are made to the loan terms and concessions are granted to the borrowers due to financial difficulty experienced by those borrowers.

Allowance for loan losses:

During 2020, pursuant to Section 4013 of the Coronavirus Aid, Relief, and Economic Security (CARES) Act, the Company deferred loan payments for various customers who were experiencing financial strain resulting from the COVID-19 Pandemic. Loans receiving these types of payment deferrals were not considered to be delinquent and were not classified as TDRs.

The Company's loan policies, guidelines, and procedures establish the basic guidelines governing its lending operations. They address the types of loans sought, target markets, underwriting, collateral requirements, term, interest rate, yield considerations and compliance with laws and regulations. The loan policies are reviewed and approved annually by the Board of Directors.

The allowance for loan losses (ALLL) is a reserve established through a provision for loan losses charged to expense. Loan balances are charged off against the ALLL when the collectability of principal is unlikely.

Subsequent recoveries, if any, are credited to the ALLL. The ALLL is maintained at a level based on management's best estimate of probable credit losses that are inherent in the loan portfolio. Management evaluates the adequacy of the ALLL on at least a quarterly basis.

Note 2. Summary of Significant Accounting Policies, continued

Allowance for loan losses, continued:

The Company segments the loan portfolio into broad categories with similar risks for the purposes of computing the Allowance for loan losses. Certain of these broad groupings are further segmented based on additional risks used to calculate the ALLL. Management evaluates loans originated under government guaranteed lending (GGL) programs separately from loans originated from traditional sources due to risks specific to GGL lending, including risks related to customers being out of the Company's primary market areas.

The Company's loan segments and the specific risks of each segment are described below.

Construction/development loans – Risks common to construction/development loans are cost overruns, changes in market demand for property, inadequate long-term financing arrangements and declines in real estate values. Construction/development loans are further segmented into residential construction/development loans, GGL construction/development loans and other construction/development loans. Residential construction/ development loans are also susceptible to risks associated with residential mortgage loans. Changes in market demand for property could lead to longer marketing times resulting in higher carrying costs, declining values, and higher interest rates.

Commercial real estate loans – Loans in this category are susceptible to declines in occupancy rates, business failure and general economic conditions. Also, declines in real estate values and lack of suitable alternative use for the properties are risks for loans in this category. Commercial real estate loans are further segmented into loans secured by non-owner occupied commercial real estate, loans secured by owner-occupied real estate that are originated under GGL programs, and loans secured by all other owner-occupied commercial real estate.

1-4 family loans – Residential mortgage loans are susceptible to weakening general economic conditions and increases in unemployment rates and declining real estate values. This segment includes loans secured by both first lien and subordinate lien positions.

Commercial and industrial loans – Risks to this loan category include industry concentration and the inability to monitor the condition of the collateral which often consists of inventory, accounts receivable and other non-real estate assets. Equipment and inventory obsolescence can also pose a risk. Declines in general economic conditions and other events can cause cash flows to fall to levels insufficient to service debt. Commercial and industrial loans are further segmented into commercial and industrial loans estate that are originated under GGL programs, including solar, and all other commercial and industrial loans.

Home equity loans – Risks common to home equity loans and lines of credit are general economic conditions, including an increase in unemployment rates, and declining real estate values which reduce or eliminate the borrower's home equity.

Note 2. Summary of Significant Accounting Policies, continued

Allowance for loan losses, continued:

Other consumer loans – Risks common to these loans include regulatory risks, unemployment and changes in local economic conditions as well as the inability to monitor collateral consisting of personal property.

The evaluation of the adequacy of the ALLL includes both loans evaluated collectively for impairment and loans evaluated individually for impairment. For loans evaluated collectively for impairment, loans are grouped based on common risk characteristics. Historical loss rates are then combined with certain qualitative factors to determine the ALLL reserve rates for each loan grouping. Qualitative factors include consideration of certain internal and external factors, such as loan delinquency levels and trends, loan growth, loan portfolio composition and concentrations, local and national economic conditions, the loan review function, and other factors management deems relevant to the ALLL calculation.

A loan is considered individually impaired when, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal and interest when due according to the contractual terms of the loan agreement. Reserves, or charge-offs, on individually impaired loans that are collateral dependent are based on the fair value of the underlying collateral, less an estimate of selling costs, while reserves, or charge-offs, on loans that are not collateral dependent are based on either an observable market price, if available, or the present value of expected future cash flows discounted at the historical effective interest rate. The Company evaluates loans that are classified as doubtful, substandard or special mention to determine whether or not they are individually impaired. This evaluation includes several factors, including review of the loan payment status and the borrower's financial condition and operating results such as cash flows, operating income or loss, etc.

Purchased credit-impaired loans:

The evaluation of the ALLL is inherently subjective, and management uses the best information available to establish this estimate. However, if factors such as economic conditions differ substantially from assumptions, or if amounts and timing of future cash flows expected to be received on impaired loans vary substantially from the estimates, future adjustments to the ALLL may be necessary.

Loans acquired in a transfer, including business combinations, where there is evidence of credit deterioration since origination and it is probable at the date of acquisition that we will not collect all contractually required principal and interest payments, are accounted for as purchased credit-impaired (PCI) loans. Where possible, PCI loans with common risk characteristics are grouped into pools at acquisition. For PCI loan pools, the excess of the cash flows initially expected to be collected over the fair value of the loans at the acquisition date (i.e., the accretable yield) is accreted into interest income over the estimated remaining life of the PCI loans using the effective yield method, provided that the timing and the amount of future cash flows is reasonably estimable.

Note 2. Summary of Significant Accounting Policies, continued

Purchased credit-impaired loans, continued:

Accordingly, such loans are not classified as nonaccrual and they are considered to be accruing because their interest income relates to the accretable yield recognized under accounting for PCI loans and not to contractual interest payments. The difference between the contractually required payments and the cash flows expected to be collected at acquisition, considering the impact of prepayments, is referred to as the nonaccretable difference.

Subsequent to acquisition, estimates of cash flows expected to be collected are updated based on current assumptions regarding default rates, loss severities, and other factors that are reflective of current market conditions. If the Company has probable decreases in pool-level cash flows expected to be collected, the provision for loan losses is charged, resulting in an increase to the ALLL. If the Company has probable and significant increases in pool-level cash flows expected to be collected, the Company will first reverse any previously established ALLL and then increase interest income as a prospective yield adjustment over the remaining life of the loan pool. The impact of changes in variable interest rates is recognized prospectively as adjustments to interest income.

Premises and equipment:

Land is carried at cost. Other components of premises and equipment are stated at cost less accumulated depreciation. Depreciation is calculated on the straight-line method over the estimated useful lives of assets, which range from thirty-seven to forty years for buildings and three to seven years for furniture and equipment. Leasehold improvements are amortized over the terms of the respective leases or the estimated useful lives of the improvements, whichever is shorter. Repairs and maintenance costs are charged to operations as incurred, and additions and improvements to premises and equipment are capitalized. Upon sale or retirement, the cost and related accumulated depreciation are removed from the accounts and any gains or losses are reflected in earnings.

Premises and equipment are reviewed for impairment whenever events or changes in circumstances indicate that the carrying value may not be recoverable. Assets to be disposed of are transferred to other real estate owned and are reported at the lower of the carrying amount or fair value less costs to sell.

Bank-owned life insurance:

The Company has purchased life insurance policies on certain current and former employees and directors. These policies are recorded at their cash surrender value, or the amount that could be realized by surrendering the policies. Income from these policies and changes in the net cash surrender value are recorded in non-interest income.

Income taxes:

Deferred tax assets and liabilities are included in other assets. Deferred tax assets and liabilities reflect the estimated future tax consequences attributable to differences between the tax basis of assets and liabilities and their carrying amounts for financial reporting purposes. Deferred tax assets are also

Note 2. Summary of Significant Accounting Policies, continued

Income taxes, continued:

recognized for operating loss carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates in effect for the year in which the temporary differences are expected to be recovered or settled. Deferred tax assets are reduced by a valuation allowance if it is more likely than not that the tax benefits will not be realized.

Income taxes:

Deferred tax assets and liabilities are included in other assets. Deferred tax assets and liabilities reflect the estimated future tax consequences attributable to differences between the tax basis of assets and liabilities and their carrying amounts for financial reporting purposes. Deferred tax assets are also recognized for operating loss carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates in effect for the year in which the temporary differences are expected to be recovered or settled. Deferred tax assets are reduced by a valuation allowance if it is more likely than not that the tax benefits will not be realized.

Other real estate owned:

Other real estate owned is included in other assets and includes assets acquired through loan foreclosure. These properties are held for sale and are initially recorded at fair value less costs to sell upon foreclosure. After foreclosure, valuations are periodically performed, and the assets are carried at the lower of carrying amount or fair value less cost to sell. Revenue and expenses from operations and valuation adjustments are included in noninterest expense. There was no other real estate owned as of December 31, 2022 or 2021.

Equity investments at cost:

As a requirement for membership, the Company has invested in common stock of the Federal Home Loan Bank of Atlanta. This investment, which is included in other assets, is carried at cost and is periodically evaluated for impairment.

Stock-based compensation:

Compensation cost is recognized for restricted stock awards granted to employees. Compensation cost is based on the fair value of restricted stock awards based on the market price of the Company’s common stock at the date of grant. Compensation cost is recognized over the required service period, generally defined as the vesting period for restricted stock awards.

Note 2. Summary of Significant Accounting Policies, continued

Fair value measurements:

Fair value is defined as the exchange price that would be received to sell an asset or paid to transfer a liability in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. The Company follows the fair value hierarchy which gives the highest priority to quoted prices in active markets (observable inputs) and the lowest priority to management's assumptions (unobservable inputs). For assets and liabilities recorded at fair value, the Company's policy is to maximize the use of observable inputs and minimize the use of unobservable inputs when developing fair value measurements.

The Company utilizes fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. Investment securities available for sale are recorded at fair value on a recurring basis. Additionally, the Company may be required to record at fair value other assets on a nonrecurring basis, such as impaired loans and other real estate owned. These nonrecurring fair value adjustments typically involve application of lower of cost or market accounting or write-downs of individual assets.

Assets and liabilities measured at fair value are grouped 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. An adjustment to the pricing method used within either Level 1 or Level 2 inputs could generate a fair value measurement that effectively falls to a lower level in the hierarchy. These levels are described as follows:

Level 1: Valuations for assets and liabilities traded in active exchange markets.

Level 2: Valuations for assets and liabilities that can be obtained from readily available pricing sources via independent providers for market transactions involving similar assets or liabilities. The Company's principal market for these securities is the secondary institutional markets, and valuations are based on observable market data in those markets.

Level 3: Valuations for assets and liabilities that are derived from other valuation methodologies, including discounted cash flow models and similar techniques, and not based on market exchange, dealer, or broker traded transactions. Level 3 valuations incorporate certain assumptions and projections in determining the fair value assigned to such assets or liabilities.

The determination of where an asset or liability falls in the fair value hierarchy requires significant judgment. The Company evaluates its hierarchy disclosures at each reporting period and based on various factors, it is possible that an asset or liability may be classified differently. However, management expects that changes in classifications between levels will be rare.

(dollars in thousands, except share information)

Note 2. Summary of Significant Accounting Policies, continued

Accumulated other comprehensive loss:

The Company's accumulated other comprehensive loss is comprised of unrealized gains and losses, net of taxes, on investment securities available for sale.

Segment reporting:

Operating segments are components of an enterprise about which separate financial information is available that is evaluated regularly by the chief operating decision maker in deciding how to allocate resources and in assessing performance. Management has determined that the Company has a single operating segment, which is providing general commercial banking and financial services to individuals and businesses located in North Carolina and to customers in various states through its GGL Small Business Administration (SBA) lending program. The Company's various products and services are those generally offered by community banks, and the allocation of resources is based on the overall performance of the Company versus individual regions, branches, products and services.

Revenue from contracts with customers:

All of the Company's revenues that are within the scope of ASC 606 are recognized within noninterest income. The following table presents 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.

	Year ended December 31,	
	2022	**2021**
Non-interest income		
Government-guaranteed lending[1]	$ 9,841	$ 13,279
Service charges and fees on deposit accounts	1,311	878
Bank-owned life insurance[1]	696	580
Gain on sales of investment securities available for sale, net[1]	9	4
Other[2]	215	265
Total non-interest income	$ 12,072	$ 15,006

[1]Not within the scope of ASC 606

[2]The other category includes $215 and $265 of income sources that are within the scope of ASC 606 but determined immaterial as of December 31, 2022 and 2021, 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 has noninterest income related to government-guaranteed lending, changes in cash surrender value of life insurance and sales of investment securities available for sale, these are not within the scope of ASC 606. Service charge revenue generated from contracts with customers is noninterest income and relates to fees charged on deposit accounts and certain loan and deposit fees.

Note 2. Summary of Significant Accounting Policies, continued

Revenue from contracts with customers, continued:

Revenues generated from each of these contracts are recognized when a performance obligation is met, and each obligation is associated with a transaction tied to an account. Given each of these accounts are transactional and the related contracts are day-to-day contracts, the performance obligations on these accounts occur when the contract provision is triggered on the account, which results in the related service charge.
Based on the Company's analysis, there are no fees generated for opening an account or for a service on the account where the good or service has not been transferred or prior to the performance obligation being met.

As of December 31, 2022 and 2021, the Company did not have amounts of material receivables, contract assets or contract liabilities tied to these contracts with customers. The Company believes that while loan and deposit accounts generate service charge income, these contracts do not create receivables, assets or liabilities given the fees associated with these service charges are typically charged and collected once the performance obligation is triggered. In addition, during the years ended December 31, 2022 and 2021, the Company did not recognize revenue that was included in any contract liabilities, and no revenues were recognized related to performance obligations satisfied in prior reporting periods. The Company analyzes its payment streams associated with contracts with customers on a quarterly basis.

As of December 31, 2022 and 2021, the nature of the performance obligations within the contracts generating these service charges on deposit and loan accounts have a duration of one year or less. Also, based on the Company's analysis and the nature of the contracts discussed within this note, management determined that there are no significant judgements associated with the recognition of revenue associated with these contracts. Based on the Company's analysis, each of the service charge revenues discussed above are associated with the transfer of services through administration of a customer's deposit account or through an agreed-upon, fixed amount that is disclosed in the customer's contract and are charged to the customer when the related service is performed on the customer's account. In addition, 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 asset associated with these contracts as of December 31, 2022 and 2021.

Recently issued accounting pronouncements:

FASB ASU 2016-13, *Financial Instruments-Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments (ASC 326)*

In June 2016, the FASB issued ASC 326 to change the accounting for credit losses and modify the impairment model for certain debt securities. As discussed below, subsequent additional guidance related to ASC 326 has resulted in an anticipated adoption no later than periods beginning after December 15, 2022. ASC 326 introduces a new credit loss methodology which requires earlier recognition of credit losses, replacing multiple impairment methods currently allowed under accounting principles generally accepted in the United States of America.

Note 2. Summary of Significant Accounting Policies, continued

Recently issued accounting pronouncements, continued:

FASB ASU 2016-13, *Financial Instruments-Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments (ASC 326), continued*

The ASC 326 amendments require loss estimates be determined over the lifetime of the asset and broaden the information an entity must consider in developing its expected credit losses. ASC 326 does not specify a method for measuring expected credit losses and allows an entity to apply methods that reasonably reflect its expectations of the credit loss estimate based on the entity's size, complexity and risk profile. The standard will apply to the Company's loans, unfunded loan commitments and debt securities.

The Company will apply the amendments to ASC 326 through a cumulative-effect adjustment to retained earnings as of the beginning of the year of adoption. As a result of the adoption of ASC 326 on January 1, 2023, the Company estimates that there will be a charge to retained earnings in the range of $1.4 million to $1.8 million, net of tax, arising from an increase to the allowance for loan losses and reserve for unfunded commitments. There is no allowance for credit losses on held-to-maturity debt securities anticipated at adoption. This impact will be fully recognized in 2023.

FASB ASU 2022-02, Financial Instruments—Credit Losses (Topic 326): Troubled Debt Restructurings and Vintage Disclosures

In March 2022, the FASB issued ASU 2022-02. The amendments in this ASU: (i) eliminate the previous recognition and measurement guidance for TDRs and requires an entity to apply the loan refinancing and restructuring guidance to determine whether a modification results in a new loan or a continuation of an existing loan, (ii) require new disclosures for loan modifications when a borrower is experiencing financial difficulty and (iii) require disclosures of current period gross charge-offs by year of origination in the vintage disclosures.

The Company will adopt ASU 2022-02 on January 1, 2023, along with the adoption of ASC 326. As a result of adopting this ASU, the Company does not expect a material impact to our consolidated results of operations or our consolidated financial position. The additional disclosures are required to be applied prospectively.

Other accounting standards that have been issued or proposed by the FASB or other standards-setting bodies are not expected to have a material impact on the Company's financial position, results of operations or cash flows.

(dollars in thousands, except share information)

Note 3. Investment Securities

The following tables summarize the amortized cost, gross unrealized gains and losses, and fair value of investment securities available for sale and held to maturity by major classification:

	December 31, 2022			
	Amortized Cost	Unrealized Loss	Unrealized Gain	Fair Value
Investment securities available for sale:				
Agency residential mortgage-backed	$ 19,243	$ (2,067)	$ 34	$ 17,210
Corporate bonds	15,000	(1,424)	-	13,576
US Treasury securities	5,933	(686)	-	5,247
Agency commercial mortgage-backed	3,451	(311)	-	3,140
Agency CMO/REMIC	1,906	(55)	19	1,870
	$ 45,533	$ (4,543)	$ 53	$ 41,043
Investment securities held to maturity:				
Agency residential mortgage-backed	$ 36,012	$ (3,568)	$ -	$ 32,444
Agency CMO/REMIC	24,387	(4,690)	-	19,697
Taxable municipals	12,895	(2,485)	-	10,410
Municipal securities	4,990	(1,006)	-	3,984
US Government agency securities	1,885	(105)	-	1,780
Commercial mortgage-backed	1,343	(158)	-	1,185
	$ 81,512	$ (12,012)	$ -	$ 69,500

	December 31, 2021			
	Amortized Cost	Unrealized Loss	Unrealized Gain	Fair Value
Investment securities available for sale:				
Agency residential mortgage-backed	$ 35,896	$ (397)	$ 29	$ 35,528
Agency CMO/REMIC	10,485	(176)	13	10,322
Corporate bonds	11,000	(48)	84	11,036
US Treasury securities	5,927	(24)	25	5,928
Agency commercial mortgage-backed	4,146	(123)	-	4,023
US Government agency securities	1,999	(15)	-	1,984
	$ 69,453	$ (783)	$ 151	$ 68,821
Investment securities held to maturity:				
Taxable municipals	$ 11,664	$ (55)	$ 74	$ 11,683
Agency CMO/REMIC	17,457	(350)	-	17,107
Agency residential mortgage-backed	8,273	(61)	20	8,232
Municipal securities	5,055	(31)	17	5,041
	$ 42,449	$ (497)	$ 111	$ 42,063

(dollars in thousands, except share information)

Note 3. Investment Securities, continued

The amortized cost and fair values of investment securities available for sale and held to maturity, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	December 31, 2022	
	Amortized Cost	Fair Value
Investment securities available for sale with scheduled maturities:		
Within 1 year	$ 1,500	$ 1,440
After 1 through 5 years	16,457	15,082
After 5 years through 10 years	27,576	24,521
	$ 45,533	$ 41,043
Investment securities held to maturity with scheduled maturities:		
After 1 through 5 years	$ 2,326	$ 2,209
After 5 years through 10 years	62,055	52,781
After 10 years	17,131	14,510
	$ 81,512	$ 69,500

	December 31, 2021	
	Amortized Cost	Fair Value
Investment securities available for sale with scheduled maturities:		
Within 1 year	$ -	$ -
After 1 through 5 years	37,242	36,943
After 5 years through 10 years	32,211	31,878
	$ 69,453	$ 68,821
Investment securities held to maturity with scheduled maturities:		
After 1 through 5 years	$ 18,463	$ 18,133
After 5 years through 10 years	8,772	8,709
After 10 years	15,214	15,221
	$ 42,449	$ 42,063

During 2022, the Company transferred certain investment securities available for sale to investment securities held to maturity. At the time of the transfer the securities had an amortized cost basis of $34,365 and a fair value of $32,212. The $2,154 difference between the amortized cost basis and fair value at the date of transfer is amortized as a yield adjustment over the remaining life of the securities and the $32,213 fair value, adjusted for subsequent amortization, became the securities new cost basis.

(dollars in thousands, except share information)

Note 3. Investment Securities, continued

During 2021, the Company transferred certain investment securities available for sale to investment securities held to maturity. At the time of the transfer the securities had an amortized cost basis of $37,970 and a fair value of $37,750. The $220 difference between the amortized cost basis and fair value at the date of transfer is amortized as a yield adjustment over the remaining life of the securities and the $37,750 fair value, adjusted for subsequent amortization, became the securities new cost basis.

As of December 31, 2022, sixty-six securities totaling $74,956 in investment securities have been in an unrealized loss for more than twelve months. As of December 31, 2021, four securities totaling $4,687 in investment securities have been in an unrealized loss position for more than a twelve-month period.

The securities in an unrealized loss position as of December 31, 2022 and 2021 continue to perform and are expected to perform through maturity, and the issuers have not experienced significant adverse events that would call into question their ability to repay these debt obligations according to contractual terms.

Further, because the Company does not intend to sell these investments and does not believe that it will be required to sell the investments before recovery of their amortized cost bases, which may be maturity, unrealized losses on such securities were not considered to represent other-than-temporary impairment as of December 31, 2022 and 2021.

As of December 31, 2022, the Company held no individual investment securities with an aggregate book value greater than 10 percent of total shareholders' equity.

The following table summarizes realized securities gains and losses for the periods presented:

	2022	2021
Realized gains on investment securities available for sale	$ -	$ 207
Realized gains on marketable equity securities	9	17
Realized losses on investment securities available for sale	-	(220)
	$ 9	$ 4

The Company owns 36,000 shares of common stock of a North Carolina community bank. This investment is classified as a marketable equity security and has a cost basis of $227. As of December 31, 2022 and 2021, the fair value was $252 and $243, respectively.

(dollars in thousands, except share information)

Note 4. Loans and Allowance for Loan Losses

The following table summarizes the Company's loans by type:

	2022	2021
Construction/development - GGL	$ 39,926	$ 20,358
Construction/development - other	74,616	78,574
Commercial real estate - owner occupied - GGL	30,375	17,999
Commercial real estate - owner occupied - other	187,096	138,156
Commercial real estate - non-owner occupied - GGL	9,226	-
Commercial real estate - non-owner occupied - other	247,339	143,954
Commercial and industrial - GGL	63,817	52,961
Commercial and industrial - other	83,153	68,867
1-4 family	108,400	53,929
Home equity	13,988	13,378
Construction/development - residential	16,551	975
Other consumer	1,635	2,528
	$ 876,122	$ 591,679

The preceding table and all following disclosures exclude $6,656 and $61,327 of PPP loans as of December 31, 2022 and 2021, respectively.

The Company had $52,589 and $27,754 in loans guaranteed by the SBA as of December 31, 2022 and 2021, respectively.

As of December 31, 2022 and 2021, loans with a recorded investment of $371,360 and $246,726, respectively, were pledged to secure borrowings or available lines of credit with correspondent banks.

As of December 31, 2022 and 2021, there were no loans to directors and executive officers outstanding.

(dollars in thousands, except share information)

Note 4. Loans and Allowance for Loan Losses, continued

Allowance for Loan Losses

The following tables summarize the activity in the allowance for loan losses for the periods presented:

December 31, 2022

	Construction/ development - GGL	Construction / development - other	Commercial real estate – owner - occupied- GGL	Commercial real estate – owner- occupied -other	Commercial real estate – non- owner occupied- GGL	Commercial real estate – non- owner occupied - other	Commercial and industrial - GGL	Commercial and industrial - other	1-4 family	Home equity	Construction/ development - residential	Other consumer	Total
Beginning balance	$ 470	$ 642	$ 403	$ 885	$ -	$ 937	$ 1,945	$ 652	$ 564	$ 81	$ 16	$ 30	$ 6,625
Charge-offs	-	-	(132)	-	-	-	(471)	-	-	-	-	(5)	(608)
Recoveries	-	-	-	-	-	-	-	-	-	-	-	1	1
Provision (credit) for loan losses	406	(122)	372	162	204	473	956	15	186	(5)	73	(10)	2,710
Ending balance	$ 876	$ 520	$ 643	$ 1,047	$ 204	$ 1,410	$ 2,430	$ 667	$ 750	$ 76	$ 89	$ 16	$ 8,728

December 31 2021

	Construction/ development - GGL	Construction / development - other	Commercial real estate – owner - occupied- GGL	Commercial real estate – owner- occupied - other	Commercial real estate – non- owner occupied- GGL	Commercial real estate – non- owner occupied - other	Commercial and industrial - GGL	Commercial and industrial - other	1-4 family	Home equity	Construction/ development - residential	Other consumer	Total
Beginning balance	$ 164	$ 458	$ 115	$ 462	$ -	$ 554	$ 1,080	$ 475	$ 566	$ 84	$ 6	$ 23	$ 3,987
Charge-offs	-	-	-	-	-	-	(119)	(136)	-	-	-	(2)	(257)
Recoveries	-	-	-	-	-	-	-	1	24	-	-	2	27
Provision (credit) for loan losses	306	184	288	423	-	383	984	312	(26)	(3)	10	7	2,868
Ending balance	$ 470	$ 642	$ 403	$ 885	$ -	$ 937	$ 1,945	$ 652	$ 564	$ 81	$ 16	$ 30	$ 6,625

(dollars in thousands, except share information)

Note 4. Loans and Allowance for Loan Losses, continued

Allowance for Loan Losses, continued

The following tables summarize the ending allowance for loans losses and the recorded investment in loans by portfolio segment and impairment method:

	December 31, 2022												
	Construction/ development - GGL	**Construction / development - other**	**Commercial real estate – owner - occupied- GGL**	**Commercial real estate – owner- occupied - other**	**Commercial real estate – non-owner occupied- GGL**	**Commercial real estate – non-owner occupied**	**Commercial and industrial - GGL**	**Commercial and industrial - other**	**1-4 family**	**Home equity**	**Construction/ development - residential**	**Other consumer**	**Total**
Allowance for loans loss ending balance													
Collectively evaluated for impairment	$ 876	$ 518	$ 643	$ 1,047	$ 204	$ 1,410	$ 2,430	$ 659	$ 600	$ 76	$ 89	$ 13	$ 8,565
Individually evaluated for impairment	-	-	-	-	-	-	-	-	-	-	-	-	-
Purchased credit non-impaired	-	2	-	-	8	-	-	-	2	-	-	3	15
Purchased credit impaired	-	-	-	-	-	-	-	-	148	-	-	-	148
	$ 876	$ 520	$ 643	$ 1,047	$ 212	$ 1,410	$ 2,430	$ 659	$ 750	$ 76	$ 89	$ 16	$ 8,728
Loans ending balance													
Collectively evaluated for impairment	$ 39,926	$ 74,347	$ 30,161	$ 185,939	$ 9,165	$ 242,098	$ 63,459	$ 82,783	$ 106,598	$ 13,150	$ 16,551	$ 1,534	$ 865,711
Individually evaluated for impairment	-	-	214	-		-	357	367	123	2	-	-	1,063
Purchased credit non-impaired	-	269	-	795	61	4,861	1	3	1,295	836	-	101	8,222
Purchased credit impaired	-	-	-	362	-	380	-	-	384	-	-	-	1,126
	$ 39,926	$ 74,616	$ 30,375	$ 187,096	$ 9,226	$ 247,339	$ 63,817	$ 83,153	$ 108,400	$ 13,988	$ 16,551	$ 1,635	$ 876,122

(dollars in thousands, except share information)

Note 4. Loans and Allowance for Loan Losses, continued

Allowance for Loan Losses, continued

The following tables summarize the ending allowance for loans losses and the recorded investment in loans by portfolio segment and impairment method:

	December 31, 2021											
	Construction/ development - GGL	Construction / development - other	Commercial real estate – owner - occupied- GGL	Commercial real estate – owner- occupied -other	Commercial real estate – non- owner occupied	Commercial and industrial - GGL	Commercial and industrial - other	1-4 family	Home equity	Construction/ development - residential	Other consumer	Total
Allowance for loans loss ending balance												
Collectively evaluated for impairment	$ 470	$ 636	$ 398	$ 881	$ 937	$ 1,945	$ 652	$ 342	$ 81	$ 6	$ 28	$ 6,376
Individually evaluated for impairment	-	-	-	-	-	-	-	-	-	-	-	-
Purchased credit non-impaired	-	4	5	4	-	-	-	7	-	-	2	22
Purchased credit impaired	-	2	-	-	-	-	-	215	-	10	-	227
	$ 470	$ 642	$ 403	$ 885	$ 937	$ 1,945	$ 652	$ 564	$ 81	$ 16	$ 30	$ 6,625
Loans ending balance												
Collectively evaluated for impairment	$ 20,358	$ 78,062	$ 17,749	$ 132,850	$ 136,977	$ 52,918	$ 65,421	$ 49,797	$ 11,860	$ 965	$ 2,390	$ 569,347
Individually evaluated for impairment	-	1	-	-	-	42	3,432	103	21	-	-	3,599
Purchased credit non-impaired	-	506	250	4,846	6,657	1	14	3,322	1,497	-	138	17,231
Purchased credit impaired	-	5	-	460	320	-	-	707	-	10	-	1,502
	$ 20,358	$ 78,574	$ 17,999	$ 138,156	$ 143,954	$ 52,961	$ 68,867	$ 53,929	$ 13,378	$ 975	$ 2,528	$ 591,679

Note 4. Loans and Allowance for Loan Losses, continued

Allowance for Loan Losses, continued

The Company categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt including current financial information, historical payment experience, credit documentation, public information, and current economic trends, among other factors. The Company analyzes loans individually by classifying the loans according to credit risk. The Company uses the following general definitions for risk ratings:

Pass – These loans range from superior quality with minimal credit risk to loans requiring heightened management attention but that are still an acceptable risk and continue to perform as contracted.

Special Mention – Loans classified as special mention have a potential weakness that deserves management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or of the institution's credit position at some future date.

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

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

(dollars in thousands, except share information)

Note 4. Loans and Allowance for Loan Losses, continued

Allowance for Loan Losses, continued

The following tables summarize the risk category of loans by class of loans:

	December 31, 2022			
	Pass	**Special Mention**	**Substandard**	**Total**
Construction/development - GGL	$ 39,926	$ -	$ -	$ 39,926
Construction/development - other	69,066	5,550	-	74,616
Commercial real estate - owner occupied - GGL	30,148	-	227	30,375
Commercial real estate - owner occupied - other	185,749	-	1,347	187,096
Commercial real estate - non-owner occupied - GGL	9,117	109	-	9,226
Commercial real estate - non-owner occupied - other	245,968	-	1,371	247,339
Commercial and industrial - GGL	60,920	1,769	1,128	63,817
Commercial and industrial - other	81,726	1,060	367	83,153
1-4 family	108,323	-	77	108,400
Home equity	13,985	-	3	13,988
Construction/development - residential	16,551	-	-	16,551
Other consumer	1,627	7	1	1,635
	$ 863,106	$ 8,495	$ 4,521	$ 876,122

	December 31, 2021			
	Pass	**Special Mention**	**Substandard**	**Total**
Construction/development - GGL	$ 20,358	$ -	$ -	$ 20,358
Construction/development - other	78,573	-	1	78,574
Commercial real estate - owner occupied - GGL	15,885	2,114	-	17,999
Commercial real estate - owner occupied - other	129,700	8,456	-	138,156
Commercial real estate - non-owner occupied - other	142,418	1,536	-	143,954
Commercial and industrial - GGL	52,639	303	19	52,961
Commercial and industrial - other	66,759	1,709	399	68,867
1-4 family	53,535	106	288	53,929
Home equity	13,232	123	23	13,378
Construction/development - residential	975	-	-	975
Other consumer	2,524	-	4	2,528
	$ 576,598	$ 14,347	$ 734	$ 591,679

(dollars in thousands, except share information)

Note 4. Loans and Allowance for Loan Losses, continued

Allowance for Loan Losses, continued

The following tables summarize the past due status of loans based on contractual terms:

	December 31, 2022			December 31, 2021		
	30-59 days past due	60-89 days past due	90+ days past due	30-59 days past due	60-89 days past due	90+ days past due
Construction/development - GGL	$ -	$ -	$ -	$ 630	$ -	$ -
Construction/development - other	-	-	-	-	-	1
Commercial real estate - owner occupied - GGL	-	535	214	110	-	-
Commercial real estate - owner occupied - other	193	-	-	-	-	-
Commercial real estate - non-owner occupied - GGL						
Commercial real estate - non-owner occupied - other	-	-	-	-	-	-
Commercial and industrial - GGL	887	269	658	554	208	42
Commercial and industrial - other	-	-	367	-	-	399
1-4 family	58	-	77	51	-	125
Home equity	-	-	1	8	-	46
Construction/development - residential	-	-	-	-	-	-
Other consumer	-	2	-	-	-	1
	$ 1,138	$ 806	$ 1,317	$ 1,353	$ 208	$ 614

The following table summarizes the recorded investment in loans that are 90 days or more past due and still accruing and on nonaccrual status as of December 31, 2022 and 2021:

	December 31, 2022		December 31, 2021	
	90+ days past due and accruing	Nonaccrual	90+ days past due and accruing	Nonaccrual
Construction/development - GGL	$ -	$ -	$ -	$ -
Construction/development - other	-	-	-	1
Commercial real estate - owner occupied - GGL	-	214	-	-
Commercial real estate - owner occupied - other	-	-	-	-
Commercial real estate - non-owner occupied - GGL				
Commercial real estate - non-owner occupied - other	-	-	-	-
Commercial and industrial - GGL	301	357	-	42
Commercial and industrial - other	-	367	-	399
1-4 family	-	77	24	101
Home equity	1	-	25	21
Construction/development - residential	-	-	-	-
Other consumer	-	-	1	-
	$ 302	$ 1,015	$ 50	$ 564

(dollars in thousands, except share information)

Note 4. Loans and Allowance for Loan Losses, continued

Allowance for Loan Losses, continued

The following tables present the recorded investment and related allowance in impaired loans by loan type:

	With a recorded allowance	With no allowance recorded	Total	Unpaid Principal Balance	Related Allowance Recorded
Year ended December 31, 2022					
Home equity	$ -	$ 2	$ 2	$ 8	$ -
1-4 family	-	123	123	123	-
Commercial real estate - owner occupied - GGL	-	214	214	227	-
Commercial and industrial - other	-	367	367	367	-
Commercial and industrial - GGL	-	357	357	400	-
	$ -	$ 1,063	$ 1,063	$ 1,125	$ -
Year ended December 31, 2021					
Construction/development - other	$ -	$ 1	$ 1	$ 1	$ -
Home equity	-	21	21	29	-
1-4 family	-	103	103	103	-
Commercial and industrial - other	-	3,432	3,432	3,432	-
Commercial and industrial - GGL	-	42	42	42	-
	$ -	$ 3,599	$ 3,599	$ 3,607	$ -

The following table provides the average recorded investment in impaired loans by loan type:

	Year ended December 31,	
	2022	2021
Commercial and industrial - other	$ 1,262	$ 1,496
Commercial real estate - owner occupied - other	734	-
Commercial real estate - owner occupied - GGL	77	-
1-4 family	120	167
Construction/development - other	-	2
Home equity	18	37
Commercial and industrial - GGL	162	57
	$ 2,373	$ 1,759

There was $62 in interest income earned on one impaired loan during the year ended December 31, 2022. There was $83 in interest income earned on impaired loans during the year ended December 31, 2021.

(dollars in thousands, except share information)

Note 4. Loans and Allowance for Loan Losses, continued

Allowance for Loan Losses, continued

The Company may modify certain loans under terms that are below market in order to maximize the amount collected from a borrower that is experiencing financial difficulties. These modifications are considered to be TDRs. TDRs are evaluated individually for impairment based on the collateral value, if the loan is determined to be collateral dependent, or discounted expected cash flows, if the loan is not determined to be collateral dependent. The Company has no commitments to lend additional funds to any borrowers that have had a loan modified in a TDR.

The following table provides the number and recorded investment of TDRs outstanding at December 31, 2022 and 2021:

	December 31, 2022		December 31, 2021	
	Recorded Investment	Number	Recorded Investment	Number
1-4 family	$ 45	5	$ 264	7
Commercial real estate - owner occupied - other	-	-	3,034	2
Home equity	2	1	-	1
	$ 47	6	$ 3,298	10

As of December 31, 2022, there were no TDRs that were not performing in accordance with the modified loan terms. As of December 31, 2021, there was one non-performing TDR with a recorded investment of $8.

The Company does not generally forgive principal or unpaid interest as part of when restructuring loans. Therefore, the recorded investments in TDRs during 2022 and 2021 did not change following the modifications. There were no new TDRs in 2022.

Note 5. Premises and Equipment

A summary of premises and equipment is presented in the table below:

	December 31, 2022	December 31, 2021
Land	$ 1,564	$ 1,564
Building and leasehold improvements	15,617	14,781
Furniture and equipment	3,045	2,329
Less accumulated depreciation	(2,849)	(2,314)
	$ 17,377	$ 16,360

Depreciation on premises and equipment, which is recorded in occupancy and equipment expense, totaled $1,502 and $1,262 for the years ended December 31, 2022 and 2021, respectively.

(dollars in thousands, except share information)

Note 5. Premises and Equipment, continued

As of December 31, 2022 and 2021, buildings and leasehold improvements included $9,124 and $8,146, respectively, related to the Company's right of use lease assets.

Note 6. Leases

The following table summarizes the Company's lease assets and liabilities as of December 31, 2022 and 2021:

Description	Balance Sheet Classification	2022	2021
Assets:			
Finance	Premises and equipment, net	$ 9,124	$ 8,146
Operating	Accrued interest receivable and other assets	452	782
Total leased assets		$ 9,576	$ 8,928
Liabilities:			
Finance	Lease liability	$ 9,730	$ 8,584
Operating	Accrued interest payable and other liabilities	453	792
Total lease liabilities		$ 10,183	$ 9,376

The following table provides information regarding the minimum lease payments in future periods that will reduce lease-related liabilities outstanding as of December 31, 2022:

	Finance Leases	Operating Leases	Total
2023	$ 1,031	$ 264	$ 1,295
2024	1,069	179	1,248
2025	1,095	28	1,123
2026	1,122	-	1,122
2027	1,149	-	1,149
Thereafter	5,751	-	5,751
Total minimum lease payments	11,217	471	11,688
Discount	(1,487)	(18)	(1,505)
Lease liability	$ 9,730	$ 453	$ 10,183

(dollars in thousands, except share information)

Note 6. Leases, continued

The following table provides the weighted average remaining lease term (in years) and the weighted average discount rate of finance and operating leases as of December 31, 2022:

	Finance Leases	Operating Leases
Weighted average remaining lease term in years	10.2	1.8
Weighted average discount rate	2.60%	1.48%

Note 7. Goodwill and other intangible assets

The table below summarizes the changes in carrying amounts of goodwill and other intangible assets (core deposit intangible) for the periods presented:

	Goodwill	Other intangible assets
Balance at December 31, 2020	$ 7,016	$ 666
Accumulated amortization	-	(323)
Balance at December 31, 2021	7,016	343
Accumulated amortization	-	(217)
Balance at December 31, 2022	$ 7,016	$ 126

Goodwill represents the excess of the purchase price over the fair value of acquired net assets under the acquisition method of accounting. The acquisition that generated the Company's goodwill was a nontaxable event and, as a result, there is no tax basis in the goodwill, and none of the goodwill is deductible for tax purposes.

Goodwill is evaluated for impairment annually or more frequently if events occur or circumstances change that may indicate that impairment exists. The most recent goodwill impairment evaluation was performed as of December 31, 2022. No goodwill impairment was recorded during 2022 or 2021.

The value of other intangible assets was determined using the present value of the difference between a market participant's cost of obtaining alternative funds and the cost to maintain the acquired deposit base. The other intangible assets are amortized over a seven-year period using an accelerated method. Other intangible assets are evaluated for impairment if events and circumstances indicate impairment may exist.

The following table presents estimated future amortization expense for the Company's other intangible assets:

2023	$ 111
2024	15
2025	-
2026	-
2027	-
Thereafter	-
	$ 126

(dollars in thousands, except share information)

Note 7. Goodwill and other intangible assets, continued

No impairment charges were recorded for other intangible assets during 2022 or 2021.

SBA servicing assets, which are included in other assets, represent the present value of projected future servicing income when an SBA loan is sold servicing retained. The SBA servicing asset was $4,143, net of $975 valuation allowance, at December 31, 2022, and $2,390, net of $177 valuation allowance at December 31, 2021. The SBA servicing asset is amortized over the servicing life of the loan and is subject to impairment based on changes in servicing values.

Note 8. Income Taxes

The significant components of the provision for income taxes for the years ended December 31, 2022 and 2021 are as follows:

	2022	2021
Current tax provision:		
Federal	$ 3,456	$ (23)
State	380	-
Total current tax expense (benefit)	3,836	(23)
Deferred tax provision:		
Federal	(710)	(616)
State	(69)	(78)
Total deferred tax benefit	(779)	(694)
Total income tax expense (benefit)	$ 3,057	$ (717)

The difference between the provision for income taxes and the amounts computed by applying the statutory federal income tax rate of 21 percent for 2022 and 2021 to income before income taxes is summarized below:

	2022	2021
Income tax expense at federal statutory rate	$ 2,867	$ 772
Increase (decrease) resulting from:		
State income taxes, net of federal benefit	259	(62)
Bank-owned life insurance	(146)	(122)
Stock-based compensation	-	(1,347)
Nondeductible expenses	99	80
Other permanent difference, net	(13)	(38)
Other	(9)	-
Total income tax expense (benefit)	$ 3,057	$ (717)

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes.

(dollars in thousands, except share information)

Note 8. Income Taxes, continued

Significant components of deferred taxes at December 31, 2022 and 2021 are as follows:

	2022	2021
Deferred tax asset relating to:		
Allowance for loan losses	$ 2,023	$ 1,522
Deferred compensation	352	270
Net operating loss carryforwards	-	282
Stock-based compensation	463	254
Unrealized loss on investment securities available for sale	1,609	197
Amortization of intangible assets	125	139
Other	25	-
Total deferred tax assets	4,597	2,664
Deferred tax liabilities relating to:		
Premises and equipment	(836)	(934)
Acquisition accounting	(40)	(30)
Other	-	(170)
Total deferred tax liabilities	(876)	(1,134)
Total deferred tax asset, net	$ 3,721	$ 1,530

As of December 31, 2022, the Company has no remaining post-2017 net operating losses. On March 27, 2020, the Coronavirus Aid, Relief, and Economic Security Act (CARES Act) was enacted in response to the COVID-19 pandemic. The CARES Act, among other things, permits carryovers and carrybacks to offset 100 percent of taxable income for taxable years beginning before 2021. In addition, the CARES Act allows net operating losses incurred in 2020, 2019 and 2018 to be carried back to each of the five preceding taxable years to generate a refund of previously paid income taxes. The Company utilized this provision in the CARES Act by carrying back the 2019 net operating loss to tax years 2018, 2017 and 2016, generating a benefit through the ability to carry back to higher tax rate years.

The Company's net deferred tax asset was $3,721 and $1,530 at December 31, 2022 and 2021, respectively. In evaluating whether it will realize the full benefit of the net deferred tax asset, the Company evaluated both positive and negative evidence, including among other things recent earnings trends, projected earnings, and asset quality. As of December 31, 2022, the deferred tax asset was primarily the result of unrealized losses on investment securities available for sale. A valuation allowance of $9 was recorded at December 31, 2022 to recognize only the portion of the deferred tax asset that is more likely than not to be realized.

(dollars in thousands, except share information)

Note 8. Income Taxes, continued

Significant negative trends in credit quality, losses from operations or other factors could impact the realization of the deferred tax asset in the future.

The Company's policy is to report interest and penalties, if any, related to uncertain tax positions in income tax expense. As of December 31, 2022 and 2021, the Company had no uncertain tax positions.

With few exceptions, the Company is no longer subject to U.S. federal, state and local, or non-U.S. income tax examinations by tax authorities for years before 2018.

Note 9. Deposits

The scheduled maturities of time deposits as of December 31, 2022 are presented below:

	Less than $250	$250 and Greater	Total
2023	$ 107,718	$ 16,535	$ 124,253
2024	13,474	656	14,130
2025	4,839	-	4,839
2026	260	-	260
2027	7,863	-	7,863
Total	$ 134,154	$ 17,191	$ 151,345

Brokered deposits totaled $74,218 and $36,019 as of December 31, 2022 and 2021, respectively. Time deposits, excluding brokered deposits, in excess of the FDIC insurance limit of $250 totaled $17,191 and $10,080 as of December 31, 2022 and 2021, respectively.

Note 10. FHLB Advances

A summary of FHLB advances as of December 31, 2022 and 2021 is presented below:

Description	Interest Rate	Maturity Date	2022	2021
Fixed Rate Hybrid	1.65%	January 31, 2022	$ -	$ 4,000
Daily Rate Credit	4.57%	June 30, 2023	60,000	-
			$ 60,000	$ 4,000

As of December 31, 2022, the Company had access to an additional $120,353 at the FHLB on a secured basis. As of December 31, 2022, the Company also had unused unsecured federal funds lines of credit with various counterparty banks totaling $80,000.

(dollars in thousands, except share information)

Note 11. Commitments and Contingencies

The Company is a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. Those instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the balance sheet. The contract or notional amounts of those instruments reflect the Company's maximum exposure. The Company uses the same credit policies in making commitments and conditional obligations as it does for on-balance sheet instruments.

Commitments to extend credit, which totaled $215,873 and $147,381 at December 31, 2022 and 2021, respectively, represent agreements to lend to a customer as long as there is no violation of conditions established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. As of December 31, 2022 and 2021, the Company had a reserve for unfunded commitments of $162 and $135, respectively, included in accrued interest payable and other liabilities on the Balance Sheet.

Since some of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Company evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Company, upon extension of credit is based on a credit evaluation of the borrower. Collateral obtained varies but may include real estate, equipment, stocks, bonds, and certificates of deposit.

Note 12. Stock-Based Compensation and Retirement Plans

Restricted Stock

The Company's 2019 Omnibus Incentive Plan authorizes up to 1,205,346 shares of the Company's voting common stock to be awarded under various incentive programs. Pursuant to authority under the 2019 Omnibus Incentive Plan, the Company adopted a restricted stock program that allows shares of stock to be awarded to employees. All shares vest over a five-year period.

In 2021, the Company accelerated the vesting of 801,490 shares of restricted stock previously granted to certain executive officers. The accelerated vesting of these shares resulted in a one-time, non-cash charge of $5,242 to stock-based compensation expense in 2021.

The following table provides information on the number of shares of restricted stock awarded in each of the years ended December 31, 2022 and 2021, the aggregate number of shares awarded as of December 31, 2022 and 2021, the restricted stock expense recorded during the years ended December 31, 2022 and 2021, and the unrecognized compensation cost for non-vested restricted stock awards as of December 31, 2022 and 2021:

	2022	2021
Shares of restricted stock awarded during current year	58,500	117,500
Shares of restricted stock awarded as of December 31	1,173,490	1,114,990
Restricted stock expense recognized in current year	$ 1,021	$ 7,274
Unrecognized compensation cost related to non-vested restricted stock awards as of December 31	2,025	2,088

Note 12. Stock-Based Compensation and Retirement Plans, continued

Defined Contribution Plans

The Company sponsors a 401(k) plan for substantially all employees. Participants may make voluntary contributions resulting in salary deferrals in accordance with Section 401(k) of the Internal Revenue Code. The plan provides for employer contributions of up to 4 percent of pre-tax salary contributed by each participant. Employer contributions to the 401(k) plans totaled $459 for the year ended December 31, 2022, compared to $385 for 2021.

Supplemental Executive Retirement Plans

As of December 31, 2022 and 2021, the Company had a $1,531 and $1,174 accrued liability related to retirement plans, respectively, included in accrued interest payable and other liabilities on the Balance Sheet. The Company had $907 in accrued liability as of both December 31, 2022 and 2021 related to obligations to two former employees, representing the present value of the future payments expected to be made pursuant to the terms of a non-qualified plan.

Additionally, in 2021 the Company implemented a long-term retention agreement with three current executives and has accrued an additional $357 and $267 as of December 31, 2022 and 2021, respectively, in accrued liability related to the present value of the future payments expected to be made to these executives under the new agreement. The Long-term retention agreements provide for specified cash retention payment amounts for 10 years generally commencing on the date that the Executive attains age 62 provided that the Executive remains employed by the Company.

Note 13. Shareholders' Equity

During the first quarter of 2021, the Company repurchased 75,000 common stock warrants at $2.28 per share, resulting in $170 decrease in capital surplus.

During the first quarter of 2021, the Company completed a secondary offering of its voting common stock in a private placement. The Company issued a total of 2,326,839 shares at an offering price of $12 per share, resulting in an additional $27,820 of new capital.

During the first quarter of 2022, the Company completed a secondary offering of its voting common stock in a private placement. The Company issued a total of 664,316 shares at an offering price of $18 per share, resulting in an additional $11,944 of new capital.

During the first quarter of 2023, the Company completed a secondary offering of its voting common stock in a private placement. The Company issued a total of 814,333 shares at an offering price of $20 per share, resulting in an additional $16,287 of new capital.

Note 14. Fair Value

Fair value of financial instruments:

Fair value 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 no quoted market prices for the Company's various financial instruments. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. Fair value estimates may not be realized in an immediate settlement, and the aggregate fair value amounts presented may not necessarily represent the underlying fair value of the Company.

Cash and cash equivalents:

The carrying amount reported in the balance sheets for cash and cash equivalents approximates fair value. The fair value of cash and cash equivalents is measured using level 1 inputs.

Investment securities available for sale:

Fair values are determined in the manner described above. The fair value of investment securities available for sale is measured using level 2 inputs.

Investment securities held to maturity:

Fair values are determined in the manner described above. The fair value of investment securities held to maturity is measured using level 2 inputs.

Marketable equity securities:

Fair values are based upon quoted market prices. The fair value of investment securities available for sale is measured using level 1 inputs.

Loans held for sale:

Fair values of SBA loans held for sale are based on estimated instrument-level gains or losses to be realized upon sale, which management consider to be level 2 inputs.

PPP loans:

The carrying value of PPP loans approximates fair value. Management believes the Company will be able to fully collect the outstanding balance of these loans.

Note 14. Fair Value, continued

Loans, excluding PPP loans, net:

The fair value of loans represents the amount at which the loans of the Company could be exchanged on the open market, based upon the current lending rate for similar types of lending arrangements discounted over the remaining life of the loans. For fixed rate loans and for variable rate loans with infrequent re-pricing or re-pricing limits, fair value is based on discounted cash flows using current market rates applied to the cash flow analysis. The fair value of non-impaired loans is measured using level 2 inputs. The fair value of impaired loans relies on level 3 inputs.

Deposits:

The fair value of time deposits is based on discounted cash flows using current market rates applied to the cash flow analysis for each time deposit. Other non-maturity deposits are reported at their carrying values. The fair value of deposits is measured using level 2 inputs.

Short-term borrowings:

Fair values of short-term borrowings are estimated using discounted cash flow analyses based on the Company's current incremental borrowing rates for similar types of borrowing arrangements. Estimated maturity dates are also included in the calculation of fair value for these borrowings. The fair value of short-term borrowings is measured using level 2 inputs.

Off-balance sheet instruments:

Off-balance sheet instruments include commitments to extend credit, standby letters of credit, and financial guarantees. Because of the uncertainty involved in attempting to assess the likelihood and timing of commitments being drawn upon, coupled with the lack of an established market and the wide diversity of fee structures, the Company does not believe it is meaningful to provide an estimate of fair value for these instruments.

(dollars in thousands, except share information)

Note 14. Fair Value, continued

The carrying amounts and fair values of the Company's financial instruments at December 31, 2022 and 2021 were as follows:

		Fair Value			
	December 31, 2022				
	Carrying Value	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs	Total
Total cash and cash equivalents	$ 39,883	$ 39,883	$ -	$ -	$ 39,883
Investment securities available for sale	41,043	-	41,043	-	41,043
Investment securities held to maturity	81,512	-	69,500	-	69,500
Marketable equity securities	252	252	-	-	252
Loans held for sale	11,545	-	11,545	-	11,545
PPP loans	6,656	-	6,656	-	6,656
Loans, excluding PPP loans, net	867,394	-	809,371	1,063	810,434
Deposits	903,916	-	901,435	-	901,435
FHLB advances	60,000	-	60,000	-	60,000

	December 31, 2021				
	Carrying Value	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs	Total
Total cash and cash equivalents	$ 95,107	$ 95,107	$ -	$ -	$ 95,107
Investment securities available for sale	68,821	-	68,821	-	68,821
Investment securities held to maturity	42,449	-	42,063	-	42,063
Marketable equity securities	243	243	-	-	243
Loans held for sale	9,330	-	9,330	-	9,330
PPP loans	61,327	-	61,327	-	61,327
Loans, excluding PPP loans, net	585,054	-	591,545	3,599	595,144
Deposits	787,714	-	787,520	-	787,520
FHLB advances	4,000	-	4,000	-	4,000

Recurring – Investment Securities Available for Sale:

Investment securities available for sale are reported at fair value utilizing measurements from independent third-party sources, which are level 2 inputs. The fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, live trading levels, trade execution data, market consensus prepayment speeds, credit information, and the bond's terms and conditions, among other inputs.

(dollars in thousands, except share information)

Note 14. Fair Value, continued

Recurring – loans held for sale:

Loans held for sale are reported at fair value utilizing projected sale price guidance, which is a level 2 input. The fair value measurements consider observable data that may include dealer quotes, market spreads, live trading levels, trade execution data, among other inputs.

The following tables summarize the Company's financial instruments measured at fair value on a recurring basis as of December 31, 2022 and December 31, 2021, segregated by the level of the valuation inputs within the fair value hierarchy.

	December 31, 2022			
	Level 1	**Level 2**	**Level 3**	**Total**
Agency mortgage-backed	$ -	$ 17,210	$ -	$ 17,210
Agency CMO/REMIC	-	1,870	-	1,870
Corporate bonds	-	13,576	-	13,576
US Treasury securities	-	5,247	-	5,247
Commercial mortgage-backed	-	3,140	-	3,140
Marketable equity security	252	-	-	252
Loans held for sale	-	11,545	-	11,545

	December 31, 2021			
	Level 1	**Level 2**	**Level 3**	**Total**
Agency mortgage-backed	$ -	$ 35,528	$ -	$ 35,528
Agency CMO/REMIC	-	10,322	-	10,322
Corporate bonds	-	11,036	-	11,036
US Treasury securities	-	5,928	-	5,928
Commercial mortgage-backed	-	4,023	-	4,023
US Government Agency securities	-	1,984	-	1,984
Marketable equity security	243	-	-	243
Loans held for sale	-	9,330	-	9,330

Non recurring – impaired loans:

The Company does not record loans at fair value on a recurring basis. However, from time to time, a loan is considered impaired when management concludes that payment of principal and interest will not be made in accordance with the contractual terms of the loan agreement. Once a loan is identified as individually impaired, management measures impairment using one of several methods, including appraised collateral value and /or tax assessed value, liquidation value and discounted expected cash flow. Those impaired loans not requiring an allowance represent loans for which the fair value of the expected repayments or collateral exceed the recorded investments in such loans. For real estate collateral, the Company frequently obtains appraisals prepared by external professional appraisers and applies of 10 percent depending on various factors including the type of property, condition and location. . For equipment and other collateral, a discount of up to the advance rate as defined by the policy.

(dollars in thousands, except share information)

Note 14. Fair Value, continued

Non recurring – impaired loans, continued:

In certain instances, the Company prepares internally generated valuations from on-site inspections, third-party valuation models or other information. Due to the significance of the unobservable market inputs and assumptions, as well as the absence of a liquid secondary market for most loans, these loans are classified as Level 3. No impaired loans were recorded at fair value as of December 31, 2022 or 2021. The Company had a recorded investment in impaired loans of $1,063 and $3,599 as of December 31, 2022 and 2021, respectively.

Note 15. Regulatory Capital Requirements

The Company is required to maintain reserve and clearing balances with the Federal Reserve Bank in the form of vault cash or deposits.

Banking regulators have established various ratios to monitor capital adequacy. Failure to comply with these capital adequacy requirements may affect various bank activities including the ability to undertake new business initiatives such as acquisitions and branch expansion, access to funding and cost of new business initiatives, the ability to pay dividends, the ability to repurchase shares or other capital instruments, the cost of deposit insurance, and the level of regulatory oversight.

Based on current regulatory guidance, banks are required to maintain a common equity tier 1 ratio of 4.50 percent, a tier 1 leverage ratio of 4.00 percent, a tier 1 risk-based capital ratio of 6.00 percent and a total risk-based capital ratio of 8.00 percent. Current regulations also require creation and maintenance of a capital conservation buffer in addition to the regulatory minimum capital requirements. The capital conservation buffer was phased in over four years beginning January 1, 2016, at 0.625 percent of risk-weighted assets. After increasing each subsequent year by an additional 0.625 percent, at January 1, 2018, the capital conservation buffer was 1.875 percent, and, as fully phased in on January 1, 2019, the capital conservation buffer is 2.50 percent.

As of December 31, 2022, and 2021, the Company exceeded all applicable capital adequacy requirements.

	2022					
	Actual		Minimum to be adequately capitalized		Minimum to be well capitalized	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
Common equity tier 1	$ 133,475	14.20%	$ 42,309	4.50%	$ 61,112	6.50%
Tier 1 leverage	133,475	12.45%	42,879	4.00%	53,599	5.00%
Tier 1 risk-based capital	133,475	14.20%	56,411	6.00%	75,215	8.00%
Total risk-based capital	142,366	15.14%	75,215	8.00%	94,019	10.00%

(dollars in thousands, except share information)

Note 15. Regulatory Capital Requirements, continued

	2021					
	Actual		Minimum to be adequately capitalized		Minimum to be well capitalized	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
Common equity tier 1	$ 110,347	16.68%	$ 29,272	4.50%	$ 43,003	6.50%
Tier 1 leverage	110,347	12.39%	35,622	4.00%	44,527	5.00%
Tier 1 risk-based capital	110,347	16.68%	39,696	6.00%	52,927	8.00%
Total risk-based capital	117,107	17.70%	52,927	8.00%	66,159	10.00%

Note 16. Subsequent Events

Subsequent events are events or transactions that occur after the balance sheet date but before financial statements are issued. Recognized subsequent events are events or transactions that provide additional evidence about conditions that existed at the date of the balance sheet, including the estimates inherent in the process of preparing financial statements. Non-recognized subsequent events are events that provide evidence about conditions that did not exist at the date of the balance sheet but arose after that date.

Between March 10, 2023 and March 12, 2023, two financial institutions unrelated to the Company experienced a significant run on deposits, leading to insolvency. These institutions failed and were placed into receivership by the FDIC. These institutions also had deposit concentrations related to higher-risk customer types, such as venture capital and cryptocurrency. The Federal Reserve determined that these institutions were a systemic risk and therefore, in concert with the FDIC, have determined that all deposits held by these two institutions will be insured. These events have created market volatility for the financial sector; however, the ongoing ramifications of these events have yet to be seen. These events have not caused any significant changes in deposit balances at Dogwood State Bank.

Management has reviewed the events occurring through March 30, 2023, the date the financial statements were issued. Except as noted in Note 13, no additional subsequent events occurred requiring accrual or disclosure.