

REFINITIV

DELTA REPORT

10-Q

FXNC - FIRST NATIONAL CORP /VA/

10-Q - MARCH 31, 2024 COMPARED TO 10-Q - SEPTEMBER 30, 2023

The following comparison report has been automatically generated

TOTAL DELTAS 1607

■ CHANGES	311
■ DELETIONS	843
■ ADDITIONS	453

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549**

FORM 10-Q

- QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended **September 30, 2023** **March 31, 2024**

or

- TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _____ to _____

Commission File Number: 1-38874



(Exact name of registrant as specified in its charter)

Virginia

54-1232965

(State or other jurisdiction of
incorporation or organization)

(I.R.S. Employer
Identification No.)

112 West King Street, Strasburg, Virginia
(Address of principal executive offices)

22657
(Zip Code)

(540) 465-9121

(Registrant's telephone number, including area code)

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

Title of each class

Common stock, par value \$1.25 per share

Trading symbol(s)

FXNC

Name of each exchange on which registered

The Nasdaq Stock Market LLC

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

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

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

Large accelerated filer	<input type="checkbox"/>	Accelerated filer	<input type="checkbox"/>
Non-accelerated filer	<input checked="" type="checkbox"/>	Smaller reporting company	<input checked="" type="checkbox"/>
		Emerging growth company	<input type="checkbox"/>

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

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date. As of November 3, 2023 May 3, 2024, 6,260,934 6,277,373 shares of common stock, par par value \$1.25 per share, of the registrant were outstanding.

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PART I – FINANCIAL INFORMATION

Item 1. Financial Statements

FIRST NATIONAL CORPORATION

Consolidated Balance Sheets

(in thousands, except share and per share data)

	(unaudited)		(unaudited)	
	September 30, 2023	December 31, 2022*	March 31, 2024	December 31, 2023*
Assets				
Cash and due from banks	\$ 17,168	\$ 20,784	\$ 14,476	\$ 17,194
Interest-bearing deposits in banks	32,931	46,130	124,233	69,967
Securities available for sale, at fair value	148,175	162,907	147,675	152,857
Securities held to maturity, at amortized cost (net of allowance for credit losses of \$131 at September 30, 2023)	149,948	153,158		
Securities held to maturity, at amortized cost (net of allowance for credit losses of \$116 at March 31, 2024)			125,825	148,244
Restricted securities, at cost	2,077	1,908	2,112	2,078
Loans, net of allowance for credit losses, 2023, \$8,896; 2022, \$7,446	943,603	913,077		
Other real estate owned, net of valuation allowance	—	184		
Loans, net of allowance for credit losses, 2024, \$12,603; 2023, \$11,974			960,371	957,456
Premises and equipment, net	21,363	21,876	21,993	22,142
Accrued interest receivable	4,502	4,543	4,978	4,655
Bank owned life insurance	24,734	24,531	24,652	24,902
Goodwill	3,030	3,030	3,030	3,030
Core deposit intangibles, net	122	136	113	117
Other assets	18,567	17,119	17,737	16,653
Total assets	\$ 1,366,220	\$ 1,369,383	\$ 1,447,195	\$ 1,419,295
Liabilities and Shareholders' Equity				
Liabilities				
Deposits:				
Noninterest-bearing demand deposits	\$ 403,774	\$ 427,344	\$ 384,092	\$ 379,208
Savings and interest-bearing demand deposits	646,980	677,139	677,458	662,169

Time deposits	184,419	136,849	197,587	192,349
Total deposits	\$ 1,235,173	\$ 1,241,332	\$ 1,259,137	\$ 1,233,726
Other borrowings			50,000	50,000
Subordinated debt, net of issuance cost	4,997	4,995	4,998	4,997
Junior subordinated debt	9,279	9,279	9,279	9,279
Accrued interest payable and other liabilities	4,792	5,417	5,965	5,022
Total liabilities	\$ 1,254,241	\$ 1,261,023	\$ 1,329,379	\$ 1,303,024
Commitments and contingencies				
Shareholders' Equity				
Preferred stock, par value \$1.25 per share; authorized 1,000,000 shares; none issued and outstanding	\$ —	\$ —	\$ —	\$ —
Common stock, par value \$1.25 per share; authorized 8,000,000 shares; issued and outstanding, 2023, 6,260,934 shares; 2022, 6,264,912 shares	7,826	7,831		
Common stock, par value \$1.25 per share; authorized 8,000,000 shares; issued and outstanding, 2024, 6,277,373 shares; 2023, 6,263,102 shares			7,847	7,829
Surplus	32,840	32,716	33,021	32,950
Retained earnings	95,988	90,284	96,465	94,198
Accumulated other comprehensive loss, net	(24,675)	(22,471)	(19,517)	(18,706)
Total shareholders' equity	\$ 111,979	\$ 108,360	\$ 117,816	\$ 116,271
Total liabilities and shareholders' equity	\$ 1,366,220	\$ 1,369,383	\$ 1,447,195	\$ 1,419,295

*Derived from audited consolidated financial statements.

See Notes to Consolidated Financial Statements

FIRST NATIONAL CORPORATION

Consolidated Statements of Income (Unaudited)
(in thousands, except per share data)

	Three Months Ended				Nine Months Ended		Three Months Ended	
	September 30,		September 30,		September 30,	September 30,	March 31,	March 31,
	2023	2022	2023	2022	2023	2022	2024	2023
Interest and Dividend Income								
Interest and fees on loans	\$ 12,640	\$ 10,759	\$ 36,038	\$ 30,218	\$ 13,484	\$ 11,512		
Interest on deposits in banks	338	380	1,441	701	1,288	344		
Interest and dividends on securities:								
Taxable interest	1,323	1,323	3,968	3,750	1,224	1,339		
Tax-exempt interest	304	307	917	921	305	306		
Dividends	26	23	81	65	33	27		
Total interest and dividend income	\$ 14,631	\$ 12,792	\$ 42,445	\$ 35,655	\$ 16,334	\$ 13,528		
Interest Expense								
Interest on deposits	\$ 3,810	\$ 927	\$ 9,428	\$ 1,680	\$ 4,771	\$ 2,216		
Interest on subordinated debt	69	70	207	208	69	69		
Interest on junior subordinated debt	69	68	203	202	68	67		
Interest on other borrowings	—	—	3	—	576	—		
Total interest expense	\$ 3,948	\$ 1,065	\$ 9,841	\$ 2,090	\$ 5,484	\$ 2,352		
Net interest income	\$ 10,683	\$ 11,727	\$ 32,604	\$ 33,565	\$ 10,850	\$ 11,176		

	100	200	200	600	1,000	—
	\$ 10,583	\$ 11,527	\$ 32,404	\$ 32,965	\$ 9,850	\$ 11,176
Provision for credit losses						
Net interest income after provision for credit losses						
Noninterest Income						
Service charges on deposit accounts	\$ 733	\$ 708	\$ 2,062	\$ 2,015	\$ 654	\$ 646
ATM and check card fees	976	915	2,624	2,462	770	800
Wealth management fees	811	739	2,336	2,302	883	776
Fees for other customer services	122	180	538	601	195	196
Brokered mortgage fees	38	72	73	224	38	—
Income from bank owned life insurance	175	166	459	441	151	149
Other operating income	198	247	623	473	1,356	211
Total noninterest income	\$ 3,053	\$ 3,027	\$ 8,715	\$ 8,518	\$ 4,047	\$ 2,778
Noninterest Expense						
Salaries and employee benefits	\$ 5,505	\$ 5,174	\$ 16,040	\$ 15,384	\$ 5,871	\$ 5,346
Occupancy	534	539	1,586	1,656	535	528
Equipment	598	546	1,756	1,725	591	587
Marketing	204	211	720	585	195	268
Supplies	128	117	423	384	116	148
Legal and professional fees	439	361	1,204	1,075	452	343
ATM and check card expense	440	332	1,265	982	361	400
FDIC assessment	161	109	479	393	177	106
Bank franchise tax	262	238	778	692	262	254
Data processing expense	266	243	720	700	246	202
Amortization expense	5	6	14	15	4	5
Other real estate owned (income) expense, net	15	14	(201)	83		
Other real estate owned expense, net					—	3
Net losses on disposal of premises and equipment					49	—
Other operating expense	1,227	1,193	3,358	2,971	1,028	1,010
Total noninterest expense	\$ 9,784	\$ 9,083	\$ 28,142	\$ 26,645	\$ 9,887	\$ 9,200

See Notes to Consolidated Financial Statements

FIRST NATIONAL CORPORATION

Consolidated Statements of Income (Unaudited)

(Continued)

(in thousands, except per share data)

	Three Months Ended		Nine Months Ended		Three Months Ended	
	September 30,	September 30,	September 30,	September 30,	March	March
					31,	31,
	2023	2022	2023	2022	2024	2023
Income before income taxes	\$ 3,852	\$ 5,471	\$ 12,977	\$ 14,838	\$ 4,010	\$ 4,754
Income tax expense	731	1,017	2,502	2,820	801	905
Net income	\$ 3,121	\$ 4,454	\$ 10,475	\$ 12,018	\$ 3,209	\$ 3,849
Earnings per common share						
Basic	\$ 0.50	\$ 0.71	\$ 1.67	\$ 1.92	\$ 0.51	\$ 0.61
Diluted	\$ 0.50	\$ 0.71	\$ 1.67	\$ 1.92	\$ 0.51	\$ 0.61

See Notes to Consolidated Financial Statements

FIRST NATIONAL CORPORATION

Consolidated Statements of Comprehensive Income (Loss) (Unaudited)

(in thousands)

	Three Months Ended		Nine Months Ended	
	September 30, 2023	September 30, 2022	September 30, 2023	September 30, 2022
	\$	\$	\$	\$
Net income	3,121	4,454	10,475	12,018
Other comprehensive income (loss), net of tax,				
Unrealized holding (losses) gains on available for sale securities, net of tax (\$1,080) and \$155 for the three months and (\$925) and (\$6,225) for the nine months ended September 30, 2023 and 2022, respectively	(4,063)	581	(3,480)	(23,424)
Unrealized holding losses on securities transferred from available for sale to held to maturity, net of tax (\$1,605) for the three months and nine months ended September 31, 2022	—	(6,036)	—	(6,036)
Amortization of unrealized holding losses on available-for-sale securities transferred to held to maturity, net of tax of \$86 and \$0 for the three months and \$258 and \$0 for the nine months ended September 30, 2023 and 2022, respectively	323	—	972	—
Change in fair value of cash flow hedges, net of tax \$113 and \$106 for the three months and \$82 and \$373 for the nine months ended September 30, 2023 and 2022, respectively	424	404	304	1,409
Total other comprehensive (loss)	(3,316)	(5,051)	(2,204)	(28,051)
Total comprehensive (loss) income	<u><u>\$ (195)</u></u>	<u><u>\$ (597)</u></u>	<u><u>\$ 8,271</u></u>	<u><u>\$ (16,033)</u></u>

	Three Months Ended	
	March 31, 2024	March 31, 2023
	\$	\$
Net income	3,209	3,849
Other comprehensive (loss) income, net of tax,		
Unrealized holding gains (losses) on available for sale securities, net of tax of (\$332) and \$576 for the three months ended March 31, 2024 and 2023, respectively	(1,246)	2,162
Amortization of unrealized holding losses on available-for-sale securities transferred to held to maturity, net of tax of \$77 and \$84 for the three months ended March 31, 2024 and 2023, respectively	290	316
Change in fair value of cash flow hedges, net of tax \$39 and (\$60) for the three months ended March 31, 2024 and 2023, respectively	145	(223)
Total other comprehensive (loss) income	(811)	2,255
Total comprehensive income	<u><u>\$ 2,398</u></u>	<u><u>\$ 6,104</u></u>

See Notes to Consolidated Financial Statements

FIRST NATIONAL CORPORATION

Consolidated Statements of Cash Flows (Unaudited)

(in thousands)

	Nine Months Ended		Three Months Ended	
	September 30,		March 31,	
	2023	2022	2024	2023
Cash Flows from Operating Activities				
Net income	\$ 10,475	\$ 12,018	\$ 3,209	\$ 3,849
Adjustments to reconcile net income to net cash provided by operating activities:				
Depreciation and amortization of premises and equipment	1,195	1,118	404	398
Amortization of core deposit intangibles	14	14	4	5
Amortization of debt issuance costs	2	2	1	1
Provision for credit losses on loans	166	600	991	—
(Recovery) of credit losses on securities held to maturity	(2)	—	—	—
Provision for credit losses on unfunded commitments	36	—	—	—
Net (gain) loss on sale of other real estate owned	(233)	33	—	—
Provision for credit losses on securities held to maturity			9	—
Increase in cash value of bank owned life insurance	(459)	(441)	(151)	(149)
Accretion of discounts and amortization of premiums on securities, net	746	891	223	249
Accretion of premium on time deposits	(68)	(159)	(17)	(25)
Accretion of certain acquisition-related loan discounts, net	(510)	(1,013)	(98)	(145)
Stock-based compensation	681	728	142	338
Excess tax benefits on stock-based compensation	4	3	1	4
(Gain) loss on disposal of premises and equipment, net	(3)	4	—	—
Loss (gain) on disposal of premises and equipment, net			50	(2)
Deferred income tax expense	323	46	46	325
Changes in assets and liabilities:				
Decrease (increase) in interest receivable	41	(344)	—	—
(Increase) decrease in interest receivable			(323)	154
(Increase) decrease in other assets	(284)	3,513	(731)	400
(Decrease) in accrued interest payable and other liabilities	(814)	(176)	—	—
Increase (decrease) in accrued interest payable and other liabilities			943	(849)
Net cash provided by operating activities	\$ 11,310	\$ 16,837	\$ 4,703	\$ 4,553
Cash Flows from Investing Activities				
Proceeds from maturities, calls, and principal payments of securities available for sale	\$ 9,623	\$ 21,556	\$ 3,389	\$ 3,056
Proceeds from maturities, calls, and principal payments of securities held to maturity	6,359	7,086	22,769	2,109
Purchases of securities available for sale	—	(21,147)	—	—
Purchases of restricted securities	(274)	—	—	—
Purchases of securities held to maturity	(2,092)	(54,038)	—	—
Net redemption (purchase) of restricted securities	105	(95)	—	—
Net (purchase) redemption of restricted securities			(34)	105
Purchase of premises and equipment	(682)	(596)	(305)	(159)
Proceeds from sale of premises and equipment	3	—	—	2
Proceeds from sale of other real estate owned	417	421	—	—
Proceeds from cash value of bank owned life insurance	256	360	401	256
Net (increase) in loans	(32,368)	(80,401)	—	—
Net cash (used in) investing activities	\$ (18,653)	\$ (126,854)	—	—
Net (increase) decrease in loans			(3,808)	1,786
Net cash provided by investing activities			\$ 22,412	\$ 7,155

See Notes to Consolidated Financial Statements

FIRST NATIONAL CORPORATION

Consolidated Statements of Cash Flows (Unaudited)
 (Continued)
 (in thousands)

	Nine Months Ended		Three Months Ended	
	September 30, 2023	September 30, 2022	March 31, 2024	March 31, 2023
Cash Flows from Financing Activities				
Net (decrease) increase in demand deposits and savings accounts	\$ (53,729)	\$ 29,090		
Net increase (decrease) in time deposits	47,638	(11,637)		
Repayment of subordinated debt	—	(5,000)		
Net increase (decrease) in demand deposits and savings accounts			\$ 20,173	\$ (17,589)
Net increase in time deposits			5,255	17,807
Cash dividends paid on common stock, net of reinvestment	(2,699)	(2,474)	(900)	(901)
Repurchase of common stock, stock incentive plan	(114)	(183)	(95)	(113)
Repurchase of common stock, stock repurchase plan	(568)	—	—	(25)
Net cash (used in) provided by financing activities	\$ (9,472)	\$ 9,796		
Decrease in cash and cash equivalents	\$ (16,815)	\$ (100,221)		
Net cash provided by (used in) financing activities			\$ 24,433	\$ (821)
Increase in cash and cash equivalents			\$ 51,548	\$ 10,887
Cash and Cash Equivalents				
Beginning	\$ 66,914	\$ 176,006	\$ 87,161	\$ 66,914
Ending	\$ 50,099	\$ 75,785	\$ 138,709	\$ 77,801
Supplemental Disclosures of Cash Flow Information				
Cash payments for:				
Interest	\$ 9,405	\$ 2,285	\$ 5,369	\$ 2,186
Income taxes	\$ 2,726	\$ 2,265		
Supplemental Disclosures of Noncash Investing and Financing Activities				
Unrealized losses on securities available for sale	\$ (4,405)	\$ (29,649)		
Unrealized losses on securities transferred from available for sale to held to maturity	\$ —	\$ (7,641)		
Fair value of securities transferred from available for sale to held to maturity	\$ —	\$ 74,416		
Unrealized (gains) losses on securities available for sale			\$ (1,578)	\$ 2,738
Change in fair value of cash flow hedges	\$ 386	\$ 1,782	\$ 184	\$ (283)
Transfer from premises and equipment to other real estate owned, net	\$ —	\$ (184)		
Issuance of common stock, dividend reinvestment plan	\$ 120	\$ 152	\$ 42	\$ 41

See Notes to Consolidated Financial Statements

FIRST NATIONAL CORPORATION

Consolidated Statements of Changes in Shareholders' Equity (Unaudited)
 (in thousands, except share and per share data)

	Common Stock	Surplus	Retained Earnings	Accumulated Other Comprehensive (Loss)	Total
Balance, June 30, 2022	\$ 7,815	\$ 32,398	\$ 82,804	\$ (22,702)	\$ 100,315
Net income	—	—	4,454	—	4,454
Other comprehensive loss	—	—	—	(5,051)	(5,051)

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Cash dividends on common stock (\$0.14 per share)	—	—	(876)	—	(876)
Stock-based compensation	—	187	—	—	187
Issuance of 2,733 shares common stock, dividend reinvestment plan	4	44	—	—	48
Issuance of 7,500 shares common stock, stock incentive plan	9	(9)	—	—	—
Balance, September 30, 2022	\$ 7,828	\$ 32,620	\$ 86,382	\$ (27,753)	\$ 99,077

	Common Stock	Surplus	Retained Earnings	Accumulated Other Comprehensive (Loss)	Total
Balance, December 31, 2022	\$ 7,831	\$ 32,716	\$ 90,284	\$ (22,471)	\$ 108,360
Adoption of new accounting standard (ASU 2016-13)	—	—	(1,952)	—	(1,952)
Net income	—	—	3,849	—	3,849
Other comprehensive income	—	—	—	2,255	2,255
Cash dividends on common stock (\$0.15 per share)	—	—	(942)	—	(942)
Stock-based compensation	—	338	—	—	338
Issuance of 2,216 shares of common stock, dividend reinvestment plan	3	38	—	—	41
Issuance of 21,302 shares of common stock, stock incentive plan	27	(27)	—	—	—
Repurchase of 1,557 shares of common stock, stock repurchase plan	(2)	(23)	—	—	(25)
Repurchase of 6,495 shares of common stock, stock incentive plan	(8)	(105)	—	—	(113)
Balance, March 31, 2023	\$ 7,851	\$ 32,937	\$ 91,239	\$ (20,216)	\$ 111,811

	Common Stock	Surplus	Retained Earnings	Accumulated Other Comprehensive (Loss)	Total
Balance, June 30, 2023	\$ 7,813	\$ 32,601	\$ 93,805	\$ (21,359)	\$ 112,860
Net income	—	—	3,121	—	3,121
Other comprehensive loss	—	—	—	(3,316)	(3,316)
Cash dividends on common stock (\$0.15 per share)	—	—	(938)	—	(938)
Stock-based compensation	—	274	—	—	274
Issuance of 2,295 shares of common stock, dividend reinvestment plan	3	37	—	—	40
Repurchase of 6,495 shares of common stock, stock incentive plan	15	(15)	—	—	—
Repurchase of 3,674 shares of common stock, stock repurchase plan	(5)	(57)	—	—	(62)
Balance, September 30, 2023	\$ 7,826	\$ 32,840	\$ 95,988	\$ (24,675)	\$ 111,979

	Common Stock	Surplus	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
Balance, December 31, 2021	\$ 7,785	\$ 31,966	\$ 76,990	\$ 298	\$ 117,039
Net income	—	—	12,018	—	12,018
Other comprehensive loss	—	—	—	(28,051)	(28,051)
Cash dividends on common stock (\$0.42 per share)	—	—	(2,626)	—	(2,626)
Stock-based compensation	—	728	—	—	728
Issuance of 7,853 shares common stock, dividend reinvestment plan	10	142	—	—	152
Issuance of 34,634 shares common stock, stock incentive plan	43	(43)	—	—	—
Repurchase of 8,283 shares common stock, stock incentive plan	(10)	(173)	—	—	(183)
Balance, September 30, 2022	\$ 7,828	\$ 32,620	\$ 86,382	\$ (27,753)	\$ 99,077

	Common Stock	Surplus	Retained Earnings	(Loss)	Accumulated Other Comprehensive	Total
Balance, December 31, 2022	\$ 7,831	\$ 32,716	\$ 90,284	\$ (22,471)	\$ 108,360	
Adoption of new accounting standard (ASU 2016-13)	—	—	(1,952)	—	—	(1,952)
Net income	—	—	10,475	—	—	10,475
Other comprehensive (loss)	—	—	—	(2,204)	—	(2,204)
Cash dividends on common stock (\$0.45 per share)	—	—	(2,819)	—	—	(2,819)
Stock-based compensation	—	681	—	—	—	681
Issuance of 7,047 shares common stock, dividend reinvestment plan	9	111	—	—	—	120
Issuance of 33,002 shares common stock, stock incentive plan	41	(41)	—	—	—	—
Repurchase of 6,495 shares common stock, stock incentive plan	(8)	(106)	—	—	—	(114)
Repurchase of 37,532 shares common stock, stock repurchase plan	(47)	(521)	—	—	—	(568)
Balance, September 30, 2023	\$ 7,826	\$ 32,840	\$ 95,988	\$ (24,675)	\$ 111,979	

	Common Stock	Surplus	Retained Earnings	(Loss)	Accumulated Other Comprehensive	Total
Balance, December 31, 2023	\$ 7,829	\$ 32,950	\$ 94,198	\$ (18,706)	\$ 116,271	
Net income	—	—	3,209	—	—	3,209
Other comprehensive income (loss)	—	—	—	(811)	—	(811)
Cash dividends on common stock (\$0.15 per share)	—	—	(942)	—	—	(942)
Stock-based compensation	—	142	—	—	—	142
Issuance of 2,350 shares common stock, dividend reinvestment plan	3	39	—	—	—	42
Issuance of 16,672 shares common stock, stock incentive plan	21	(21)	—	—	—	—
Repurchase of 4,842 shares common stock, stock incentive plan	(6)	(89)	—	—	—	(95)
Balance, March 31, 2024	\$ 7,847	\$ 33,021	\$ 96,465	\$ (19,517)	\$ 117,816	

See Notes to Consolidated Financial Statements

FIRST NATIONAL CORPORATION

Notes to Consolidated Financial Statements (Unaudited)

Note 1. General

Basis of Presentation

The accompanying unaudited consolidated financial statements of First National Corporation (the Company) and its subsidiary, First Bank (the Bank), have been prepared in accordance with U.S. generally accepted accounting principles (GAAP) for interim financial information and in accordance with guidance provided by the Securities and Exchange Commission (SEC). Accordingly, they do not include all of the information and footnotes required by GAAP for annual year-end financial statements. All significant intercompany balances and transactions have been eliminated. In the opinion of management, the accompanying unaudited consolidated financial statements contain all adjustments and reclassifications of a normal and recurring nature considered necessary to present fairly the financial positions at **September 30, 2023** **March 31, 2024** and **December 31, 2022** **2023**, the statements of income and comprehensive income (loss) for the three and nine months ended **September 30, 2023** **March 31, 2024** and **2022** **2023**, the cash flows for the nine three months ended **September 30, 2023** **March 31, 2024** and **2022** **2023**, and the changes in shareholders' equity for the three and nine months ended **September 30, 2023** **March 31, 2024** and **2022** **2023**. The statements should be read in conjunction with the consolidated financial statements and related notes included in the Annual Report on Form 10-K for the year ended December 31, **2022** **2023**. Operating results for the three and nine months ended **September 30, 2023** **March 31, 2024** are not necessarily indicative of

the results that may be expected for the year ending December 31, 2023 2024. Certain items in the prior period financial statements have been reclassified to conform to the current presentation. These reclassifications had no effect on prior year net income or shareholders' equity.

Significant Accounting Policies and Estimates

Application of the principles of GAAP and practices within the banking industry requires management to make estimates, assumptions, and judgements that affect the amounts reported in the financial statements and accompanying notes. These estimates, assumptions, and judgements are based on information available as of the date of the financial statements; accordingly, as this information changes, the financial statements may reflect different estimates, assumptions and judgements. Certain policies inherently rely more extensively on the use of estimates, assumptions, and judgements and as such may have a greater possibility of producing results that could be materially different than originally reported. Material estimates that are particularly susceptible to significant changes in the near term include estimates related to the determination of the allowance for credit losses.

The Company's significant accounting policies followed in the preparation of the unaudited consolidated financial statements are disclosed in Note 1 of the audited financial statements and notes for the year ended December 31, 2022 2023 and are contained in the Company's 2022 2023 Annual Report on Form 10-K. **There**

Business Combination

On March 25, 2024, the Company entered into an agreement to acquire Touchstone Bankshares, Inc. (Touchstone) for an aggregate purchase price of \$47.0 million in stock. The financial position and results of operations of Touchstone are not reflected in the Company's financial statements as of March 31, 2024. At the time of closing of the acquisition, Touchstone is expected to have been no twelve significant changes retail bank offices serving south-central Virginia and northern North Carolina, and an administrative office in Prince George, Virginia. The closing of the acquisition is subject to customary closing conditions, including shareholder and regulatory approvals. As of March 31, 2024, Touchstone reported total assets of \$673.2 million, gross loans of \$506.0 million, and total deposits of \$557.6 million.

In connection with the transaction, the Company expects to issue approximately 2.7 million shares of its common stock to the application shareholders of significant Touchstone. Upon completion of the transaction, Touchstone Bank, which is Touchstone's wholly owned banking subsidiary, is expected to be merged with and into First Bank. The acquisition will be accounted for as a business combination under ASC 805, **Business Combinations**. Under acquisition accounting, policies since December 31, 2022, except for assets acquired and liabilities assumed are recorded at their acquisition date fair values, and any excess of the following: purchase price over the aggregate fair value of the net assets acquired is recognized as goodwill.

Adoption of New Accounting Pronouncements

ASU In 2016-13: On January 1, July 2023, the Company adopted Financial Accounting Standards Update (ASU) Board (FASB) issued ASU 2023-03, "Presentation of Financial Statements (Topic 205), Income Statement—Reporting Comprehensive Income (Topic 220), Distinguishing Liabilities from Equity (Topic 480), Equity (Topic 505), and Compensation—Stock Compensation (Topic 718)". This ASU amends the FASB Accounting Standards Codification for SEC paragraphs pursuant to SEC Staff Accounting Bulletin No. 2016-13, 120, "Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments" (Accounting Standards Codification (ASC) 326). This standard replaced the incurred loss methodology with an expected loss methodology that is referred to as the current expected credit loss (CECL) methodology. CECL requires an estimate of credit losses for the remaining estimated life of the financial asset using historical experience, current conditions, and reasonable and supportable forecasts and generally applies to financial assets measured at amortized cost, including loan receivables and held-to-maturity debt securities, and some off-balance sheet credit exposures such as unfunded commitments to extend credit. Financial assets measured at amortized cost will be presented SEC Staff Announcement at the net amount expected March 24, 2022 EITF Meeting, and Staff Accounting Bulletin Topic 6.B, Accounting Series Release 280—General Revision of Regulation S-X: Income or Loss Applicable to be collected by using an allowance for credit losses.

In Common Stock. ASU 2023-03 is effective upon addition CECL made changes to the accounting for available for sale debt securities. One such change is to require credit losses to be presented as an allowance rather than as a write-down on available for sale debt securities if management FASB Codification. The Company does not intend to sell and does not believe that it is more likely than not that they will be required to sell.

The Company adopted ASC 326 and all related subsequent amendments thereto effective January 1, 2023 using the modified retrospective approach for all financial assets measured at amortized cost and off-balance sheet credit exposures. The transition adjustment of expect the adoption of CECL included an increase in the allowance for credit losses on loans of \$2.2 million, which is presented as a reduction to net loans outstanding, and an increase in the allowance for credit losses on unfunded commitments of \$153 thousand, which is recorded within other liabilities. The Company recorded an allowance for credit losses for held to maturity securities of \$132 thousand, which is presented as a reduction to held to maturity securities outstanding. The Company recorded a net decrease to retained earnings of \$2.0 million as of ASU January 1, 2023 for the cumulative effect of adopting CECL, which reflects the transition adjustments noted above, net of the applicable deferred tax assets recorded. Results for reporting periods beginning after January 1, 2023 are presented under CECL while prior period amounts continue to be reported in accordance with previously applicable accounting standards.

The Company adopted ASC 326 using the prospective transition approach for purchase credit deteriorated (PCD) assets that were previously classified as purchase credit impaired (PCI) under ASC 310-30. In accordance with the standard, management did not reassess whether PCI assets met the criteria of PCD assets as of the date of adoption. As of September 30, 2023, the Company had no loans classified as PCD.

The Company adopted ASC 326 using the prospective transition approach for debt securities for which other-than-temporary impairment had been recognized prior to January 1, 2023. As of December 31, 2022, the Company did not have any other-than-temporary impaired investment securities. Therefore, upon adoption of ASC 326, the Company determined that an allowance for credit losses on available for sale securities was not required.

The Company elected not 03 to measure an allowance for credit losses for accrued interest receivable and instead elected to reverse interest income on loans or securities that are placed on nonaccrual status, which is generally when the instrument is 90 days past due, or earlier if the Company believes the collection of interest is doubtful. The Company has concluded that this policy results in the timely reversal of uncollectible interest.

	December 31,	
	January 1, 2023	2022

(dollars in thousands)	As reported Under ASC 326	Pre-ASC 326 Adoption	Impact of ASC 326 Adoption
	-	-	-
Assets:			
Allowance for credit losses on held to maturity securities:			
Corporate securities	132	-	132
Allowance for credit losses on loans:			
Construction and land development	233	546	(313)
Secured by 1-4 family residential	2,517	1,108	1,409
Other real estate loans	5,311	3,609	1,702
Commercial and industrial loans	1,487	1,874	(387)
Consumer and other loans	84	309	(225)
Allowance for credit losses on loans	9,632	7,446	2,186
Liabilities:			
Allowance for credit losses for unfunded commitments	153	-	153

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Notes to Consolidated Financial Statements (Unaudited)

Allowance for Credit Losses – Held-to-Maturity Securities

The Company estimates expected credit losses on held-to-maturity securities on an individual basis based on a Probability of Default/Loss Given Default ("PD/LGD") methodology primarily using security-level credit ratings. The primary indicators of credit quality for the Company's held-to-maturity portfolio are security type and credit ratings, which are influenced by a number of factors including obligor cash flow, geography, seniority, among other factors. The Company's held-to-maturity securities with credit risk are municipal bonds and corporate debt securities. All other held-to-maturity securities are covered by the explicit or implied guarantee of the United States government or one of its agencies. Changes in the allowance for credit loss are recorded as provision for (or recovery of) credit losses in the Consolidated Statements of Income. The Company recorded an allowance for credit losses on held-to-maturity securities of \$132 thousand upon adoption of ASC 326. During the three months ended September 30, 2023, the Company recorded a recovery of credit losses on held-to-maturity securities of \$12 thousand. The allowance for credit losses on held-to-maturity securities was \$131 as of September 30, 2023.

Allowance for Credit Losses – Available-for-Sale Securities

Management evaluates all available-for-sale securities in an unrealized loss position on a quarterly basis, and more frequently when economic or market conditions warrant such evaluation. If the Company has the intent to sell the security or it is more likely than not that the Company will be required to sell the security, the security is written down to fair value and the entire loss is recorded in earnings.

If either of the above criteria is not met, the Company evaluates whether the decline in fair value is the result of credit losses or other factors. In making the assessment, the Company may consider various factors including the extent to which fair value is less than amortized cost, downgrades in the ratings of the security by a rating agency, the failure of the issuer to make scheduled interest or principal payments and adverse conditions specific to the security. If the assessment indicates that a credit loss exists, the present value of cash flows expected to be collected are compared to the amortized cost basis of the security and any deficiency is recorded as an allowance for credit loss, limited by the amount that the fair value is less than the amortized cost basis. Any amount of unrealized loss that has not been recorded through an allowance for credit loss is recognized in other comprehensive income.

Changes in the allowance for credit loss are recorded as a provision for (or recovery of) credit losses in the Consolidated Statements of Income. Losses are charged against the allowance for credit loss when management believes an available-for-sale security is confirmed to be uncollectible or when either of the criteria regarding intent or requirement to sell is met. At September 30, 2023, there was no allowance for credit loss related to the available-for-sale portfolio.

Accrued interest receivable on available-for-sale securities totaled \$786 thousand at September 30, 2023 and was excluded from the estimate of credit losses.

Allowance for Credit Losses – Loans

The allowance for loan credit losses represents an amount which, in management's judgement, is adequate to absorb the lifetime expected losses that may be sustained on outstanding loans at the balance sheet date based on the evaluation of the size and current risk characteristics of the loan portfolio, past events, current conditions, reasonable and supportable forecasts of future economic conditions, and prepayment experience. The allowance for loan credit losses is measured and recorded upon the initial recognition of a financial asset. The allowance for loan credit losses is reduced by charge-offs, net of recoveries of previous losses, and is increased or decreased by a provision for (or recovery of) credit losses, which is recorded in the Consolidated Statement of Income.

The Company is utilizing a discounted cash flow model to estimate its current expected credit losses. For the purposes of calculating its quantitative reserves, the Company has segmented its loan portfolio based on loans which share similar risk characteristics. Within the quantitative portion of the calculation, the Company utilizes at least one or a combination of loss drivers, which may include unemployment rates, home price indices, and/or gross domestic product ("GDP"), to adjust its loss rates over a reasonable and supportable forecast period of one year. A straight-line reversion technique is used for the following eight quarters, at which time the Company reverts to historical averages. To further adjust the allowance for credit losses for expected losses not already included within the quantitative component of the calculation, the Company may consider qualitative factors, including but not limited to: variability in the economic forecast, changes in volume and severity of adversity classified loans, changes in concentrations of credit, changes in the nature and volume of the loan segments, factors related to credit administration, and other idiosyncratic risks not embedded in the data used in the model.

Loans that do not share risk characteristics are evaluated on an individual basis. The Company designates individually evaluated loans on nonaccrual status as collateral dependent loans, as well as other loans that management of the Company designates as having higher risk and loans for which the repayment is expected to be provided substantially through the operation or sale of the collateral. These loans do not share common risk characteristics and are not included within the collectively evaluated loans for determining the allowance for credit losses. Under CECL, for collateral dependent loans, the Company has adopted the practical expedient to measure the allowance for credit losses based on the fair value of collateral. The allowance for credit losses is calculated on an individual loan basis based on the shortfall between the fair value of the loan's collateral, which is adjusted for liquidation costs/discounts, and amortized cost. If the fair value of the collateral exceeds the amortized cost, no allowance is required.

The adoption of CECL did not result in a significant change to any other credit risk management and monitoring processes, including identification of past due or delinquent borrowers, nonaccrual practices or charge-off policy.

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Notes to Consolidated Financial Statements (Unaudited)

Allowance for Credit Losses – Unfunded Commitments

Financial Instruments include off-balance sheet credit instruments, such as commitments to make loans and commercial letters of credit issued to meet customer financing needs. The Company's exposure to credit losses in the event of nonperformance by the other party to the financial instrument for off-balance sheet loan commitments is represented by the contractual amount of those instruments. Such financial instruments are recorded when they are funded.

The Company records all allowance for credit losses on off-balance sheet credit exposures, unless the commitments to extend credit are unconditionally cancelable, through a charge to provision for (or recovery of) credit losses in the Consolidated Statement of Income. The allowances for credit losses on off-balance sheet credit exposures is estimated by loan segment at each balance sheet date under the current expected credit losses model using the same methodology as the loan portfolio, taking into consideration the likelihood that funding will occur as well as any third-party guarantees. The allowance for unfunded commitments is included in other liabilities on the Company's consolidated balance sheet.

Accrued Interest Receivable

The Company has elected to exclude the accrued interest from the amortized cost basis in its determination of the allowance for credit losses for both loans and held-to-maturity securities, as well as elected the policy to write-off accrued interest receivable directly through the reversal of interest income. Accrued interest receivable totaled \$3.1 million on loans and \$593 thousand on held-to-maturity securities at September 30, 2023 and is included in "Accrued Interest Receivable" on the Company's Consolidated Balance Sheets.

ASU 2022-01:

On January 1, 2023, the Company adopted ASU 2022-01, "Derivatives and Hedging (Topic 815), Fair Value Hedging—Portfolio Layer Method." ASU 2022-01 clarifies the guidance in ASC 815 on fair value hedge accounting of interest rate risk for portfolios of financial assets and is intended to better align hedge accounting with an organization's risk management strategies. In 2017, FASB issued ASU 2017-12 to better align the economic results of risk management activities with hedge accounting. One of the major provisions of that standard was the addition of the last-of-layer hedging method. For a closed portfolio of fixed-rate prepayable financial assets or one or more beneficial interests secured by a portfolio of prepayable financial instruments, such as mortgages or mortgage-backed securities, the last-of-layer method allows an entity to hedge its exposure to fair value changes due to changes in interest rates for a portion of the portfolio that is not expected to be affected by prepayments, defaults, and other events affecting the timing and amount of cash flows. ASU 2022-01 renames that method the portfolio layer method. The Company adopted ASU 2022-01 prospectively and it did not have a material impact on its consolidated financial statements.

ASU In 2022-02: On January 1, March 2023, the Company adopted FASB issued ASU 2022-02, "Financial Instruments-Credit Losses" "Investments—Equity Method and Joint Ventures (Topic 326 323), Troubled Debt Restructurings and Vintage Disclosures." Accounting for Investments in Tax Credit Structures Using the Proportional Amortization Method". These amendments allow reporting entities to elect to account for qualifying tax equity investments using the proportional amortization method, regardless of the program giving rise to the related income tax credits. The ASU is effective for public business entities for fiscal years beginning after December 15, 2023, including interim periods within those fiscal years. Early adoption is permitted for all entities in any interim period. The Company does not expect the adoption of ASU 2022-02 addresses areas identified by the FASB as part of its post-implementation review of the credit losses standards (ASU 2016-13) that introduced the CECL model. The amendments eliminate the accounting guidance for troubled debt restructurings (TDRs) by creditors that have adopted the CECL model and enhance the disclosure requirements for certain loan refinancings by creditors when a borrower is experiencing financial difficulty. In addition, the amendments require that the Company disclose current-period gross write-offs for financing receivables and net investment in leases by year of origination in the vintage disclosures. The Company adopted the standard prospectively and it did not have a material impact on its consolidated financial statements.

In March 2023, the FASB issued ASU 2023-01, "Leases (Topic 842): Common Control Arrangements". These amendments require entities to amortize leasehold improvements associated with common control leases over the useful life to the common control group. The ASU is effective for fiscal years beginning after December 15, 2023, including interim periods within those fiscal years. Early adoption is permitted. If an entity adopts the amendments in an interim period, it must adopt them as of the beginning of the fiscal year that includes that interim period. Transition can be done either retrospectively or prospectively. The Company does not expect the adoption of ASU 2023-01 to have a material impact on its consolidated financial statements.

In June 2022, the FASB issued ASU 2022-03, "Fair Value Measurement (Topic 820): Fair Value Measurement of Equity Securities Subject to Contractual Sale Restrictions." ASU 2022-03 clarifies that a contractual restriction on the sale of an equity security is not considered part of the unit of account of the equity security and, therefore, is not considered in measuring fair value. The ASU is effective for fiscal years, including interim periods within those fiscal years, beginning after December 15, 2023. Early adoption is permitted. The Company does not expect the adoption of ASU 2022-03 to have a material impact on its consolidated financial statements.

Recent Accounting Pronouncements

In July 2023, March 2024, the Financial Accounting Standards Board (FASB) issued ASU 2023-03, "Presentation of Financial Statements (Topic 205), Income Statement—Reporting Comprehensive Income (Topic 220), Distinguishing Liabilities from Equity (Topic 480), Equity (Topic 505), and Compensation—Compensation—Stock Compensation (Topic 718)" Scope Application of Profits Interest and Similar Awards". This ASU amends the FASB Accounting Standards Codification provides an illustrative example intended to demonstrate how entities that account for SEC paragraphs pursuant to SEC Staff Accounting Bulletin No.120, SEC Staff Announcement at the March 24, 2022 EITF Meeting, profits interest and Staff Accounting Bulletin similar awards would determine whether a profits interest award should be accounted for in accordance with Topic 6.B, 718, Accounting Series Release 280—General Revision of Regulation S-X: Income or Loss Applicable to Common Stock. ASU 2023-03 is effective upon adoption to the FASB Codification. The Company does not expect the adoption of ASU 2023-03 to have a material impact on its consolidated financial statements.

In June 2022, the FASB issued ASU 2022-03, "Fair Value Measurement (Topic 820): Fair Value Measurement of Equity Securities Subject to Contractual Sale Restrictions." ASU 2022-03 clarifies that a contractual restriction on the sale of an equity security is not considered part of the unit of account of the equity security and, therefore, is not considered in measuring fair value. The This ASU is effective for fiscal years, including annual periods beginning after December 15, 2024, and interim periods within those fiscal years, beginning after December 15, 2023. Early adoption is permitted. The Company does not expect the adoption of ASU 2022-03 to have a material impact on its consolidated financial statements.

In March 2023, the FASB issued ASU 2023-01, "Leases (Topic 842): Common Control Arrangements". These amendments require entities to amortize leasehold improvements associated with common control leases over the useful life to the common control group. The ASU is effective for fiscal years beginning after December 15, 2023, including interim periods within those fiscal years, annual periods. Early adoption is permitted. If an entity adopts the amendments in an interim period, it must adopt them as of the beginning of the fiscal year annual period that includes that interim period. Transition can be done either retrospectively or prospectively. The Company does not expect the adoption of ASU 2023-01 to have a material impact on its consolidated (consolidated) financial statements.

In March 2023, 2024, the FASB Financial Accounting Standards Board (FASB) issued ASU 2023-02, "Investments—Equity Method and Joint Ventures (Topic 323): Accounting for Investments in Tax Credit Structures Using the Proportional Amortization Method". These amendments allow reporting entities Codification Improvements – Amendments to elect to account for qualifying tax equity investments using the proportional amortization method, regardless of the program giving rise Remove References to the related income tax credits. The Concepts Statements". This ASU contains amendments to the Codification that remove references to various Concepts Statements. In most instances, the references are extraneous and not required to understand or apply the guidance. In other instances, the references were used in prior Statements to provide guidance in certain topical areas. This ASU is effective for public business entities for fiscal years beginning after December 15, 2023, 2024, including interim periods within those fiscal years. Early adoption is permitted for permitted. The amendments should be applied prospectively to all entities new transactions recognized on or after the date that the entity first applies the amendments or retrospectively to the beginning of the earliest comparative period presented in any interim period, which the amendments were first applied. If an entity adopts the amendments retrospectively, it should adjust the opening balance of retained earnings as of the beginning of the earliest comparative period presented. The Company does not expect the adoption of ASU 2023-02 to have a material impact on its consolidated (consolidated) financial statements.

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Notes to Consolidated Financial Statements (Unaudited)

Note 2. Securities

The Company invests in U.S. Treasury securities, U.S. agency and mortgage-backed securities, obligations of state and political subdivisions, and corporate debt securities. Amortized costs, gross unrealized gains and losses, allowance for credit losses, and fair values of debt securities at September 30, 2023 March 31, 2024 and December 31, 2022 2023 were as follows (in thousands):

	September 30, 2023					March 31, 2024				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Fair Value	Allowance for Credit Losses	Amortized Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Fair Value	Allowance for Credit Losses
Securities available for sale:										
U.S. Treasury securities	\$ 12,474	\$ —	\$ (1,361)	\$ 11,113	\$ —	\$ 12,478	\$ —	\$ (1,079)	\$ 11,399	\$ —
U.S. agency and mortgage-backed securities	99,894	60	(15,660)	84,294	—	93,915	50	(12,997)	80,968	—
Obligations of states and political subdivisions	64,131	4	(11,367)	52,768	—	63,461	1	(8,154)	55,308	—
Total securities available for sale	\$ 176,499	\$ 64	\$ (28,388)	\$ 148,175	\$ —	\$ 169,854	\$ 51	\$ (22,230)	\$ 147,675	\$ —
Securities held to maturity:										

U.S. Treasury securities	\$ 38,862	\$ —	\$ (734)	\$ 38,128	\$ —	\$ 19,277	\$ —	\$ (349)	\$ 18,928	\$ —
U.S. agency and mortgage-backed securities	96,563	—	(12,216)	84,347	—	92,019	—	(10,033)	81,986	—
Obligations of states and political subdivisions	11,654	—	(1,706)	9,948	—	11,645	40	(996)	10,689	(1)
Corporate debt securities	3,000	—	(564)	2,436	(131)	3,000	—	(514)	2,486	(115)
Total securities held to maturity	\$ 150,079	\$ —	\$ (15,220)	\$ 134,859	\$ (131)	\$ 125,941	\$ 40	\$ (11,892)	\$ 114,089	\$ (116)
Total securities	\$ 326,578	\$ 64	\$ (43,608)	\$ 283,034	\$ (131)	\$ 295,795	\$ 91	\$ (34,122)	\$ 261,764	\$ (116)

	December 31, 2022					December 31, 2023					Allowance for Credit Losses	
	Amortized Cost	Gross Unrealized Gains		Gross Unrealized (Losses)		Fair Value	Amortized Cost	Gross Unrealized Gains		Gross Unrealized (Losses)		
Securities available for sale:												
U.S. Treasury securities	\$ 12,468	\$ —	\$ (1,239)	\$ 11,229	\$ 12,476	\$ —	\$ (1,026)	\$ 11,450	\$ —	\$ —	\$ —	
U.S. agency and mortgage-backed securities	109,972	95	(13,149)	96,918	96,937	55	(12,192)	84,800	—	—	—	
Obligations of states and political subdivisions	64,386	4	(9,630)	54,760	64,045	6	(7,444)	56,607	—	—	—	
Total securities available for sale	\$ 186,826	\$ 99	\$ (24,018)	\$ 162,907	\$ 173,458	\$ 61	\$ (20,662)	\$ 152,857	\$ —	\$ —	\$ —	
Securities held to maturity:												
U.S. Treasury securities	\$ 38,211	\$ —	\$ (568)	\$ 37,643	\$ 39,085	\$ —	\$ (389)	\$ 38,696	\$ —	\$ —	\$ —	
U.S. agency and mortgage-backed securities	99,374	—	(9,189)	90,185	94,617	—	(8,992)	85,625	—	—	—	
Obligations of states and political subdivisions	12,573	—	(1,252)	11,321	11,649	107	(943)	10,813	—	—	—	
Corporate debt securities	3,000	—	(352)	2,648	3,000	—	(520)	2,480	—	—	—	(107)
Total securities held to maturity	\$ 153,158	\$ —	\$ (11,361)	\$ 141,797	\$ 148,351	\$ 107	\$ (10,844)	\$ 137,614	\$ —	\$ (107)	\$ —	
Total securities	\$ 339,984	\$ 99	\$ (35,379)	\$ 304,704	\$ 321,809	\$ 168	\$ (31,506)	\$ 290,471	\$ —	\$ (107)	\$ —	

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Notes to Consolidated Financial Statements (Unaudited)

Information pertaining to securities with gross unrealized losses aggregated by investment category and length of time that individual securities have been in a continuous loss position is as follows (in thousands):

	September 30, 2023						March 31, 2024						Total	
	Less than 12 months		12 months or more		Total		Less than 12 months		12 months or more		Total			
	Fair Value	Unrealized (Loss)	Fair Value	Unrealized (Loss)	Fair Value	Unrealized (Loss)	Fair Value	Unrealized (Loss)	Fair Value	Unrealized (Loss)	Fair Value	Unrealized (Loss)		
Securities available for sale:														
U.S. Treasury securities	\$ —	\$ —	\$ 11,113	\$ (1,361)	\$ 11,113	\$ (1,361)	\$ —	\$ —	\$ 11,399	\$ (1,079)	\$ 11,399	\$ (1,079)		
U.S. agency and mortgage-backed securities	2,065	(37)	77,201	(15,623)	79,266	(15,660)	1,268	(13)	75,506	(12,984)	76,774	(12,997)		

Obligations of states and political subdivisions	7,753	(382)	44,511	(10,985)	52,264	(11,367)	5,341	(195)	48,276	(7,959)	53,617	(8,154)	
Total securities available for sale	\$ 9,818	\$ (419)	\$ 132,825	\$ (27,969)	\$ 142,643	\$ (28,388)	\$ 6,609	\$ (208)	\$ 135,181	\$ (22,022)	\$ 141,790	\$ (22,230)	
	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	_____	
December 31, 2022												December 31, 2023	
Less than 12 months												Total	
		Fair Value	Unrealized (Loss)			Fair Value	Unrealized (Loss)			Fair Value	Unrealized (Loss)		
Securities available for sale:													
U.S. Treasury securities	\$ 9,041	\$ (932)	\$ 2,188	\$ (307)	\$ 11,229	\$ (1,239)	\$ —	\$ —	\$ 11,450	\$ (1,026)	\$ 11,450	\$ (1,026)	
U.S. agency and mortgage-backed securities	27,282	(1,945)	62,342	(11,204)	89,624	(13,149)	1,281	(29)	78,800	(12,163)	80,081	(12,192)	
Obligations of states and political subdivisions	24,689	(2,581)	26,362	(7,049)	51,051	(9,630)	4,469	(215)	47,004	(7,229)	51,473	(7,444)	
Total securities available for sale	\$ 61,012	\$ (5,458)	\$ 90,892	\$ (18,560)	\$ 151,904	\$ (24,018)	\$ 5,750	\$ (244)	\$ 137,254	\$ (20,418)	\$ 143,004	\$ (20,662)	
Securities held to maturity:													
U.S. Treasury securities	\$ 19,302	\$ (258)	\$ 18,342	\$ (310)	\$ 37,644	\$ (568)							
U.S. agency and mortgage-backed securities	58,019	(6,848)	32,167	(2,341)	90,186	(9,189)							
Obligations of states and political subdivisions	8,648	(1,008)	2,672	(244)	11,320	(1,252)							
Corporate debt securities	2,648	(352)	—	—	2,648	(352)							
Total securities held to maturity	\$ 88,617	\$ (8,466)	\$ 53,181	\$ (2,895)	\$ 141,798	\$ (11,361)							
Total securities	\$ 149,629	\$ (13,924)	\$ 144,073	\$ (21,455)	\$ 293,702	\$ (35,379)							

The tables above provide information about securities that have been in an unrealized loss position for less than twelve consecutive months and securities that have been in an unrealized loss position for twelve consecutive months or more. Management evaluates securities to determine whether the impairment is due to credit-related factors or noncredit-related factors at least on a quarterly basis, and more frequently when economic or market concerns warrant such evaluation. Consideration is given to the extent to which the fair value is less than cost, the financial condition and near-term prospects of the issuer, and the intent and ability of the Company to retain its investment in the security for a period of time sufficient to allow for any anticipated recovery in fair value. Presently, the Company does not intend to sell any of these securities, does not expect to be required to sell these securities, and expects to recover the entire amortized cost of all the securities.

Accrued interest receivable on securities available for sale and securities held to maturity totaled \$786 \$756 thousand and \$593 \$548 thousand, respectively, at September 30, 2023 March 31, 2024. Accrued interest on debt securities is included in accrued interest receivable on the Company's consolidated balance sheets.

At September 30, 2023 March 31, 2024, there were three out of three U.S. Treasury securities, 94 out of 107 109 U.S. agency and mortgage-backed securities, and 97 94 out of 104 108 obligations of states and political subdivisions in an unrealized loss position. One hundred percent of the Company's investment portfolio was considered investment grade. The weighted-average re-pricing term of the portfolio was 5.9 6.2 years at September 30, 2023 March 31, 2024. One hundred percent of the Company's investment portfolio was considered investment grade at December 31, 2022 2023. The weighted-average re-pricing term of the portfolio was 6.5 5.9 years at December 31, 2022 2023. The unrealized losses at September 30, 2023 March 31, 2024 in the U.S. Treasury securities portfolio, U.S. agency and mortgage-backed securities portfolio, and obligations of states and political subdivisions portfolio were related to changes in market interest rates and not credit concerns of the issuers.

On September 1, 2022, the Bank transferred 24 securities designated as available for sale with a combined book value of \$82.2 million, market value of \$74.4 million, and unrealized loss of \$7.8 million, to securities designated held to maturity. The unrealized loss is being amortized monthly over the life of the securities with an increase to the carrying value of securities and a decrease to the related accumulated other comprehensive loss, which is included in the shareholders' equity section of the Company's balance sheet. The amortization of the unrealized loss on the transferred securities totaled \$1.2 million \$367 thousand for the first nine three months of 2023, 2024. The securities selected for transfer had larger potential decreases in their fair market values in higher interest rate environments than most of the other securities in the available for sale portfolio and included U.S. Treasury, agency, municipal and commercial mortgage-backed securities. The securities were transferred to mitigate the potential unfavorable impact that higher market interest rates may have on the carrying value of the securities and on the related accumulated other comprehensive loss.

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Notes to Consolidated Financial Statements (Unaudited)

The amortized cost and fair value of securities at September 30, 2023 March 31, 2024 by contractual maturity are shown below (in thousands). Expected maturities of mortgage-backed securities will differ from contractual maturities because borrowers may have the right to prepay obligations with or without call or prepayment penalties.

	Available for Sale		Held to Maturity		Available for Sale		Held to Maturity	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Due within one year	\$ 760	\$ 757	\$ 20,828	\$ 20,642	\$ 796	\$ 783	\$ 10,820	\$ 10,698
Due after one year through five years	23,027	21,026	28,993	27,586	28,704	26,521	23,107	21,835
Due after five years through ten years	37,962	33,340	23,514	20,658	32,673	29,684	17,972	16,117
Due after ten years	114,750	93,052	76,744	65,973	107,681	90,687	74,042	65,439
	\$ 176,499	\$ 148,175	\$ 150,079	\$ 134,859	\$ 169,854	\$ 147,675	\$ 125,941	\$ 114,089

Federal Home Loan Bank, Federal Reserve Bank, and Community Bankers' Bank stock are generally viewed as long-term investments and as restricted securities, which are carried at cost, because there is a minimal market for the stock. Therefore, when evaluating restricted securities for impairment, their value is based on the ultimate recoverability of the par value rather than by recognizing temporary declines in value.

The composition of restricted securities at September 30, 2023 March 31, 2024 and December 31, 2022 2023 was as follows (in thousands):

	September 30, 2023	December 31, 2022	March		December
			31, 2024	31, 2023	
Federal Home Loan Bank stock	\$ 965	\$ 796	\$ 999	\$ 965	
Federal Reserve Bank stock	980	980	981	981	
Community Bankers' Bank stock	132	132	132	132	
	\$ 2,077	\$ 1,908	\$ 2,112	\$ 2,078	

The Company also holds limited partnership investments in Small Business Investment Companies (SBICs), which are included in other assets in the Consolidated Balance Sheets. The limited partnership investments are measured as equity investments without readily determinable fair values at their cost, less any impairment. The amounts included in other assets for the limited partnership investments were \$642 thousand and \$599 \$642 thousand at September 30, 2023 March 31, 2024 and December 31, 2022 2023, respectively.

Credit Quality Indicators & Allowance for Credit Losses - HTM

The Company monitors the credit quality of the debt securities held to maturity through the use of credit ratings from Moody's, S&P, and Egan-Jones. The Company monitors the credit ratings on a quarterly basis. The following table summarizes the amortized cost of debt securities held to maturity at **September 30, 2023** **March 31, 2024**, aggregated by credit quality indicators.

	U.S. Treasury securities	U.S. agency and mortgage- backed securities	Obligations of states and political subdivisions	Corporate debt securities	Total Held to Maturity Securities	U.S. Treasury securities	U.S. agency and mortgage- backed securities	Obligations of states and political subdivisions	Corporate debt securities	Total Held to Maturity Securities
September 30, 2023										
March 31, 2024										
Aaa										
Aaa	\$ 38,862	\$ 22,877	\$ 2,812	\$ —	\$ 64,551	\$ 19,277	\$ 22,994	\$ 2,802	\$ —	\$ 45,073
Aa1 / Aa2 / Aa3	—	—	8,842	—	8,842	—	—	8,843	—	8,843
Baa1 / Baa2 / Baa3	—	—	—	3,000	3,000	—	—	—	3,000	3,000
Not rated - Agency (1)	—	73,686	—	—	73,686	—	69,025	—	—	69,025
Total	\$ 38,862	\$ 96,563	\$ 11,654	\$ 3,000	\$ 150,079	\$ 19,277	\$ 92,019	\$ 11,645	\$ 3,000	\$ 125,941
December 31, 2022										
December 31, 2023										
Aaa	\$ 38,211	\$ 22,706	\$ 3,126	\$ —	\$ 64,043	\$ 39,085	\$ 22,936	\$ 2,807	\$ —	\$ 64,828
Aa1 / Aa2 / Aa3	—	—	9,447	—	9,447	—	—	8,842	—	8,842
Baa1 / Baa2 / Baa3	—	—	—	3,000	3,000	—	—	—	3,000	3,000
Not rated - Agency (1)	—	76,668	—	—	76,668	—	71,681	—	—	71,681
Total	\$ 38,211	\$ 99,374	\$ 12,573	\$ 3,000	\$ 153,158	\$ 39,085	\$ 94,617	\$ 11,649	\$ 3,000	\$ 148,351

(1) Generally considered not to have credit risk given the implied governmental guarantees associated with these agencies.

The following table summarizes the change in the allowance for credit losses on held to maturity securities for the **nine** **three** months ended **September 30, 2023** **March 31, 2024**.

	U.S. Treasury securities	U.S. agency and mortgage- backed securities	Obligations of states and political subdivisions	Corporate debt securities	Total Held to Maturity Securities	U.S. Treasury securities	U.S. agency and mortgage- backed securities	Obligations of states and political subdivisions	Corporate debt securities	Total Held to Maturity Securities
Balance, December 31, 2022	\$ —	\$ —	\$ —	\$ —	\$ —	—	—	—	—	—
Adjustment for adoption of ASU 2016-13	—	—	—	134	134	—	—	—	—	—
Balance, December 31, 2023	—	—	—	—	—	\$ —	\$ —	\$ —	\$ 107	\$ 107
Provision for credit losses	—	—	—	10	10	—	—	1	8	9
Charge-offs of securities	—	—	—	—	—	—	—	—	—	—
Recoveries	—	—	—	(13)	(13)	—	—	—	—	—
Balance, September 30, 2023	\$ —	\$ —	\$ —	\$ 131	\$ 131	\$ —	\$ —	\$ 1	\$ 115	\$ 116
Balance, March 31, 2024	—	—	—	—	—	\$ —	\$ —	\$ 1	\$ 115	\$ 116

At **September 30, 2023** **March 31, 2024**, the Company had no securities held-to-maturity that were past due 30 days or more as to principal and interest payments. The Company had no securities held-to-maturity classified as nonaccrual as of **September 30, 2023** **March 31, 2024**.

Note 3. Loans

Loans at September 30, 2023 March 31, 2024 and December 31, 2022 2023 are summarized as follows (in thousands):

	September 30, 2023	December 31, 2022	March 31, 2024	December 31, 2023
Real estate loans:				
Construction and land development	\$ 50,405	\$ 51,840	\$ 53,364	\$ 52,680
Secured by 1-4 family residential	340,773	331,421	347,014	344,369
Other real estate loans	433,177	418,456	445,085	447,272
Commercial and industrial loans	117,130	111,225	113,562	113,074
Consumer and other loans	11,014	7,581	13,949	12,035
Total loans	\$ 952,499	\$ 920,523	\$ 972,974	\$ 969,430
Allowance for credit losses	(8,896)	(7,446)	(12,603)	(11,974)
Loans, net	\$ 943,603	\$ 913,077	\$ 960,371	\$ 957,456

Net deferred loan fees included in the above loan categories were \$929 thousand \$1.1 million and \$838 thousand \$1.1 million at September 30, 2023 March 31, 2024 and December 31, 2022 2023, respectively. Consumer respectively. Unamortized premiums on loans purchased from a third-party loan originator are included in the commercial and industrial loan categories and totaled \$7.4 million as of March 31, 2024 and \$7.9 million as of December 31, 2023. Consumer and other loans included \$368 \$251 thousand and \$197 \$222 thousand of demand deposit overdrafts at September 30, March 31, 2024 and December 31, 2023, respectively.

Loans acquired in business combinations are recorded in the Consolidated Balance Sheets at fair value at the acquisition date under the acquisition method of accounting. The principal balance of purchased loans is included in the allowance for credit losses calculation. The remaining net discount on purchased loans at March 31, 2024 was \$1.8 million. The outstanding principal balance and the carrying amount at March 31, 2024 and December 31, 2022, respectively, of loans acquired in business combinations were as follows:

	March 31, 2024	December 31, 2023
(Dollars in thousands)	Acquired Loans-	Acquired Loans-
	Non-Purchased	Non-Purchased
Outstanding principal balance	\$ 155,913	\$ 164,028
Carrying amount		
Real estate loans:		
Construction and land development	\$ 7,676	\$ 7,851
Secured by 1-4 family residential	35,044	36,290
Other real estate loans	91,362	94,882
Commercial and industrial loans	16,558	19,611
Consumer and other loans	3,428	3,451
Total acquired loans	\$ 154,068	\$ 162,085

Risk characteristics of each loan portfolio class that are considered by the Company include:

- 1-4 family residential mortgage loans carry risks associated with the continued creditworthiness of the borrower and changes in the value of the collateral.
- Real estate construction and land development loans carry risks that the project may not be finished according to schedule, the project may not be finished according to budget, and the value of the collateral may, at any point in time, be less than the principal amount of the loan. Construction loans also bear the risk that the general contractor, who may or may not be a loan customer, may be unable to finish the construction project as planned because of financial pressure or other factors unrelated to the project.
- Other real estate loans carry risks associated with the successful operation of a business or a real estate project, in addition to other risks associated with the ownership of real estate, because repayment of these loans may be dependent upon the profitability and cash flows of the business or project.

- Commercial and industrial loans carry risks associated with the successful operation of a business because repayment of these loans may be dependent upon the profitability and cash flows of the business. In addition, there is risk associated with the value of collateral other than real estate which may depreciate over time and cannot be appraised with as much reliability. Commercial and industrial loans also include purchased loans which could have been originated outside of the Company's market area.
- Consumer and other loans carry risks associated with the continued creditworthiness of the borrower and the value of the collateral, if any. Consumer loans are typically either unsecured or secured by rapidly depreciating assets such as automobiles. They are also likely to be immediately and adversely affected by job loss, divorce, illness, personal bankruptcy, or other changes in circumstances. Consumer and other loans also include purchased consumer loans which could have been originated outside of the Company's market area. Other loans included in this category include loans to states and political subdivisions.

Loans acquired in business combinations are recorded in the Consolidated Balance Sheets at fair value at the acquisition date under the acquisition method of accounting. The principal balance of purchased loans is included in the allowance for credit losses calculation. The remaining net discount on purchased loans at September 30, 2023 was \$2.0 million. The outstanding principal balance and the carrying amount at September 30, 2023 and December 31, 2022 of loans acquired in business combinations were as follows:

(Dollars in thousands)	September 30, 2023		December 31, 2022	
	Acquired Loans-		Acquired Loans-	
	Non-Purchased		Non-Purchased	
	Credit Deteriorated	Credit Deteriorated	Credit Deteriorated	Credit Deteriorated
Outstanding principal balance	\$ 166,349		\$ 187,017	
Carrying amount				
Real estate loans:				
Construction and land development		\$ 8,450		\$ 9,823
Secured by 1-4 family residential		36,405		42,915
Other real estate loans		95,313		103,521
Commercial and industrial loans		20,681		24,661
Consumer and other loans		3,472		3,560
Total acquired loans	<u>\$ 164,321</u>		<u>\$ 184,480</u>	

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Notes to Consolidated Financial Statements (Unaudited)

The following tables provide a summary of loan classes and an aging of past due loans as of September 30, 2023 March 31, 2024 and December 31, 2022 2023 (in thousands):

	September 30, 2023								March 31, 2024								
	30-59	60-89	> 90	Total	Current	Total	Non-	90 Days	30-59	60-	> 90	Total	Current	Total	Non-	90 Days	
	Days	Days	Days	Days					Days	89	Days	Days	Days				
	Days	Days	Days	Days	Days	Days	Days	Days	Days	Days	Days	Days	Days	Days	Days	Days	Days
Real estate loans:																	
Construction and land development	\$ —	\$ —	\$ 39	\$ 39	\$ 50,366	\$ 50,405	\$ 39	\$ —	\$ —	\$ —	\$ —	\$ —	\$ 53,364	\$ 53,364	\$ 37	\$ —	
Secured by 1-4 family residential	1,242	58	534	1,834	338,939	340,773	546	368	1,604	65	130	1,799	345,215	347,014	775	130	
Other real estate loans	—	—	62	62	433,115	433,177	67	—	—	—	—	—	445,085	445,085	—	—	
Commercial and industrial	83	—	—	83	117,047	117,130	2,464	—	474	769	45	1,288	112,274	113,562	7,203	45	

Consumer and other loans	10	2	2	14	11,000	11,014	—	2	53	6	—	59	13,890	13,949	—	—
Total	\$ 1,335	\$ 60	\$ 637	\$ 2,032	\$ 950,467	\$ 952,499	\$ 3,116	\$ 370	\$ 2,131	\$ 840	\$ 175	\$ 3,146	\$ 969,828	\$ 972,974	\$ 8,015	\$ 175

December 31, 2022															
	30-59 Days Past Due			60-89 Days Past Due			> 90 Days Past Due			Total Past Due		Current	Total Loans	Non-accrual Loans	90 Days or More Past Due and Accruing
	30-59 Days	59-89 Days	89-90 Days	60-89 Days	90-109 Days	109+ Days	Total	Past Due	Due	Current	Due	Current			
Real estate loans:															
Construction and land development	\$ 115	\$ 20	\$ 0	\$ 1,045	\$ 1,180	\$ 0	\$ 50,660	\$ 51,840	\$ 1,045	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	
Secured by 1-4 family residential	1,033	60	—	207	1,300	330,121	331,421	530	—	—	—	—	—	—	
Other real estate loans	109	—	—	—	109	418,347	418,456	13	—	—	—	—	—	—	
Commercial and industrial	31	130	—	1,085	1,246	109,979	111,225	1,085	—	—	—	—	—	—	
Consumer and other loans	26	25	—	—	51	7,530	7,581	—	—	—	—	—	—	—	
Total	\$ 1,314	\$ 235	\$ 2,337	\$ 3,886	\$ 916,637	\$ 920,523	\$ 2,673	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	
December 31, 2023															
	30-59 Days Past Due			60-89 Days Past Due			> 90 Days Past Due			Total Past Due		Current	Total Loans	Non-accrual Loans	90 Days or More Past Due and Accruing
	30-59 Days	59-89 Days	89-90 Days	60-89 Days	90-109 Days	109+ Days	Total	Past Due	Due	Current	Due	Current			
Real estate loans:															
Construction and land development	\$ 183	\$ 4	\$ 0	\$ 38	\$ 225	\$ 0	\$ 52,455	\$ 52,680	\$ 38	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	
Secured by 1-4 family residential	1,364	350	—	392	2,106	342,263	344,369	495	245	—	—	—	—	—	
Other real estate loans	—	—	—	82	82	447,190	447,272	82	—	—	—	—	—	82	
Commercial and industrial	252	316	—	197	765	112,309	113,074	6,230	197	—	—	—	—	—	
Consumer and other loans	33	—	—	—	33	12,002	12,035	—	—	—	—	—	—	—	
Total	\$ 1,832	\$ 670	\$ 709	\$ 3,211	\$ 966,219	\$ 969,430	\$ 6,763	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	\$ 524	

Credit Quality Indicators

As part of the ongoing monitoring of the credit quality of the Company's loan portfolio, management tracks certain credit quality indicators including trends related to the risk grading of specified classes of loans. The Company utilizes a risk grading matrix to assign a rating to each of its loans. The loan ratings are summarized into the following categories: pass, special mention, substandard, doubtful, and loss. Pass rated loans include all risk rated credits other than those included in special mention, substandard, or doubtful. Loans classified as loss are charged-off. Loan officers assign risk grades to loans at origination and as renewals arise. The Bank's Credit Administration department reviews risk grades for accuracy on a quarterly basis and as credit issues arise. In addition, a certain amount of loans are reviewed each year through the Company's internal and external loan review process. A description of the general characteristics of the loan grading categories is as follows:

Pass – Loans classified as pass exhibit acceptable operating trends, balance sheet trends, and liquidity. Sufficient cash flow exists to service the loan. All obligations have been paid by the borrower as agreed.

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 the Bank's credit position at some future date.

Substandard – Loans classified as substandard are inadequately protected by the current net worth and payment 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 Bank 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. The Company considers all doubtful loans to be impaired and places the loan on non-accrual status.

Loss – Loans classified as loss are considered uncollectable and of such little value that their continuance as bankable assets is not warranted.

Notes to Consolidated Financial Statements (Unaudited)

The following table presents the Company's recorded investment in loans by credit quality indicators by year of origination as of **September 30, 2023** **March 31, 2024** (in thousands).

		September 30, 2023									Term Loans by Year of Origination		Revolving		Total	
		2023		2022		2021		2020		2019						
Construction	and	land														
Pass		\$ 2,625	\$ 3,311	\$ 7,824	\$ 2,613	\$ 2,127	\$ 3,290	\$ 28,576	\$ 50,366							
Special Mention		—	—	—	—	—	—	—	—							
Substandard		—	—	—	—	—	—	—	39						39	
Doubtful		—	—	—	—	—	—	—	—							
Total Construction and land development		\$ 2,625	\$ 3,311	\$ 7,824	\$ 2,613	\$ 2,127	\$ 3,329	\$ 28,576	\$ 50,405							
Current period gross write-offs		\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —							
Secured by 1-4 family residential																
Pass		\$ 32,461	\$ 78,044	\$ 65,455	\$ 42,454	\$ 33,258	\$ 78,826	\$ 9,438	\$ 339,936							
Special Mention		—	—	—	—	—	—	—	—							
Substandard		—	98	19	—	—	—	720	—						837	
Doubtful		—	—	—	—	—	—	—	—							
Total Secured by 1-4 family residential		\$ 32,461	\$ 78,142	\$ 65,474	\$ 42,454	\$ 33,258	\$ 79,546	\$ 9,438	\$ 340,773							
Current period gross write-offs		\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —							
Other real estate loans																
Pass		\$ 34,365	\$ 93,010	\$ 87,799	\$ 42,599	\$ 40,686	\$ 123,320	\$ 11,331	\$ 433,110							
Special Mention		—	—	—	—	—	—	—	—							
Substandard		—	—	—	—	—	—	—	67						67	
Doubtful		—	—	—	—	—	—	—	—							
Total Other real estate loans		\$ 34,365	\$ 93,010	\$ 87,799	\$ 42,599	\$ 40,686	\$ 123,320	\$ 11,398	\$ 433,177							
Current period gross write-offs		\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —							
Commercial and industrial																
Pass		\$ 21,279	\$ 30,216	\$ 25,491	\$ 4,373	\$ 5,135	\$ 8,729	\$ 18,050	\$ 113,273							
Special Mention		—	—	—	—	—	—	—	—							
Substandard		—	2,870	—	100	—	887	—	3,857							
Doubtful		—	—	—	—	—	—	—	—							
Total Commercial and industrial		\$ 21,279	\$ 33,086	\$ 25,491	\$ 4,473	\$ 5,135	\$ 9,616	\$ 18,050	\$ 117,130							
Current period gross write-offs		\$ —	\$ —	\$ —	\$ —	\$ 624	\$ —	\$ 253	\$ —						877	
Consumer and other loans																
Pass		\$ 2,625	\$ 1,408	\$ 395	\$ 1,505	\$ 2,222	\$ 29	\$ 2,830	\$ 11,014							

Special Mention	—	—	—	—	—	—	—	—	—
Substandard	—	—	—	—	—	—	—	—	—
Doubtful	—	—	—	—	—	—	—	—	—
Total Consumer and other loans	\$ 2,625	\$ 1,408	\$ 395	\$ 1,505	\$ 2,222	\$ 29	\$ 2,830	\$ 11,014	
Current period gross write-offs	\$ 273	\$ 55	\$ 3	\$ 14	\$ 3	\$ 3	\$ —	\$ 351	

The following tables provide an analysis of the credit risk profile of each loan class as of December 31, 2022 (in thousands):

	December 31, 2022					March 31, 2024				
	Pass	Special Mention	Substandard	Doubtful	Total	Term Loans by Year of Origination				
Real estate loans:										
Construction and land development	\$ 50,795	\$ —	\$ 1,045	\$ —	\$ 51,840	2024	2023	2022	2021	2020
Pass						\$ 419	\$ 1,716	\$ 2,809	\$ 4,183	\$ 3,330
Special Mention						—	—	—	—	—
Substandard						—	—	—	—	37
Doubtful						—	—	—	—	—
Total Construction and land development						\$ 419	\$ 1,716	\$ 2,809	\$ 4,183	\$ 3,330
Current period gross write-offs						\$ —	\$ —	\$ 4	\$ —	\$ —
Secured by 1-4 family residential	330,590	—	831	—	331,421					
Pass						\$ 3,937	\$ 37,427	\$ 65,965	\$ 58,505	\$ 37,782
Special Mention						—	—	—	—	—
Substandard						—	89	208	—	760
Doubtful						—	—	—	—	—
Total Secured by 1-4 family residential						\$ 3,937	\$ 37,427	\$ 66,054	\$ 58,713	\$ 37,782
Current period gross write-offs						\$ —	\$ —	\$ —	\$ —	\$ 10
Other real estate loans	416,559	1,884	13	—	418,456					
Pass						\$ 2,876	\$ 49,906	\$ 94,347	\$ 92,627	\$ 40,803
Special Mention						—	—	—	—	—
Substandard						—	—	—	—	—
Doubtful						—	—	—	—	—
Total Other real estate loans						\$ 2,876	\$ 49,906	\$ 94,347	\$ 92,627	\$ 40,803
Current period gross write-offs						\$ —	\$ —	\$ —	\$ —	\$ —
Commercial and industrial	110,065	75	1,085	—	111,225					
Pass						\$ 7,403	\$ 22,279	\$ 19,892	\$ 17,278	\$ 2,449

Special Mention	—	—	1,371	—	—	—	—	—	1,371
Substandard	—	696	4,130	1,440	—	952	—	—	7,218
Doubtful	—	—	—	—	—	—	—	—	—
Total Commercial and industrial	\$ 7,403	\$ 22,975	\$ 25,393	\$ 18,718	\$ 2,449	\$ 11,317	\$ 25,307	\$ 113,562	
Current period gross write-offs	\$ —	\$ 317	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ 317
Consumer and other loans	7,581	—	—	—	7,581				
Total	\$ 915,590	\$ 1,959	\$ 2,974	\$ —	\$ 920,523				
Pass	\$ 1,951	\$ 2,427	\$ 1,027	\$ 326	\$ 1,328	\$ 2,116	\$ 4,774	\$ 13,949	
Special Mention	—	—	—	—	—	—	—	—	—
Substandard	—	—	—	—	—	—	—	—	—
Doubtful	—	—	—	—	—	—	—	—	—
Total Consumer and other loans	\$ 1,951	\$ 2,427	\$ 1,027	\$ 326	\$ 1,328	\$ 2,116	\$ 4,774	\$ 13,949	
Current period gross write-offs	\$ 70	\$ 4	\$ 6	\$ 3	\$ —	\$ —	\$ —	\$ —	83

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Notes to Consolidated Financial Statements (Unaudited)

Note 4. Allowance for Credit Losses

The following tables present, as of and during the periods ended **September 30, 2023** **March 31, 2024**, December 31, **2022** **2023** and **September 30, 2022** **March 31, 2023**, the activity in the Allowance for Credit Losses on Loans (ACLL) (previously Allowance for Loan Losses) by portfolio, and information about individually evaluated and collectively evaluated loans (in thousands):

	September 30, 2023						March 31, 2024					
	Construction and Land Development	Secured by 1-4 Family Residential	Other Real Estate	Commercial and Industrial	Consumer and Other Loans	Total	Construction and Land Development	Secured by 1-4 Family Residential	Other Real Estate	Commercial and Industrial	Consumer and Other Loans	Total
	Allowance for credit losses:											
Beginning Balance, December 31, 2022	\$ 546	\$ 1,108	\$ 3,609	\$ 1,874	\$ 309	\$ 7,446						
Adjustment to allowance for adoption of ASU 2016-13	(313)	1,409	1,702	(387)	(225)	2,186						
Beginning Balance, December 31, 2023							\$ 312	\$ 3,159	\$ 4,698	\$ 3,706	\$ 99	\$ 11,974
Charge-offs	—	—	—	(877)	(351)	(1,228)	(4)	(10)	—	(317)	(83)	(414)
Recoveries	1	13	13	145	154	326	—	4	1	6	41	52

Provision for (recovery of) credit losses	68	(97)	(179)	165	209	166						
Ending Balance, September 30, 2023	\$ 302	\$ 2,433	\$ 5,145	\$ 920	\$ 96	\$ 8,896						
Provision for (recovery of) credit losses on loans					47	(396)	225	1,098	17	991		
Ending Balance, March 31, 2024												
Ending Balance:												
Individually evaluated	—	—	—	307	—	307	—	—	3,569	—	3,569	
Collectively evaluated	302	2,433	5,145	613	96	8,589	355	2,757	4,924	924	74	9,034
Loans:												
Ending Balance	\$ 50,405	\$ 340,773	\$ 433,177	\$ 117,130	\$ 11,014	\$ 952,499	\$ 53,364	\$ 347,014	\$ 445,085	\$ 113,562	\$ 13,949	\$ 972,974
Individually evaluated	39	546	67	2,464	—	3,116	37	772	—	7,202	—	8,011
Collectively evaluated	50,366	340,227	433,110	114,666	11,014	949,383	53,327	346,242	445,085	106,360	13,949	964,963

Allowance for loan losses:	December 31, 2022						December 31, 2023					
	Construction and Land Development	Secured by 1-4 Family Residential	Other Real Estate	Commercial and Industrial	Consumer and Other Loans	Total	Construction and Land Development	Secured by 1-4 Family Residential	Other Real Estate	Commercial and Industrial	Consumer and Other Loans	Total
Beginning												
Balance, December 31, 2021	\$ 345	\$ 1,077	\$ 3,230	\$ 718	\$ 340	\$ 5,710						
Beginning												
Balance, December 31, 2022							\$ 546	\$ 1,108	\$ 3,609	\$ 1,874	\$ 309	\$ 7,446
Adjustment to allowance for adoption of ASU 2016-13							(313)	1,409	1,702	(387)	(225)	2,186
Charge-offs	—	(6)	—	(32)	(491)	(529)	—	(59)	(34)	(3,452)	(448)	(3,993)
Recoveries	10	19	15	145	226	415	—	47	14	145	212	418
Provision for (recovery of) loan losses	191	18	364	1,043	234	1,850						

Ending Balance, December 31, 2022	\$ 546	\$ 1,108	\$ 3,609	\$ 1,874	\$ 309	\$ 7,446	79	654	(593)	5,526	251	5,917
Provision for (recovery of) credit losses on loans												
Ending Balance, December 31, 2023							\$ 312	\$ 3,159	\$ 4,698	\$ 3,706	\$ 99	\$ 11,974
Ending Balance:												
Individually evaluated for impairment	—	—	—	888	—	888	—	—	—	2,705	—	2,705
Collectively evaluated for impairment	546	1,108	3,609	986	309	6,558	312	3,159	4,698	1,001	99	9,269
Loans:												
Ending Balance	\$ 51,840	\$ 331,421	\$ 418,456	\$ 111,225	\$ 7,581	\$ 920,523	\$ 52,680	\$ 344,369	\$ 447,272	\$ 113,074	\$ 12,035	\$ 969,430
Individually evaluated for impairment	1,045	530	13	1,085	—	2,673	38	495	—	6,230	—	6,763
Collectively evaluated for impairment	50,795	330,891	418,443	110,140	7,581	917,850	52,642	343,874	447,272	106,844	12,035	962,667

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Notes to Consolidated Financial Statements (Unaudited)

Allowance for loan losses:	September 30, 2022						March 31, 2023					
	Construction and Land Development	Secured by 1-4 Family Residential	Other Real Estate	Commercial and Industrial	Consumer and Other Loans	Total	Construction and Land Development	Secured by 1-4 Family Residential	Other Real Estate	Commercial and Industrial	Consumer and Other Loans	Total
	Beginning Balance, December 31, 2021	\$ 345	\$ 1,077	\$ 3,230	\$ 718	\$ 340	\$ 546	\$ 1,108	\$ 3,609	\$ 1,874	\$ 309	\$ 7,446
Beginning Balance, December 31, 2022												

Adjustment to allowance for adoption of ASU 2016-13						(313)	1,409	1,705	(391)	(224)	2,186
Charge-offs	—	(6)	—	—	(387)	(393)	—	—	—	(851)	(126)
Recoveries	10	15	12	144	194	375	—	5	2	—	55
Provision for (recovery of) loan losses	99	(22)	331	69	123	600	—	—	—	—	62
Ending Balance, September 30, 2022	\$ 454	\$ 1,064	\$ 3,573	\$ 931	\$ 270	\$ 6,292	—	—	—	—	—
Provision for (recovery of) credit losses on loans					11	74	(150)	(15)	80	—	—
Ending Balance, March 31, 2023					\$ 244	\$ 2,596	\$ 5,166	\$ 617	\$ 94	\$ 8,717	—
Ending Balance:											
Individually evaluated for impairment	—	—	—	—	—	—	—	—	—	—	—
Collectively evaluated for impairment	454	1,064	3,573	931	270	6,292	244	2,596	5,166	617	94
Loans:											
Ending Balance	\$ 51,352	\$ 317,414	\$ 417,504	\$ 112,145	\$ 8,099	\$ 906,514	\$ 48,610	\$ 334,302	\$ 416,001	\$ 110,937	\$ 8,117
Individually evaluated for impairment	—	549	17	—	—	566	1,044	474	73	—	1,591
Collectively evaluated for impairment	51,352	316,865	417,487	112,145	8,099	905,948	47,566	333,828	415,928	110,937	8,117
											916,376

Nonaccrual loans

The following is a summary of the Company's nonaccrual loans by major categories for the periods indicated (in thousands):

CECL	Incurred Loss				
	September 30, 2023	December 31, 2022	March 31, 2024	December 31, 2023	March 31, 2022

	Nonaccrual Loans with No Allowance				Nonaccrual Loans with an Allowance				Total Nonaccrual Loans				Nonaccrual Loans with No Allowance				Nonaccrual Loans with an Allowance				Total Nonaccrual Loans			
	Nonaccrual Loans with No Allowance	Nonaccrual Loans with an Allowance	Total Nonaccrual Loans	Nonaccrual Loans	Nonaccrual Loans with No Allowance	Nonaccrual Loans with an Allowance	Total Nonaccrual Loans	Nonaccrual Loans with No Allowance	Nonaccrual Loans with an Allowance	Total Nonaccrual Loans	Nonaccrual Loans with No Allowance	Nonaccrual Loans with an Allowance	Total Nonaccrual Loans	Nonaccrual Loans with No Allowance	Nonaccrual Loans with an Allowance	Total Nonaccrual Loans	Nonaccrual Loans with No Allowance	Nonaccrual Loans with an Allowance	Total Nonaccrual Loans	Nonaccrual Loans with No Allowance	Nonaccrual Loans with an Allowance	Total Nonaccrual Loans		
Real estate loans:																								
Construction and land development	\$ 39	\$ —	\$ 39	\$ 1,045	\$ 37	\$ —	\$ 37	\$ 38	\$ —	\$ 38	\$ 38	\$ 1,044	\$ —											
Secured by 1-4 family residential	546	—	546	530	775	—	775	495	—	495	—	474	—											
Other real estate loans	67	—	67	13	—	—	—	—	—	—	—	73	—											
Commercial and industrial	—	2,464	2,464	1,085	—	7,203	7,203	—	6,230	6,230	—	—	—											
Total	\$ 652	\$ 2,464	\$ 3,116	\$ 2,673	\$ 812	\$ 7,203	\$ 8,015	\$ 533	\$ 6,230	\$ 6,763	\$ 1,591	\$ —												

Prior to the adoption of ASU 2016-13, loans were considered impaired when, based on current information and events, it was probable the Company would be unable to collect all amounts due in accordance with the original contractual terms of the loan agreements. Impaired loans included loans on nonaccrual status and accruing troubled debt restructurings. When determining if the Company would be unable to collect all principal and interest payments due in accordance with the contractual terms of the loan agreement, the Company considered the borrower's capacity to pay, which included such factors as the borrower's current financial statements, an analysis of global cash flow sufficient to pay all debt obligations and an evaluation of secondary sources of repayment, such as guarantor support and collateral value. The Company individually assessed for impairment all nonaccrual loans and troubled debt restructurings. The tables below include information on all loans deemed impaired. Interest payments on impaired loans were typically applied to principal unless collectability of the principal amount was reasonably assured, in which case interest was recognized on a cash basis.

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Notes to Consolidated Financial Statements (Unaudited)

Impaired loans and the related allowance as of and for the periods ended December 31, 2022 and September 30, 2022, were as follows (in thousands):

	December 31, 2022																							
	Unpaid Principal Balance			Recorded Investment with No Allowance			Recorded Investment with Allowance			Total Recorded Investment			Related Allowance			Average Recorded Investment			Interest Income Recognized					
	Real estate loans:																							
Construction and land development	\$ 2,412	\$ 1,045	\$ —	\$ 1,045	\$ 1,045	\$ —	\$ 1,045	\$ 1,045	\$ —	\$ 30	\$ 75													
Secured by 1-4 family residential	680	530	—	530	—	—	530	530	—	580	11													
Other real estate loans	26	13	—	13	—	—	13	13	—	22	—													
Commercial and industrial	1,084	—	1,085	1,085	1,085	1,085	888	888	650	40														
Total	\$ 4,202	\$ 1,588	\$ 1,085	\$ 2,673	\$ 888	\$ 888	\$ 1,282	\$ 1,282	\$ 126															
September 30, 2022																								
			Unpaid Principal Balance			Recorded Investment with No Allowance			Recorded Investment with Allowance			Total Recorded Investment			Related Allowance			Average Recorded Investment			Interest Income Recognized			
Real estate loans:																								
Secured by 1-4 family residential	\$ 560	\$ 549	\$ —	\$ 549	\$ —	\$ 549	\$ —	\$ 549	\$ —	\$ 593	\$ 11													
Other real estate loans	29	17	—	17	—	17	—	17	—	24	—													
Commercial and industrial	—	—	—	—	—	—	—	—	—	823	—													

Total	\$ 589	\$ 566	\$ —	\$ 566	\$ —	\$ 1,440	\$ 11
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The "Recorded Investment" amounts in the table above represent the outstanding principal balance on each loan represented in the table. The "Unpaid Principal Balance"

represents the outstanding principal balance on each loan represented in the table plus any amounts that have been charged off on each loan and/or payments that have been applied towards principal on non-accrual loans. Only loan classes with balances are included in the tables above.

As of December 31, 2022, loans classified as TDRs and included in impaired loans in the disclosure above totaled \$101 thousand. At December 31, 2022, none of the loans classified as TDRs were performing under the restructured terms and all were considered non-performing assets. Modified terms under TDRs included rate reductions, extension of terms that are considered to be below market, conversion to interest only, and other actions intended to minimize the economic loss and to avoid foreclosure or repossession of the collateral.

For the nine months ended September 30, 2023 and 2022, there were no TDRs that subsequently defaulted within twelve months of the loan modification. Management defines default as over ninety days past due or the foreclosure and repossession of the collateral or charge-off of the loan during the twelve month period subsequent to the modification.

Collateral-Dependent Loans

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

- Commercial real estate loans can be secured by either owner occupied commercial real estate or non-owner occupied investment commercial real estate. Typically, owner occupied commercial real estate loans are secured by office buildings, warehouses, manufacturing facilities and other commercial and industrial properties occupied by operating companies. Non-owner occupied commercial real estate loans are generally secured by office buildings and complexes, retail facilities, multifamily complexes, land under development, industrial properties, as well as other commercial or industrial real estate.
- Residential real estate loans are typically secured by first mortgages, and in some cases could be secured by a second mortgage.
- Home equity lines of credit are generally secured by second mortgages on residential real estate property.
- Consumer loans are generally secured by automobiles, motorcycles, recreational vehicles and other personal property. Some consumer loans are unsecured and have no underlying collateral.

The following table presents the amortized cost of collateral-dependent loans (in thousands):

(Dollars in thousands)	September 30, 2023			March 31, 2024			December 31, 2023			March 31, 2023		
	Real Estate Secured	Non-Real Estate Secured	Total Collateral- Dependent Loans	Real Estate Secured	Non- Real Estate Secured	Total Collateral- Dependent Loans	Real Estate Secured	Non- Real Estate Secured	Total Collateral- Dependent Loans	Real Estate Secured	Non- Real Estate Secured	Total Collateral- Dependent Loans
	Real estate loans:											
Construction and land development	\$ 39	\$ —	\$ 39	\$ 37	\$ —	\$ 37	\$ 38	\$ —	\$ 38	\$ 1,044	\$ —	\$ 1,044
Secured by 1-4 family residential	546	—	546	775	—	775	495	—	495	474	—	474
Other real estate loans	67	—	67	—	—	—	—	—	—	73	—	73
Commercial and industrial	—	2,464	2,464	—	—	—	—	—	—	—	—	—
Total	\$ 652	\$ 2,464	\$ 3,116	\$ 812	\$ —	\$ 812	\$ 533	\$ —	\$ 533	\$ 1,591	\$ —	\$ 1,591

At September 30, March 31, 2024 and 2023, there was an allowance/no allowance for credit losses of \$307 thousand on collateral-dependent loans.

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Notes to Consolidated Financial Statements (Unaudited)

Modifications Made to Borrowers Experiencing Financial Difficulty

The allowance for credit losses incorporates an estimate of lifetime expected credit losses and is recorded on each asset upon asset origination or acquisition. The starting point for the estimate of the allowance for credit losses is historical loss information, which includes losses from modifications of receivables to borrowers experiencing financial difficulty. The Company uses a probability of default/loss given default model to determine the allowance for credit losses. An assessment of whether a borrower is experiencing financial difficulty is made on the date of a modification.

Because the effect of most modifications made to borrowers experiencing financial difficulty is already included in the allowance for credit losses because of the measurement methodologies used to estimate the allowance, a change to the allowance for credit losses is generally not recorded upon modification. Occasionally, the Company modifies loans by providing principal forgiveness on certain of its real estate loans. When principal forgiveness is provided, the amortized cost basis of the asset is written off against the allowance for credit losses. The amount of the principal forgiveness is deemed to be uncollectible; therefore, that portion of the loan is written off, resulting in a reduction of the amortized cost basis and a corresponding adjustment to the allowance for credit losses.

In some cases, the Company will modify a certain loan by providing multiple types of concessions. Typically, one type of concession, such as a term extension, is granted initially. If the borrower continues to experience financial difficulty, another concession, such as principal forgiveness, may be granted. For the real estate loans included in the "combination" columns below, multiple types of modifications have been made on the same loan within the current reporting period. The combination is at least two of the following: a term extension, principal forgiveness, and interest rate reduction.

The following table shows For the amortized cost basis as of September 30, 2023 three of the months ended March 31, 2024, there were no loans modified to borrowers experiencing financial difficulty, disaggregated by class of loans and type of concession granted and describes the financial effect of the modifications made to borrowers experiencing financial difficulty.

Term Extension			
(Dollars in thousands)	Amortized Cost Basis	% of Total Loan Type	Financial Effect
Real estate loans:			
Construction and land development	\$ —	0.00 %	
Secured by 1-4 family residential	64	0.02 %	Converted HELOC to 15 year term loan.
Other real estate loans	—	0.00 %	
Commercial and industrial	2,464	2.10 %	Decrease in loan payment
Total	\$ 2,528	2.12 %	
Principal Forgiveness			
(Dollars in thousands)	Amortized Cost Basis	% of Total Loan Type	Financial Effect
Real estate loans:			
Construction and land development	\$ —	0.00 %	
Secured by 1-4 family residential	17	0.01 %	Reduced the amortized cost basis of the loan by \$29 thousand.
Other real estate loans	—	0.00 %	
Commercial and industrial	—	0.00 %	
Total	\$ 17	0.01 %	

Upon the Company's determination that a modified loan (or portion of a loan) has subsequently been deemed uncollectible, the loan (or a portion of the loan) is written off. Therefore, the amortized cost basis of the loan is reduced by the uncollectible amount and the allowance for credit losses is adjusted by the same amount. For the nine three months ended September 30, 2023 March 31, 2024 and 2022 2023, there were no payment defaults of modified loans that were modified during the previous twelve months. At September 30, March 31, 2024 and 2023, there was an was no allowance for credit losses of \$307 thousand on modified loans.

Unfunded Commitments

The Company maintains a separate reserve for credit losses on off-balance-sheet credit exposures, including unfunded loan commitments, which is included in other liabilities on the consolidated balance sheet. The reserve for credit losses on off-balance-sheet credit exposures is adjusted as a provision for credit losses in the income statement. The estimate includes consideration of the likelihood that funding will occur and an estimate of expected credit losses on commitments expected to be funded over its estimated life, utilizing the same models and approaches for the Company's other loan portfolio segments described in Note 1, as these unfunded commitments share similar risk characteristics as its loan portfolio segments. The Company has identified the unfunded portion of certain lines of credit as unconditionally cancellable credit exposures, meaning the Company can cancel the unfunded commitment at any time. No credit loss estimate is reported for off-balance-sheet credit exposures that are unconditionally cancellable by the Company or for undrawn amounts under such arrangements that may be drawn prior to the cancellation of the arrangement.

There was no provision for credit losses on unfunded commitments during the first quarter of 2024. On January 1, 2023, the Company recorded an adjustment for unfunded commitments of \$153 thousand for the adoption of ASC Topic 326. For the three months ended **September 30, 2023**, the Company recorded a recovery of provision for credit losses for unfunded commitments of \$8 thousand. At September 30, 2023, the liability commitments. The allowance for credit losses on off-balance-sheet off-balance sheet exposures included in other liabilities was \$189 thousand. \$413 and \$153 thousand at March 31, 2024 and 2023, respectively.

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Notes to Consolidated Financial Statements (Unaudited)

Note 5. Earnings per Common Share

Basic earnings per common share represents income available to common shareholders divided by the weighted-average number of common shares outstanding during the period. Diluted earnings per common share reflects additional common shares that would have been outstanding if dilutive potential common shares had been issued, as well as any adjustment to income that would result from the assumed issuance.

The following table presents the computation of basic and diluted earnings per share for the three and **nine** months ended **September 30, 2023** **March 31, 2024** and **2022** (dollars in thousands, except per share data):

	Three Months Ended		Nine Months Ended		Three Months Ended	
	September 30, 2023	September 30, 2022	September 30, 2023	September 30, 2022	March 31, 2024	March 31, 2023
(Numerator):						
Net income	\$ 3,121	\$ 4,454	\$ 10,475	\$ 12,018	\$ 3,209	\$ 3,849
(Denominator):						
Weighted average shares outstanding – basic	6,256,663	6,257,040	6,266,707	6,248,847	6,269,790	6,273,913
Potentially dilutive common shares – restricted stock units	14,688	7,067	9,795	6,121	12,744	7,203
Weighted average shares outstanding – diluted	6,271,351	6,264,107	6,276,502	6,254,968	6,282,534	6,281,116
Income per common share						
Basic	\$ 0.50	\$ 0.71	\$ 1.67	\$ 1.92	\$ 0.51	\$ 0.61
Diluted	\$ 0.50	\$ 0.71	\$ 1.67	\$ 1.92	\$ 0.51	\$ 0.61

Restricted stock units for **603,882** shares of common stock were not considered in computing diluted earnings per share for the three and **nine** months ended **September 30, 2023** **March 31, 2024** because they were antidilutive. There were no antidilutive shares of common stock for the three and **nine** months ended **September 30, 2023** and **2022**, **March 31, 2024**.

Note 6. Fair Value Measurements

Determination of Fair Value

The Company uses fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. In accordance with the "Fair Value Measurement and Disclosures" topic of FASB ASC, the fair value of a financial instrument is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value is best determined based upon quoted market prices. However, in many instances, there are 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. Accordingly, the fair value estimates may not be realized in an immediate settlement of the instrument.

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

Fair Value Hierarchy

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

- Level 1 - Valuation is based on quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date. Level 1 assets and liabilities generally include debt and equity securities that are traded in an active exchange market. Valuations are obtained from readily available pricing sources for market transactions involving identical assets or liabilities.
- Level 2 - Valuation is based on inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. The valuation may be based on quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the asset or liability.
- Level 3 - Valuation is based on unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which determination of fair value requires a significant management judgment or estimation.

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

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Notes to Consolidated Financial Statements (Unaudited)

The following describes the valuation techniques used by the Company to measure certain assets recorded at fair value on a recurring basis in the financial statements:

Securities available for sale

Securities available for sale are recorded at fair value on a recurring basis. Fair value measurement is based upon quoted market prices, when available (Level 1). If quoted market prices are not available, fair values are measured utilizing independent valuation techniques of identical or similar securities for which significant assumptions are derived primarily from or corroborated by observable market data. Third party vendors compile prices from various sources and may determine the fair value of identical or similar securities by using pricing models that consider observable market data (Level 2).

Derivative asset/liability - cash flow hedges

Cash flow hedges are recorded at fair value on a recurring basis. The fair value of the Company's cash flow hedges is determined by a third party vendor using the discounted cash flow method (Level 2).

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Notes to Consolidated Financial Statements (Unaudited)

The following tables present the balances of assets measured at fair value on a recurring basis as of September 30, 2023 March 31, 2024 and December 31, 2022 2023 (in thousands).

Description	Fair Value Measurements at September 30, 2023				Fair Value Measurements at March 31, 2024			
	Balance as of September 30, 2023	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance as of March 31, 2024	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:								
Securities available for sale								

U.S. Treasury securities	\$ 11,113	\$ —	\$ 11,113	\$ —	\$ 11,399	\$ —	\$ 11,399	\$ —
U.S. agency and mortgage-backed securities	84,294	—	84,294	—	80,968	—	80,968	—
Obligations of states and political subdivisions	52,768	—	52,768	—	55,308	—	55,308	—
Total securities available for sale	\$ 148,175	\$ —	\$ 148,175	\$ —	\$ 147,675	\$ —	\$ 147,675	\$ —
Derivatives - cash flow hedges	3,065	—	3,065	—	2,672	—	2,672	—
Total assets	\$ 151,240	\$ —	\$ 151,240	\$ —	\$ 150,347	\$ —	\$ 150,347	\$ —

Description	Fair Value Measurements at December 31, 2022						Fair Value Measurements at December 31, 2023					
	Quoted Prices in Active Markets for Identical Assets (Level 1)			Significant Other Observable Inputs (Level 2)			Quoted Prices in Active Markets for Identical Assets (Level 1)			Significant Other Observable Inputs (Level 2)		
	Balance as of December 31, 2022			Balance as of December 31, 2023			Balance as of December 31, 2023			Balance as of December 31, 2023		
Assets:												
Securities available for sale												
U.S. Treasury securities	\$ 11,229	\$ —	\$ 11,229	\$ —	\$ 11,450	\$ —	\$ 11,450	\$ —	\$ 11,450	\$ —	\$ 11,450	\$ —
U.S. agency and mortgage-backed securities	96,918	—	96,918	—	84,800	—	84,800	—	84,800	—	84,800	—
Obligations of states and political subdivisions	54,760	—	54,760	—	56,607	—	56,607	—	56,607	—	56,607	—
Total securities available for sale	\$ 162,907	\$ —	\$ 162,907	\$ —	\$ 152,857	\$ —	\$ 152,857	\$ —	\$ 152,857	\$ —	\$ 152,857	\$ —
Derivatives - cash flow hedges	2,679	—	2,679	—	2,488	—	2,488	—	2,488	—	2,488	—
Total assets	\$ 165,586	\$ —	\$ 165,586	\$ —	\$ 155,345	\$ —	\$ 155,345	\$ —	\$ 155,345	\$ —	\$ 155,345	\$ —

Certain assets are measured at fair value on a nonrecurring basis in accordance with GAAP. Adjustments to the fair value of these assets usually result from the application of lower-of-cost-or-market accounting or write-downs of individual assets.

The following describes the valuation techniques used by the Company to measure certain assets recorded at fair value on a nonrecurring basis in the financial statements:

Collateral Dependent Loans with an ACLL

In accordance with ASC 326, the Company may determine that an individual loan exhibits unique risk characteristics which differentiate it from other loans within our loan pools. In such cases, the loans are evaluated for expected credit losses on an individual basis and excluded from the collective evaluation. Specific allocations of the allowance for credit losses are determined by analyzing the borrower's ability to repay amounts owed, collateral deficiencies, the relative risk grade of the loan and economic conditions affecting the borrower's industry, among other things. A loan is considered to be collateral dependent when, based upon management's assessment, the borrower is experiencing financial difficulty and repayment is expected to be provided substantially through the operation or sale of the collateral. In such cases, expected credit losses are based on the fair value of the collateral at the measurement date, adjusted for estimated selling costs if satisfaction of the loan depends on the sale of the collateral. We reevaluate the fair value of collateral supporting collateral dependent loans on a quarterly basis. The fair value of real estate collateral supporting collateral dependent loans is evaluated by appraisal services using a methodology that is consistent with the Uniform Standards of Professional Appraisal Practice. There was no allowance for credit losses on collateral dependent loans at **September 30, 2023** **March 31, 2024**.

Other Real Estate Owned

Certain assets such as OREO are measured at fair value less cost to sell. Valuation of OREO is determined using current appraisals from independent parties, a Level 2 input. If current appraisals cannot be obtained prior to reporting dates, or if declines in value are identified after a recent appraisal is received, appraisal values are discounted, resulting in Level 3 estimates. If the Company markets the property with a realtor, estimated selling costs reduce the fair value, resulting in a valuation based on Level 3 inputs.

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Notes to Consolidated Financial Statements (Unaudited)

The following tables summarize the Company's assets that were measured at fair value on a nonrecurring basis during the periods (dollars in thousands):

Description	Fair Value Measurements at September 30, 2023						Fair Value Measurements at March 31, 2024					
	Quoted Prices in Active Markets for Identical Assets (Level 1)			Significant Other Observable Inputs (Level 2)			Quoted Prices in Active Markets for Identical Assets (Level 1)			Significant Other Observable Inputs (Level 2)		
	Balance as of September 30, 2023	Markets for Identical Assets (Level 1)	Significant Inputs (Level 2)	Balance as of March 31, 2024	Markets for Identical Assets (Level 1)	Significant Inputs (Level 2)	Balance as of September 30, 2023	Markets for Identical Assets (Level 1)	Significant Inputs (Level 2)	Balance as of March 31, 2024	Markets for Identical Assets (Level 1)	Significant Inputs (Level 2)
	Assets (Level 1)	2)	Inputs (Level 2)	Assets (Level 1)	2)	Inputs (Level 2)	Assets (Level 1)	2)	Inputs (Level 2)	Assets (Level 1)	2)	Inputs (Level 2)
Collateral dependent loans	\$ 3,116	\$ —	\$ —	\$ 3,116	\$ 812	\$ —	\$ —	\$ —	\$ —	\$ 812	\$ —	\$ —

Description	Fair Value Measurements at December 31, 2022					
	Quoted Prices in Active Markets for Identical Assets (Level 1)					
	Balance as of December 31, 2022		Significant Other Observable Inputs (Level 2)		Significant Unobservable Inputs (Level 3)	
	\$ 184	\$ —	\$ —	\$ —	\$ 184	\$ —
Other real estate owned	\$ 184	\$ —	\$ —	\$ —	\$ 184	\$ —
Impaired loans, net	197	—	—	—	197	—

Description	Fair Value Measurements at December 31, 2023					
	Quoted Prices in Active Markets for Identical Assets (Level 1)					
	Balance as of December 31, 2023		Significant Other Observable Inputs (Level 2)		Significant Unobservable Inputs (Level 3)	
	\$ 533	\$ —	\$ —	\$ —	\$ 533	\$ —
Collateral dependent loans	\$ 533	\$ —	\$ —	\$ —	\$ 533	\$ —

Description	Quantitative information about Level 3 Fair Value Measurements for September 30, 2023					
	Fair Value				Valuation Technique	
	Fair Value		Valuation Technique		Unobservable Input	
	\$ 3,116	\$ —	Property appraisals	Selling cost	\$ —	6.00 %
Collateral dependent loans	\$ 3,116	\$ —	Property appraisals	Selling cost	\$ —	6.00 %

Description	Quantitative information about Level 3 Fair Value Measurements for March 31, 2024					
	Fair Value				Valuation Technique	
	Fair Value		Valuation Technique		Unobservable Input	
	\$ 812	\$ —	Present value of cash flows	Discount rate	\$ —	6.50 %
Collateral dependent loans	\$ 812	\$ —	Present value of cash flows	Discount rate	\$ —	6.50 %

Description	Quantitative information about Level 3 Fair Value Measurements for December 31, 2022					
	Fair Value				Valuation Technique	
	Fair Value		Valuation Technique		Unobservable Input	
	\$ 184	\$ —	Property appraisals	Selling cost	\$ —	10.00 %
Other real estate owned	\$ 184	\$ —	Property appraisals	Selling cost	\$ —	10.00 %

	Present value of cash flows	Discount rate	6.50%
Impaired loans, net	197		

	Quantitative information about Level 3 Fair Value Measurements for December 31, 2023				
	Fair Value	Valuation Technique	Unobservable Input	Range (Weighted Average) (1)	
				Present value of cash flows	Discount rate
Collateral dependent loans	\$ 533				6.50 %

(1) Unobservable inputs were weighted by the relative fair value of the instruments.

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Notes to Consolidated Financial Statements (Unaudited)

Accounting guidance requires disclosure of the fair value of financial assets and financial liabilities, including those financial assets and financial liabilities that are not measured and reported at fair value on a recurring basis or non-recurring basis. The carrying values and estimated fair values of the Company's financial instruments at **September 30, 2023** **March 31, 2024** and December 31, **2022** **2023** are as follows (in thousands):

	Fair Value Measurements at September 30, 2023 Using						Fair Value Measurements at March 31, 2024 Using						
	Carrying Amount	Quoted Prices in Active Markets for Identical Assets Level 1	Significant Other Observable Inputs Level 2		Significant Unobservable Inputs Level 3		Fair Value	Carrying Amount	Quoted Prices in Active Markets for Identical Assets Level 1	Significant Other Observable Inputs Level 2		Significant Unobservable Inputs Level 3	
			Significant Observable Inputs Level 2	Significant Unobservable Inputs Level 3	Significant Observable Inputs Level 2	Significant Unobservable Inputs Level 3				Significant Observable Inputs Level 2	Significant Unobservable Inputs Level 3	Significant Observable Inputs Level 2	Significant Unobservable Inputs Level 3
Financial Assets													
Cash and interest-bearing deposits in banks	\$ 50,099	\$ 50,099	\$ —	\$ —	\$ 50,099	\$ 138,709	\$ 138,709	\$ —	\$ —	\$ —	\$ —	\$ 138,709	
Securities available for sale	148,175	—	148,175	—	148,175	147,675	—	147,675	—	—	—	147,675	
Securities held to maturity, net	149,948	—	134,728	—	134,728	125,825	—	113,973	—	—	—	113,973	
Securities held to maturity													
Restricted securities	2,077	—	2,077	—	2,077	2,112	—	2,112	—	—	—	2,112	
Loans, net	943,603	—	—	901,921	901,921	960,371	—	—	922,604	—	922,604	922,604	
Bank owned life insurance	24,734	—	24,734	—	24,734	24,652	—	24,652	—	—	—	24,652	
Accrued interest receivable	4,502	—	4,502	—	4,502	4,978	—	4,978	—	—	—	4,978	
Derivatives - cash flow hedges	3,065	—	3,065	—	3,065	2,672	—	2,672	—	—	—	2,672	
Financial Liabilities													
Deposits	\$ 1,235,173	\$ —	1,050,754	\$ 179,959	\$ 1,230,713	\$ 1,259,137	\$ —	1,061,550	\$ 194,320	\$ 1,255,870	\$ 49,816	\$ 49,816	
Other borrowings							\$ 50,000	—	—	—	—	—	
Subordinated debt	4,997	—	—	5,161	5,161	4,998	—	—	5,487	—	5,487	5,487	
Junior subordinated debt	9,279	—	—	6,290	6,290	9,279	—	—	8,141	—	8,141	8,141	
Accrued interest payable	667	—	667	—	667	864	—	864	—	—	—	864	
Fair Value Measurements at December 31, 2022 Using						Fair Value Measurements at December 31, 2023 Using							

	Quoted Prices in Active Markets for Identical Assets						Quoted Prices in Active Markets for Identical Assets					
	Carrying Amount	Significant Other Observable Inputs Level 2	Significant Unobservable Inputs Level 3			Fair Value	Carrying Amount	Significant Other Observable Inputs Level 2	Significant Unobservable Inputs Level 3			Fair Value
			Level 1	Level 1	Level 1				Level 1	Level 1	Level 1	
Financial Assets												
Cash and interest-bearing deposits in banks	\$ 66,914	\$ 66,914	\$ —	\$ —	\$ 66,914	\$ 87,161	\$ 87,161	\$ —	\$ —	\$ —	\$ 87,161	
Securities available for sale	162,907	—	162,907	—	162,907	152,857	—	152,857	—	—	152,857	
Securities held to maturity, net	153,158	—	141,797	—	141,797							
Securities held to maturity						148,244	—	137,507	—	—	137,507	
Restricted securities	1,908	—	1,908	—	1,908	2,078	—	2,078	—	—	2,078	
Loans, net	913,077	—	—	880,473	880,473	957,456	—	—	919,266	—	919,266	
Bank owned life insurance	24,531	—	24,531	—	24,531	24,902	—	24,902	—	—	24,902	
Accrued interest receivable	4,543	—	4,543	—	4,543	4,655	—	4,655	—	—	4,655	
Derivatives - cash flow hedges	2,679	—	2,679	—	2,679	2,488	—	2,488	—	—	2,488	
Financial Liabilities												
Deposits	\$ 1,241,332	\$ —	\$ 1,104,483	\$ 131,304	\$ 1,235,787	\$ 1,233,726	\$ —	\$ 1,041,377	\$ 189,354	\$ 1,230,731		
Other borrowings						50,000	—	—	49,987	—	49,987	
Subordinated debt	4,995	—	—	5,267	5,267	4,997	—	—	5,412	—	5,412	
Junior subordinated debt	9,279	—	—	6,067	6,067	9,279	—	—	8,493	—	8,493	
Accrued interest payable	163	—	163	—	163	764	—	764	—	—	764	

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Notes to Consolidated Financial Statements (Unaudited)

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

Note 7. Stock Compensation Plans

On May 10, 2023, the Company's shareholders approved the First National Corporation 2023 Stock Incentive Plan, which replaced the 2014 Stock Incentive Plan and makes available up to 325,000 shares of common stock for the granting of stock options, restricted stock awards, restricted stock units, stock appreciation rights, and other stock-based awards. Beginning on May 11, 2023, new equity awards granted by the Company are from the 2023 Stock Incentive Plan and not from the 2014 Stock Incentive Plan. Awards are made at the discretion of the Board of Directors and compensation cost equal to the fair value of the award is recognized over the vesting period.

Stock Awards

Whenever the Company deems it appropriate to grant a stock award, the recipient receives a specified number of unrestricted shares of employer stock. Stock awards may be made by the Company at its discretion without cash consideration and may be granted as settlement of a performance-based compensation award.

There was no compensation expense related to stock awards totaled \$202 thousand and \$402 thousand for the three months and nine months ended September 30, 2023 March 31, 2024, respectively. Compensation expense related to stock awards totaled \$130 thousand and \$481 thousand for the three months and nine months ended September 30, 2022 March 31, 2023, respectively.

Restricted Stock Units

Restricted stock units are an award of units that correspond in number and value to a specified number of shares of employer stock which the recipient receives according to a vesting plan and distribution schedule after achieving required performance milestones or upon remaining with the employer for a particular length of time. Each restricted stock unit that vests entitles the recipient to receive one share of common stock on a specified issuance date.

During the first quarter of 2023 2024, 13,727 13,412 restricted stock units were granted to employees, with 4,580 4,475 units vesting immediately, on February 15, 2024, and 9,147 8,937 units subject to a two year vesting schedule with one half of the units vesting each year. During the second quarter of 2023, 10,000 restricted stock units were granted to employees, with 4,000 units vesting in February 2025, and 6,000 units subject to a three-year vesting schedule beginning in February 2026 with one third of the units vesting each year. The recipient does not have any stockholder rights, including voting, dividend, or liquidation rights, with respect to the shares underlying awarded restricted stock units until vesting has occurred and the recipient becomes the record holder of those shares. The unvested restricted stock units will vest on the established schedule if the employees remain employed by the Company on future vesting dates.

A summary of the activity for the Company's restricted stock units for the period indicated is presented in the following table:

	Nine Months Ended September 30, 2023		Three Months Ended March 31, 2024	
	Shares	Weighted Average Grant Date Fair Value	Shares	Weighted Average Grant Date Fair Value
Unvested, beginning of year	29,181	\$ 20.31	41,507	\$ 18.47
Granted	23,727	16.56	13,412	19.06
Vested	(11,401)	19.20	(17,762)	19.59
Forfeited	—	—	—	—
Unvested, end of period	41,507	\$ 18.47	37,157	\$ 18.25

At September 30, 2023 March 31, 2024, based on restricted stock unit awards outstanding at that time, the total unrecognized pre-tax compensation expense related to unvested restricted stock unit awards was \$422 \$464 thousand. This expense is expected to be recognized through 2028. Compensation expense related to restricted stock unit awards recognized for the three months ended September 30, 2023 March 31, 2024 and 2022 2023 totaled \$72 \$142 thousand and \$56 thousand, respectively. Compensation expense related to restricted stock unit awards recognized for the nine months ended September 30, 2023 and 2022 totaled \$279 thousand and \$247 \$138 thousand, respectively.

On May 11, 2023, the Company's shareholders approved the First National Corporation 2023 Stock Incentive Plan, which makes available up to 325,000 shares of common stock for the granting of stock options, restricted stock awards, stock appreciation rights, and other stock-based awards. Awards are made at the discretion of the Board of Directors and compensation cost is equal to the fair value of the award and recognized over the vesting period.

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Notes to Consolidated Financial Statements (Unaudited)

Note 8. Accumulated Other Comprehensive Income (Loss)

Changes in each component of accumulated other comprehensive income (loss) were as follows (in thousands):

	Net Unrealized Gains (Losses) on Securities	Change in Fair Value of Cash Flow Hedges	Accumulated Other Comprehensive Income (Loss)
Balance at June 30, 2022	\$ (24,450)	\$ 1,748	\$ (22,702)
Unrealized holding losses (net of tax, \$155)	581	—	581
Unrealized holding losses transferred from available for sale to held to maturity (net of tax and amortization of (\$1,605) and (\$157), respectively)	(6,036)	—	(6,036)
Change in fair value of cash flow hedge (net of tax, \$106)	—	404	404

Change during period	(5,455)	404	(5,051)
Balance at September 30, 2022	\$ (29,905)	\$ 2,152	\$ (27,753)
Balance at June 30, 2023	\$ (23,355)	\$ 1,996	\$ (21,359)
Unrealized holding losses (net of tax, (\$1,080))	(4,063)	—	(4,063)
Amortization of unrealized holding losses on available-for-sale securities transferred to held to maturity (net of tax of \$86)	323	—	323
Change in fair value of cash flow hedge (net of tax, \$113)	—	424	424
Change during period	(3,740)	424	(3,316)
Balance at September 30, 2023	\$ (27,095)	\$ 2,420	\$ (24,675)
			Accumulated Other
	Net Unrealized (Losses) on Securities	Change in Fair Value of Cash Flow Hedges	Comprehensive Income (Loss)
Balance at December 31, 2021	\$ (445)	\$ 743	\$ 298
Unrealized holding losses (net of tax, (\$6,225))	(23,424)	—	(23,424)
Unrealized holding losses transferred from available for sale to held to maturity (net of tax and amortization of (\$1,605) and (\$157), respectively)	(6,036)	—	(6,036)
Change in fair value of cash flow hedge (net of tax, \$373)	—	1,409	1,409
Change during period	(29,460)	1,409	(28,051)
Balance at September 30, 2022	\$ (29,905)	\$ 2,152	\$ (27,753)
Balance at December 31, 2022	\$ (24,587)	\$ 2,116	\$ (22,471)
Unrealized holding losses (net of tax, (\$925))	(3,480)	—	(3,480)
Amortization of unrealized holding losses on available-for-sale securities transferred to held to maturity (net of tax of \$258)	972	—	972
Change in fair value of cash flow hedge (net of tax, \$82)	—	304	304
Change during period	(2,508)	304	(2,204)
Balance at September 30, 2023	\$ (27,095)	\$ 2,420	\$ (24,675)

	Net Unrealized Gains (Losses) on Securities	Change in Fair Value of Cash Flow Hedges	Accumulated Other Comprehensive Income (Loss)
Balance at December 31, 2022	\$ (24,587)	\$ 2,116	\$ (22,471)
Unrealized holding losses (net of tax, \$576)	2,162	—	2,162
Amortization of unrealized holding losses on available-for-sale securities transferred to held to maturity (net of tax of \$84)	316	—	316
Change in fair value of cash flow hedge (net of tax, (\$60))	—	(223)	(223)
Change during period	2,478	(223)	2,255
Balance at March 31, 2023	\$ (22,109)	\$ 1,893	\$ (20,216)
Balance at December 31, 2023	\$ (20,671)	\$ 1,965	\$ (18,706)
Unrealized holding losses (net of tax, (\$332))	(1,246)	—	(1,246)
Amortization of unrealized holding losses on available-for-sale securities transferred to held to maturity (net of tax of \$77)	290	—	290
Change in fair value of cash flow hedge (net of tax, \$38)	—	145	145
Change during period	(956)	145	(811)
Balance at March 31, 2024	\$ (21,627)	\$ 2,110	\$ (19,517)

Note 9. Revenue Recognition

Most revenue associated with financial instruments, including interest income, loan origination fees, and credit card fees, is outside the scope of ASC topic 606. Gains and losses on investment securities, derivatives, financial guarantees, and sales of financial instruments are similarly excluded from the scope. The guidance is applicable to noninterest revenue streams such as service charges on deposit accounts, ATM and check card fees, wealth management fees, and fees for other customer services. Noninterest revenue streams within the scope of Topic 606 are discussed below.

Service charges on deposit accounts

Service charges on deposit accounts consist of monthly service fees, overdraft and nonsufficient funds fees, and other deposit account related fees. The Company's performance obligation for monthly service fees is generally satisfied, and the related revenue recognized, over the period in which the service is provided. Payment for service charges on deposit accounts is primarily received immediately or in the following month through a direct charge to customers' accounts. Overdraft and nonsufficient funds fees and other deposit account related fees are transactional based, and therefore, the Company's performance obligation is satisfied, and related revenue recognized, at a point in time.

ATM and check card fees

ATM fees are primarily generated when a Company cardholder uses a non-Company ATM or a non-Company cardholder uses a Company ATM. ATM fees are transactional based, and therefore, the Company's performance obligation is satisfied, and related revenue recognized, at a point in time. Check card fees are primarily comprised of interchange fee income. Interchange fees are earned whenever the Company's debit cards are processed through card payment networks, such as Visa. The Company's performance obligation for interchange fee income is largely satisfied, and related revenue recognized, when the services are rendered or upon completion. Payment is typically received immediately or in the following month.

Wealth management fees

Wealth management fees are primarily comprised of fees earned from the management and administration of trusts and other customer assets. The Company's performance obligation is generally satisfied over time and the resulting fees are primarily recognized monthly, based upon the month-end market value of the assets under management and the applicable fee rate. Payment is generally received a few days after month-end through a direct charge to customers' accounts. Estate management fees are based upon the size of the estate. Revenue for estate management fees are recorded periodically, according to a fee schedule, and are based on the services that have been provided.

Brokered mortgage fees

Brokered mortgage fees are comprised of loan fee income earned from generating loans in the secondary market. Brokered mortgage fee income is recognized at loan closing.

Fees for other customer services

Fees for other customer services include fees for brokered loans, check ordering charges, merchant services income, safe deposit box rental fees, and other service charges. Check ordering charges are transactional based, and therefore, the Company's performance obligation is satisfied, and related revenue recognized, at a point in time. Merchant services income mainly represent fees charged to merchants to process their debit and credit card transactions. The Company's performance obligation for merchant services income is largely satisfied, and related revenue recognized, when the services are rendered or upon completion. Payment is typically received immediately or in the following month. Safe deposit box rental fees are charged to the customer on an annual basis and recognized upon receipt of payment. The Company determined that since rentals and renewals occur fairly consistently over time, revenue is recognized on a basis consistent with the duration of the performance obligation.

The following table presents noninterest income, segregated by revenue streams in-scope and out-of-scope of Accounting Standards Codification Topic 606, for the three and ~~nine~~ three months ended ~~September 30, 2023~~ ~~March 31, 2024~~ and ~~2022~~ ~~2023~~ (in thousands):

	Three Months Ended		Nine Months Ended		Three Months Ended	
	September 30, 2023	September 30, 2022	September 30, 2023	September 30, 2022	March 31, 2024	March 31, 2023
					March 31, 2024	March 31, 2023
Noninterest Income						
Service charges on deposit accounts	\$ 733	\$ 708	\$ 2,062	\$ 2,015	\$ 654	\$ 646
ATM and check card fees	976	915	2,624	2,462	770	800

Wealth management fees	811	739	2,336	2,302	883	776
Brokered mortgage fees	38	72	73	224	38	—
Income from bank owned life insurance	175	166	459	441		
Fees for other customer services	122	14	538	160	195	196
Noninterest income (in-scope of Topic 606)	\$ 2,855	\$ 2,614	\$ 8,092	\$ 7,604	\$ 2,540	\$ 2,418
Noninterest income (out-of-scope of Topic 606)	198	413	623	914	1,507	360
Total noninterest income	\$ 3,053	\$ 3,027	\$ 8,715	\$ 8,518	\$ 4,047	\$ 2,778

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Notes to Consolidated Financial Statements (Unaudited)

Note 10. Derivative Financial Instruments

On April 21, 2020, the Company entered into two interest rate swap agreements related to its outstanding junior subordinated debt. One swap agreement was related to the Company's junior subordinated debt with a redemption date of June 17, 2034, which became effective on March 17, 2020. The notional amount of the interest rate swap was \$5.0 million and terminates on June 17, 2034. Under the terms of the agreement, the Company pays interest quarterly at a fixed rate of 0.79% and receives interest quarterly at a variable rate of the three-month CME Term SOFR plus 0.26161% term secured overnight finance rate (SOFR). The variable rate resets on each interest payment date. The other swap agreement was related to the Company's junior subordinated debt with a redemption date of October 1, 2036, which became effective on April 1, 2020. The notional amount of the interest rate swap was \$4.0 million and terminates on October 1, 2036. Under the terms of the agreement, the Company pays interest quarterly at a fixed rate of 0.82% and receives interest quarterly at a variable rate of the three-month CME Group Term Secured Overnight Financing Rate ("CME Term SOFR") plus 0.26161% term SOFR. The variable rate resets on each interest payment date. The Company's junior subordinated debt instruments transitioned from a LIBOR-indexed floating rate of interest to a Secured Overnight Financing Rate ("SOFR") indexed floating rate on July 3, 2023.

The Company entered into interest rate swaps to reduce interest rate risk and to manage interest expense. By entering into these agreements, the Company converted variable rate debt into fixed rate debt. Alternatively, the Company may enter into interest rate swap agreements to convert fixed rate debt into variable rate debt. Interest differentials paid or received under interest rate swap agreements are reflected as adjustments to interest expense. The Company designated the interest rate swaps as hedging instruments in qualifying cash flow hedges. Changes in fair value of these designated hedging instruments is reported as a component of other comprehensive (loss) income. Interest rate swaps designated as cash flow hedges are expected to be highly effective in offsetting the effect of changes in interest rates on the amount of variable rate interest payments, and the Company assesses the effectiveness of each hedging relationship quarterly. If the Company determines that a cash flow hedge is no longer highly effective, future changes in the fair value of the hedging instrument would be reported as earnings. As of September 30, 2023 March 31, 2024, the Company has designated cash flow hedges to manage its exposure to variability in cash flows on certain variable rate borrowings for periods that end between June 2034 and October 2036. The notional amounts of the interest rate swaps were not exchanged and do not represent exposure to credit loss. In the event of default by a counterparty, the risk in these transactions is the cost of replacing the agreements at current market rates.

All interest rate swaps were entered into with counterparties that met the Company's credit standards and the agreements contain collateral provisions protecting the at-risk party. The Company believes that the credit risk inherent in these derivative contracts is not significant.

Unrealized gains or losses recorded in other comprehensive (loss) income related to cash flow hedges are reclassified into earnings in the same period(s) during which the hedged interest payments affect earnings. When a designated hedging instrument is terminated and the hedged interest payments remain probable of occurring, any remaining unrecognized gain or loss in other comprehensive (loss) income is reclassified into earnings in the period(s) during which the forecasted interest payments affect earnings. Amounts reclassified into earnings and interest receivable or payable under designated interest rate swaps are reported in interest expense. The Company does not expect any unrealized losses related to cash flow hedges to be reclassified into earnings in the next twelve months.

The following table summarizes key elements of the Company's derivative instruments at September 30, 2023 March 31, 2024 and December 31, 2022 2023 (in thousands):

	September 30, 2023				March 31, 2024			
	Notional Amount	Assets	Liabilities	Collateral Pledged(1)	Notional Amount	Assets	Liabilities	Collateral Pledged(1)
Cash Flow Hedges								
Interest rate swap contracts	\$ 9,000	\$ 3,065	\$ —	\$ —	\$ 9,000	\$ 2,672	\$ —	\$ —
December 31, 2022						December 31, 2023		

	Notional Amount	Assets	Liabilities	Collateral Pledged(1)	Notional Amount	Assets	Liabilities	Collateral Pledged(1)
Cash Flow Hedges								
Interest rate swap contracts	\$ 9,000	\$ 2,679	\$ —	\$ —	\$ 9,000	\$ 2,488	\$ —	\$ —

(1) Collateral pledged may be comprised of cash or securities.

Note 11. Subsequent Events Acquisition

During the month of On October 2023, March 25, 2024, the Company signed entered into an agreement to acquire Touchstone for an aggregate purchase price of \$47.0 million in stock (based on the Company's closing stock price as of two March 25, 2024). The financial position and results of operations of Touchstone are not new leases for real estate reflected in the Company's financial statements as of March 31, 2024. At the time of closing of the acquisition, Touchstone is expected to be occupied have twelve retail bank offices serving south-central Virginia and northern North Carolina, and an administrative office in 2024 Prince George, Virginia. The first lease closing of the acquisition is for a new retail branch office subject to customary closing conditions, including shareholder and regulatory approvals. As of March 31, 2024, Touchstone reported total assets of \$673.2 million, gross loans of \$506.0 million, and total deposits of \$557.6 million.

In connection with the transaction, the Company expects to issue approximately 2.7 million shares of its common stock to the shareholders of Touchstone. Upon completion of the transaction, Touchstone Bank, which is Touchstone's wholly owned banking subsidiary, is expected to be opened in Roanoke, Virginia. This lease is merged with and into First Bank. The acquisition will be accounted for as a business combination under ASC 120-805, *Business Combinations*. Under acquisition accounting, assets acquired and includes an option to renew the term liabilities assumed are recorded at their acquisition date fair values, and any excess of the lease for two additional 60-month periods. Occupancy purchase price over the aggregate fair value of the net assets acquired is expected to begin no later than June 1, 2024. The second lease will replace an existing lease for a loan production office in Glen Allen, Virginia. This lease is for an 86-month term. Occupancy is expected to begin no later than February 1, 2024.

recognized as goodwill.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Cautionary Statement Regarding Forward-Looking Statements

First National Corporation (the Company) makes forward-looking statements in this Form 10-Q that are subject to risks and uncertainties. These forward-looking statements include, but are not limited to, statements regarding profitability, liquidity, adequacy of capital, allowance for credit losses, interest rate sensitivity, market risk, growth strategy, strategy, and the impact of the Company's acquisition (the Merger) of Touchstone Bankshares, Inc. (Touchstone), including the expected levels of merger related expenses to be incurred by the Company, the expected benefits of the Merger, and the potential impact of the Merger on the Company's and First Bank's (the Bank) liquidity and capital levels, as well as certain financial and other goals. The words "believes," "expects," "may," "will," "should," "projects," "contemplates," "anticipates," "forecasts," "intends," or other similar words or terms are intended to identify forward-looking statements. These forward-looking statements are subject to significant uncertainties because they are based upon or are affected by factors including:

- the ability of the Company and the Bank to realize the anticipated benefits of the Merger, including the ability to close the Merger within the expected time frame, or at all, and to successfully integrate Touchstone's systems and processes into the Company's systems and processes;
- expected revenue synergies and cost savings from the Merger that may not be fully realized or realized within the expected time frame;
- revenues following the Merger that may be lower than expected;
- general business conditions, as well as conditions within the financial markets;
- general economic conditions, including unemployment levels, inflation and slowdowns in economic growth;
- the Company's branch and market expansions, technology initiatives and other strategic initiatives;
- the impact of competition from banks and non-banks, including financial technology companies (Fintech);
- the composition of the loan and deposit portfolio, including the types of accounts and customers, may change, which could impact the amount of net interest income and noninterest income in future periods, including revenue from service charges on deposits;
- limited availability of financing or inability to raise capital;
- reliance on third parties for key services;
- the Company's credit standards and its on-going credit assessment processes might not protect it from significant credit losses;
- the quality of the loan portfolio and the value of the collateral securing those loans;

- prepayments of loans and securities could materially impact earnings through a reduction in interest income and fees on loans and interest income on securities;
- demand for loan products;
- deposit flows;
- the level of net charge-offs on loans and the adequacy of the allowance for loan losses;
- the concentration in loans secured by real estate may adversely affect earnings due to changes in the real estate markets;
- the value of securities held in the Company's investment portfolio;
- legislative or regulatory changes or actions, including the effects of changes in tax laws;
- changes in accounting principles, policies and guidelines and elections made by the Company thereunder;
- cyber threats, attacks or events;
- the ability to maintain adequate liquidity by retaining deposit customers and secondary funding sources, especially if the Company's or the industry's reputation were to become damaged;
- monetary and fiscal policies of the U.S. Government, including policies of the U.S. Department of the Treasury and the Federal Reserve Board, and the effect of those policies on interest rates and business in the Company's markets;
- changes in interest rates could have a negative impact on the value of the Company's securities portfolio and its net interest income and an unfavorable impact on the Company's customers' ability to repay loans;
- geopolitical conditions, including acts or threats of terrorism, international hostilities, or actions taken by the U.S. or other governments in response to acts or threats of terrorism and/or military conflicts, which could impact business and economic conditions in the U.S. and abroad; and
- other factors identified in Item 1A. Risk Factors of the Company's Form 10-K for the year ending December 31, 2022, December 31, 2023 and in this Form 10-Q.

Because of these and other uncertainties, actual results may be materially different from the results indicated by these forward-looking statements. In addition, past results of operations do not necessarily indicate future results. The following discussion and analysis of the financial condition at September 30, 2023 March 31, 2024 and statements of income of the Company for the three and nine months ended September 30, 2023 March 31, 2024 and 2022 2023 should be read in conjunction with the consolidated financial statements and related notes included in Part I, Item 1, of this Form 10-Q and in Part II, Item 8, of the Form 10-K for the period ending December 31, 2022 December 31, 2023. The statements of income for the three and nine months ended September 30, 2023 March 31, 2024 may not be indicative of the results to be achieved for the year.

Executive Overview

The Company

First National Corporation (the Company) is the bank holding company of:

- First Bank (the Bank). The Bank owns:
 - First Bank Financial Services, Inc.
 - Bank of Fincastle Services, Inc.
 - ESF, LLC
 - Shen-Valley Land Holdings, LLC
- First National (VA) Statutory Trust II (Trust II)
- First National (VA) Statutory Trust III (Trust III and, together with Trust II, the Trusts)

First Bank Financial Services, Inc. owns an interest in an entity that provides title insurance services. Bank of Fincastle Services, Inc. is no longer an active operating entity. Shen-Valley Land Holdings, LLC and ESF, LLC were formed to hold other real estate owned and future office sites. The Trusts were formed for the purpose of issuing redeemable capital securities, commonly known as trust preferred securities and are not included in the Company's consolidated financial statements in accordance with authoritative accounting guidance because management has determined that the Trusts qualify as variable interest entities.

Products, Services, Customers and Locations

The Bank offers loan, deposit, and wealth management products and services. Loan products and services include consumer loans, residential mortgages, home equity loans, and commercial loans. Deposit products and services include checking accounts, treasury management solutions, savings accounts, money market accounts, certificates of deposit, and individual retirement accounts. Wealth management services include estate planning, investment management of assets, trustee under an agreement, trustee under a will, individual retirement accounts, and estate settlement. Customers include small and medium-sized businesses, individuals, estates, local governmental entities, and non-profit organizations.

The Bank's office locations are well-positioned in attractive markets along the Interstate 81, Interstate 66, and Interstate 64 corridors in the Shenandoah Valley, the Roanoke Valley, central regions of Virginia, and the city of Richmond. Within these markets, there are diverse types of industry including medical and professional services, manufacturing, retail, warehousing, Federal and local government, hospitality, and higher education. The Bank's products and services are delivered through 20 bank branch offices, a loan production office and customer service centers in two retirement villages. For the location and general character of each of these offices, see Item 2 of the Company's Form 10-K for the year ended December 31, 2022 December 31, 2023. Many of the Bank's services are also delivered through the Bank's mobile banking platform, its website, www.fbvirginia.com, and a network of ATMs located throughout its market area.

Revenue Sources and Expense Factors

The primary source of revenue is from net interest income earned by the Bank. Net interest income is the difference between interest income and interest expense and typically represents between 70% and 80% of the Company's total revenue. Interest income is determined by the amount of interest-earning assets outstanding during the period and the interest rates earned on those assets. The Bank's interest expense is a function of the amount of interest-bearing liabilities outstanding during the period and the interest rates paid. In addition to net interest income, noninterest income is the other source of revenue for the Company. Noninterest income is derived primarily from service charges on deposits, fee income from wealth management services, and ATM and check card fees.

Primary expense categories are salaries and employee benefits, which comprised 57% 59% of noninterest expenses for the nine three months ended September 30, 2023 March 31, 2024, followed by occupancy and equipment expense, which comprised 12% 11% of noninterest expenses. The provision for credit losses is also typically a primary expense of the Bank. The provision is determined by factors that include net charge-offs, asset quality, economic conditions, and loan growth. Changing economic conditions caused by inflation, recession, unemployment, or other factors beyond the Company's control have a direct correlation with asset quality, net charge-offs, and ultimately the required provision for credit losses.

Acquisition of Touchstone Bankshares, Inc.

On March 25, 2024, the Company entered into an agreement to acquire Touchstone for an aggregate purchase price of approximately \$47.0 million in stock (based on the Company's closing stock price as of March 25, 2024). The closing of the acquisition is subject to customary closing conditions, including shareholder and regulatory approvals, and the Company expects to complete the acquisition in the fourth quarter of 2024. At the time of closing of the acquisition, Touchstone is expected to have 12 retail bank offices serving south-central Virginia and northern North Carolina, and an administrative office in Prince George, Virginia. After the acquisition is completed, the former Touchstone branches will continue to operate as Touchstone Bank, a division of First Bank, until the systems conversion is completed, expected in the first quarter of 2025. As of March 31, 2024, Touchstone reported total assets of \$673.2 million, gross loans of \$506.0 million, and total deposits of \$557.6 million. In connection with the transaction, the Company expects to issue approximately 2.7 million shares of its common stock to the shareholders of Touchstone. There were no merger related expenses incurred for the three months ended March 31, 2024 in connection with its acquisition of Touchstone. The Company estimates that it will incur aggregate pre-tax merger related expenses of approximately \$3.3 million during 2024.

Overview of Quarterly Financial Performance

Comparing the Three-Month Periods Ending September 30, 2023 and September 30, 2023

Net income decreased \$1.3 million \$640 thousand, or 17%, to \$3.2 million, or 30%, to \$3.1 million, or \$0.50 \$0.51 per diluted share, for the three months ended September 30, 2023 March 31, 2024, compared to \$4.5 million \$3.8 million, or \$0.71 \$0.61 per diluted share, for the same period in 2022 2023. Return on average assets was 0.91% 0.90% and return on average equity was 10.96% 11.07% for the third first quarter of 2023 2024, compared to 1.27% 1.15% and 17.27% 14.20%, respectively, for the same period in 2022 2023.

The decrease in net income resulted from a \$1.0 million, \$326 thousand, or 9% 3%, decrease in net interest income, a \$1.0 million increase in provision for credit losses, and a \$701 \$687 thousand, or 8%, increase in total noninterest expense, which were partially offset by a \$26 thousand, \$1.3 million, or 1% 46%, increase in total noninterest income.

Net interest income decreased \$326 thousand, or 1%, from a \$100 thousand decrease \$3.1 million increase in total interest expense, which was partially offset by a \$2.8 million increase in total interest income. Net interest income was negatively impacted by a 36-basis point contraction of the net interest margin to 3.24% and was partially offset by the positive impact of a \$93.3 million, or 7%, increase in average earning assets.

The provision for credit losses and a \$286 thousand decrease in income tax expense.

Net interest income decreased from a 23-basis point decrease in increased to \$1.0 million for the net interest margin and a 1% decrease in average earning assets. The net interest margin was impacted by changes in market interest rates, including the Federal funds target rate, which averaged 5.43% in the third first quarter of 2023 2024 compared to 2.35% no provision for the same period one year ago. The rise in the Federal funds rate had an impact allowance for credit losses on the Company's cost loans totaled \$12.6 million, or 1.30% of funds, total loans at March 31, 2024, which was a \$3.9 million increase compared to \$8.7 million, or 0.95% of total loans at March 31, 2023. The allowance for credit losses on loans individually evaluated increased 94 basis points. The higher cost of funds was partially offset by a 68-basis point increase in the yield on earning assets.

The net interest margin decreased by 1 basis point in the third quarter of 2023 \$3.6 million compared to the linked second quarter of 2023, which was an improvement compared to a 24-basis point decrease same period in the second quarter of 2023 prior year. The allowance for credit losses on loans collectively evaluated increased \$318 thousand compared to the linked first quarter of 2023, and a 10-basis point decrease same period one year ago. Net charge-offs totaled \$362 thousand in the first quarter of 2023 compared to the linked fourth quarter of 2022 2024 and \$915 thousand in 2023.

Total noninterest income increased \$1.3 million from an increase in other operating income, which was attributable to a recovery on a loan that was acquired through a business combination in 2021. Total noninterest expenses increased by \$701 thousand, or 8%, and was primarily attributable to increases in salaries and employee benefits and legal and professional expenses, ATM and check card expenses, and FDIC assessment costs.

Comparing the Nine-Month Periods Ending September 30, 2023 and September 30, 2022

Net income decreased \$1.5 million, or 13%, to \$10.5 million, or \$1.67 per diluted share, for the nine months ended September 30, 2023, compared to \$12.0 million, or \$1.92 per diluted share, for the same period in 2022. Return on average assets was 1.03% and return on average equity was 12.57% for the nine months ending 2023, compared to 1.14% and 15.12%, respectively, for the same period in 2022.

The decrease in net income resulted from a \$961 thousand, or 3%, decrease in net interest income and a \$1.5 million, or 6%, increase in total noninterest expense, which were partially offset by a \$197 thousand, or 2%, increase in total noninterest income, a \$400 thousand decrease in the provision for credit losses, and a \$318 thousand decrease in income tax expense.

Net interest income decreased from a 13-basis point decrease in the net interest margin, which was partially offset by a 1% increase in average earning assets. The net interest margin was impacted by changes in market interest rates, including the Federal funds target rate, which averaged 5.09% for the nine months ending September 30, 2023, compared to 1.20% for the same period one year ago. The rise in the Federal funds rate had an impact on the Company's cost of funds, which increased 85 basis points. The higher cost of funds was partially offset by a 68 basis point increase in the yield on earning assets.

Total noninterest expense increased by \$1.5 million, or 6%, and was primarily attributable to increases in salaries and employee benefits, marketing expense, ATM and check card expenses, and other operating expenses.

For a more detailed discussion of the Company's quarterly performance, see "Net Interest Income," "Provision for Credit Losses," "Noninterest Income," "Noninterest Expense" and "Income Taxes" below.

Non-GAAP Financial Measures

This report refers to the efficiency ratio, which is computed by dividing noninterest expense, excluding amortization of intangibles, net gains (loss) on disposal of premises and equipment, other real estate owned (income) expense, net, and merger related expenses, by the sum of net interest income on a tax-equivalent basis and noninterest income, excluding securities gains. This is a non-GAAP financial measure that the Company believes provides investors with important information regarding operational efficiency. Such information is not prepared in accordance with GAAP and should not be construed as such. Management believes, however, such financial information is meaningful to the reader in understanding operating performance, but cautions that such information not be viewed as a substitute for GAAP. The methodology for determining this measurement may differ among companies. The Company, in referring to its net income, is referring to income under GAAP. The components of the efficiency ratio calculation are summarized in the following table (dollars in thousands).

	Efficiency Ratio				Efficiency Ratio	
	Three Months Ended		Nine Months Ended		Three Months Ended	
	September 30, 2023	September 30, 2022	September 30, 2023	September 30, 2022	March 31, 2024	March 31, 2023
Noninterest expense	\$ 9,784	\$ 9,083	\$ 28,142	\$ 26,645	\$ 9,887	\$ 9,200
Add/(Subtract): other real estate owned (income) expense, net	(15)	(14)	201	(83)	—	(3)
Subtract: amortization of intangibles	(5)	(6)	(14)	(15)	(4)	(5)
Subtract: merger related expenses	—	—	—	(20)	—	—
Subtract: loss on disposal of premises and equipment, net	\$ 9,764	\$ 9,063	\$ 28,329	\$ 26,527	\$ 9,833	\$ 9,192
Tax-equivalent net interest income	\$ 10,764	\$ 11,809	\$ 32,848	\$ 33,818	\$ 10,931	\$ 11,258
Noninterest income	3,053	3,027	8,715	8,515	4,047	2,778
	\$ 13,817	\$ 14,836	\$ 41,563	\$ 42,333	\$ 14,978	\$ 14,036
Efficiency ratio	70.67 %	61.09 %	68.16 %	62.66 %	65.65 %	65.49 %

This report also refers to net interest margin, which is calculated by dividing tax equivalent net interest income by total average earning assets. Because a portion of interest income earned by the Company is nontaxable, the tax equivalent net interest income is considered in the calculation of this ratio. Tax equivalent net interest income is calculated by adding the tax benefit realized from interest income that is nontaxable to total interest income then subtracting total interest expense. The tax rate utilized in calculating the tax benefit for both 2023 and 2022 is 21%. The reconciliation of tax equivalent net interest income, which is not a measurement under GAAP, to net interest income, is reflected in the table below (in thousands).

Reconciliation of Net Interest Income to Tax-Equivalent Net Interest Income									Reconciliation of Net Interest Income to Tax-Equivalent Net Interest Income					
									Three Months Ended					
									September 30, 2023	September 30, 2022	September 30, 2023	September 30, 2022	March 31, 2024	March 31, 2023
GAAP measures:														
Interest income – loans	\$	12,640	\$	10,759	\$	36,038	\$	30,218	\$	13,484	\$	11,512		
Interest income – investments and other		1,991		2,033		6,407		5,437		2,850		2,016		
Interest expense – deposits		(3,810)		(927)		(9,428)		(1,680)		(4,771)		(2,216)		
Interest expense – subordinated debt		(69)		(70)		(207)		(208)		(69)		(69)		
Interest expense – junior subordinated debt		(69)		(68)		(203)		(202)		(68)		(67)		
Interest expense – other borrowings		—		—		(3)		—		(576)		—		
Total net interest income	\$	10,683	\$	11,727	\$	32,604	\$	33,565	\$	10,850	\$	11,176		
Non-GAAP measures:														
Tax benefit realized on non-taxable interest income – loans	\$	—	\$	—	\$	—	\$	8	\$	—	\$	—		
Tax benefit realized on non-taxable interest income – municipal securities		81		82		244		245		81		82		
Total tax benefit realized on non-taxable interest income	\$	81	\$	82	\$	244	\$	253	\$	81	\$	82		
Total tax-equivalent net interest income	\$	10,764	\$	11,809	\$	32,848	\$	33,818	\$	10,931	\$	11,258		

Critical Accounting Policies

The Company's consolidated financial statements are prepared in accordance with GAAP. The financial information contained within our statements is, to a significant extent, based on measures of the financial effects of transactions and events that have already occurred. A variety of factors could affect the ultimate value obtained when earning income, recognizing an expense, recovering an asset or relieving a liability. Although the economics of the Company's transactions may not change, the timing of events that would impact the transactions could change.

Critical accounting policies are most important to the portrayal of the Company's financial condition or results of operations and require management's most difficult, subjective, and complex judgments about matters that are inherently uncertain. If conditions occur that differ from our assumptions, depending upon the severity of such differences, the Company's financial condition or results of operations may be materially impacted. The Company evaluates its critical accounting estimates and assumptions on an ongoing basis and updates them as needed. The Company provides additional information on its critical accounting policies and estimates under "Management's Discussion and Analysis of Financial Condition and Results of Operations—Critical Accounting Policies" in its [2022](#)[2023](#) Form 10-K and in Note 1 "Significant Accounting Policies and Estimates" in Part I, Item 1 of this Quarterly Report.

Lending Policies

There have been no material changes in the Company's lending policies disclosed in the Annual Report on Form 10-K for the year ended [December 31, 2022](#)[December 31, 2023](#).

Results of Operations

General

Net interest income represents the primary source of earnings for the Company. Net interest income equals the amount by which interest income on interest-earning assets, predominantly loans and securities, exceeds interest expense on interest-bearing liabilities, including deposits, other borrowings, subordinated debt, and junior subordinated debt. Changes in the volume and mix of interest-earning assets and interest-bearing liabilities, as well as their respective yields and rates, are the components that impact the level of net interest income. The net interest margin is calculated by dividing tax-equivalent net interest income by average earning assets. The provision for credit losses, noninterest income, and noninterest expense are the other components that determine net income. Noninterest income and expense primarily consist of income from service charges on deposit accounts, revenue from wealth management services, ATM and check card income, revenue from other customer services, income from bank owned life insurance, general and administrative expenses, amortization expense, and other real estate owned expense.

Net Income

Three Month Period Ended September 30, 2023

Net income decreased ~~\$1.3 million~~ ~~\$640 thousand~~, or 17%, to ~~\$3.2 million~~, or 30%, to ~~\$3.1 million~~, or ~~\$0.50~~ ~~\$0.51~~ per diluted share, for the three months ended ~~September 30, 2023~~ ~~March 31, 2024~~, compared to ~~\$4.5 million~~ ~~\$3.8 million~~, or ~~\$0.71~~ ~~\$0.61~~ per diluted share, for the same period in ~~2022, 2023~~. Return on average assets was ~~0.91%~~ ~~0.90%~~ and return on average equity was ~~10.96%~~ ~~11.07%~~ for the ~~third~~ ~~first~~ quarter of ~~2023, 2024~~, compared to ~~1.27%~~ ~~1.15%~~ and ~~17.27%~~ ~~14.20%~~, respectively, for the same period in ~~2022, 2023~~.

The decrease in net income resulted from a ~~\$1.0 million~~, ~~\$326 thousand~~, or ~~9%~~ ~~3%~~, decrease in net interest income, a ~~\$1.0 million~~ increase in provision for credit losses and a ~~\$701~~ ~~\$687~~ thousand, or 8%, increase in total noninterest expense, which were partially offset by a ~~\$26 thousand~~, ~~\$1.3 million~~, or ~~1%~~ ~~46%~~, increase in total noninterest income, a ~~\$100 thousand~~ decrease in the provision for credit losses, and a ~~\$286 thousand~~ decrease in income tax expense.

Nine Month Period Ended September 30, 2023

Net income decreased \$1.5 million, or 13%, to \$10.5 million, or \$1.67 per diluted share, for the nine months ended September 30, 2023, compared to \$12.0 million, or \$1.92 per diluted share, for the same period in 2022. Return on average assets was 1.03% and return on average equity was 12.57% for the nine months ended September 30, 2023, compared to 1.14% and 15.12%, respectively, for the same period in 2022.

The decrease in net income was attributable to a \$1.5 million, or 6%, increase in noninterest expenses, and a \$961 thousand decrease in net interest income. These changes were partially offset by a \$197 thousand increase in noninterest income, and a \$400 thousand decrease in the provision for credit losses, and a \$318 thousand decrease in income tax expense.

Net Interest Income

Three Month Period Ended September 30, 2023

Net interest income decreased from a 23-basis point decrease in the net interest margin and a 1% decrease in average earning assets. The net interest margin was impacted by changes in market interest rates, including the Federal funds target rate, which averaged 5.43% in the third quarter of 2023, compared ~~\$326 thousand~~, or 3%, to ~~2.35%~~ ~~\$10.9 million~~ for the same period one year ago. The rise in the Federal funds rate had an impact on the Company's cost of funds, which increased 94 basis points. The higher cost of funds was partially offset by a 68-basis point increase in the yield on earning assets.

The net interest margin decreased by 1 basis point in the third quarter of 2023 compared to the linked second quarter of 2023, which was an improvement compared to a 24-basis point decrease in the second quarter of 2023 compared to the linked first quarter of 2023, and a 10-basis point decrease in the first quarter of 2023 compared to the linked fourth quarter of 2022.

Net interest income decreased by \$1.0 million as total interest income increased by \$1.8 million, which was offset by a \$2.9 million increase in total interest expense. Although both interest income and interest expense increased as a result of the higher interest rate environment in 2023, interest expense increased more than interest income, comparing the third quarter of 2023 with the same period of the prior year.

Total interest income increased primarily from interest and fees on loans, which resulted from both higher yields and higher average balances, while interest on deposits in banks increased solely from higher yields, as their average balances decreased ~~2024~~ compared to the same period of ~~in~~ the prior year. The yield on loans Total interest expense increased by 52 basis points to 5.31% ~~\$3.1 million~~ and the average balance of loans increased to 74% of average earning assets, compared to 68% for the same period one year ago. The yield on interest-bearing deposits in banks was partially offset by total interest income, which increased by 344 basis points to 5.39%, while the average balance decreased to 2% of average earning assets, compared to 6% for the same period of the prior year.

Net accretion of discounts on purchased loans totaled \$61 thousand in the third quarter of 2023 compared to \$295 thousand for the third quarter of 2022.

The increase in interest expense was attributable to higher interest expense on deposits. Deposit costs increased from higher interest rates paid on deposit accounts in 2023, as well as a change in the deposit portfolio composition, as interest-bearing deposits increased as a percentage of total deposits, while noninterest-bearing deposits decreased. Additionally, within the interest-bearing deposit portfolio, higher cost time deposit balances and money market balances increased, while lower cost checking and savings balances decreased. The average balance of time deposits increased to 22% of average interest-bearing deposits, compared to 16% for the same period of the prior year. The cost of interest-bearing deposits increased by 139 basis points to 1.82% for the current period, compared to 0.43% for the same period of the prior year. The total cost of funds increased 94-basis points to 1.27% for the current period compared to 0.33% for the same period of the prior year.

Nine Month Period Ended September 30, 2023

\$2.8 million. Net interest income decreased from was negatively impacted by a 13-basis ~~36~~-basis point decrease in the net interest margin, which was partially offset by a ~~1%~~ ~~\$93.3 million~~, or 7%, increase in average earning assets. The net interest margin was impacted by changes in market interest rates, including the Federal funds target rate, which averaged 5.09% for the nine months ending September 30, 2023, compared to 1.20% for the same period one year ago. The rise in the Federal funds rate had an impact on the Company's cost of funds, which increased 85 basis points. The higher cost of funds was partially offset by a 68-basis point increase in the yield on earning assets.

Net interest income decreased \$961 thousand as total interest income increased \$6.8 million and was offset by a \$7.8 million ~~The~~ increase in total interest expense. Although both interest income and interest expense increased as was attributable to a result of the higher interest rate environment in 2023, the \$2.0 million, or 17%, increase in interest income was offset by the and fees on loans and a \$944 thousand increase in interest expense, comparing the nine-month period of 2023 with income on interest-bearing deposits in banks. The increase in interest income on loans was attributable to a 49-basis point increase in yield and a 6% increase in average balances compared to the same period of ~~in~~ the prior year. The increase in interest income on interest-bearing deposits in other banks was attributable to a 117-basis point increase in yield and a \$65.8 million, or 187% increase in average balances compared to the same period in the prior year.

Total interest income increased from interest and fees on loans and from interest on deposits in banks. Interest and fees on loans increased from higher yields and higher average balances. Interest on deposits in banks increased solely from higher yields, as their average balances decreased compared to the same period of the prior year. The yield on loans increased by 49 basis points to 5.19% and the average balance increased to 73% of total average earning assets, compared to 68% for the same period of the prior year. The yield on interest-bearing deposits in banks increased by 420 basis points to 4.95%, while the average balance of interest-bearing deposits decreased to 3% of average earning assets, compared to 10% for the same period of the prior year.

Accretion of PPP income, net of costs, and accretion of discounts on purchased loans, net of premiums, were included in interest and fees on loans. There was no accretion of PPP income for the nine months ended September 30, 2023, compared to \$358 thousand for the same period of 2022. Net accretion of discounts on purchased loans totaled \$510 thousand for the nine-month period ended September 30, 2023, compared to \$1.0 million for the same period of 2022.

The increase in total interest expense was attributable to higher a \$2.6 million increase in interest expense on deposits and a \$576 thousand increase in interest expense on other borrowings. The higher interest expense on deposits resulted from a 110-basis point increase in the cost of interest-bearing deposits and a 7% increase in average interest-bearing deposit balances. The increase in the cost of deposits was also impacted by a change in the composition of the deposit portfolio composition. Interest as lower cost deposit balances decreased, while higher cost deposit balances increased. The higher interest expense on deposits increased other borrowings resulted from higher a \$49.8 million increase in average balances.

The net interest rates paid on deposit accounts margin was 3.23% for the first quarter of 2024 compared to 3.60% for the same period in 2023, the prior year as well as an the increase in the average balances cost of higher cost deposits and a decrease funds exceeded the increase in yield on earning assets. Although the net interest margin in the average balances first quarter of 2024 was 37-basis points lower cost deposits. The average balance of time deposits balances increased to 20% of total average interest-bearing deposits, compared to 16% for than the same period one year ago. The cost of ago, the net interest margin has been stable in recent quarterly periods. In December 2023, the Bank borrowed \$50.0 million from the Federal Reserve Bank through its Bank Term Funding Program and invested the proceeds in interest-bearing deposits deposit in other banks, which increased net interest income. Although net interest income increased, the transaction negatively impacted net interest margin by 1269 basis points to 1.52% in the first quarter of 2024. The net interest margin was 3.35% for the current period, compared to 0.26% linked fourth quarter of 2023, 3.35% for third quarter of 2023, and 3.36% for the same period second quarter of 2023. The net interest margin has been stable in recent quarterly periods as the prior year. The total rising cost of funds increased 85-basis points to 1.06% for the current period compared to 0.21% for the same period of the prior year. has been offset by an increase in earning asset yields.

The following tables show interest income on earning assets and related average yields as well as interest expense on interest-bearing liabilities and related average rates paid for the periods indicated (dollars in thousands):

Average Balances, Income and Expenses, Yields and Rates (Taxable Equivalent Basis)

	Three Months Ended						Three Months Ended					
	September 30, 2023			September 30, 2022			March 31, 2024			March 31, 2023		
	Average Balance	Interest Income/Expense	Yield/Rate	Average Balance	Interest Income/Expense	Yield/Rate	Average Balance	Interest Income/Expense	Yield/Rate	Average Balance	Interest Income/Expense	Yield/Rate
Assets												
Securities:												
Taxable	\$ 251,623	\$ 1,323	2.09%	\$ 285,482	\$ 1,323	1.84%	\$ 233,003	\$ 1,224	2.11%	\$ 260,034	\$ 1,224	2.11%
Tax-exempt (1)	53,238	384	2.87%	54,319	389	2.84%	54,336	386	2.86%	54,733	386	2.86%
Restricted	1,904	27	5.57%	1,908	23	4.75%	2,084	33	6.29%	1,905	33	6.29%
Total securities	\$ 306,765	\$ 1,734	2.24%	\$ 341,709	\$ 1,735	2.01%	\$ 289,423	\$ 1,643	2.31%	\$ 316,672	\$ 1,643	2.31%
Loans: (2)												
Taxable	\$ 943,452	\$ 12,640	5.31%	\$ 890,696	\$ 10,759	4.79%	\$ 970,615	\$ 13,484	5.59%	\$ 915,863	\$ 13,484	5.59%
Tax-exempt (1)	—	—	—	—	—	0.00%	—	—	—	—	—	—
Total loans	\$ 943,452	\$ 12,640	5.31%	\$ 890,696	\$ 10,759	4.79%	\$ 970,615	\$ 13,484	5.59%	\$ 915,863	\$ 13,484	5.59%
Federal funds sold	—	—	—	1	—	—	8	—	0.00%	1	—	0.00%
Interest-bearing deposits with other institutions	24,894	338	5.39%	77,388	380	1.95%	101,126	1,288	5.12%	35,293	1,288	5.12%
Total earning assets	\$ 1,275,111	\$ 14,712	4.58%	\$ 1,309,794	\$ 12,874	3.90%	\$ 1,361,172	\$ 16,415	4.86%	\$ 1,267,829	\$ 16,415	4.86%
Less: allowance for credit losses on loans	(8,847)	(6,152)					(11,981)	(11,981)		(9,534)	(9,534)	

Total non-earning assets	88,914	89,666	82,421	93,334							
Total assets	<u>\$ 1,355,178</u>	<u>\$ 1,393,308</u>	<u>\$ 1,431,612</u>	<u>\$ 1,351,629</u>							
Liabilities and Shareholders' Equity											
Interest bearing deposits:											
Checking	\$ 264,193	\$ 1,194	1.79%	\$ 293,169	\$ 416	0.56%	\$ 255,579	\$ 702	1.11%	\$ 276,611	\$
Regular savings	163,550	49	0.12%	205,608	56	0.11%	147,938	662	1.80%	194,751	
Money market accounts	223,121	1,348	2.40%	215,199	284	0.52%	269,407	1,843	2.75%	198,177	
Time deposits	180,729	1,219	2.68%	133,293	171	0.51%	197,065	1,564	3.19%	143,070	
Total interest-bearing deposits	\$ 831,593	\$ 3,810	1.82%	\$ 847,269	\$ 927	0.43%	\$ 869,989	\$ 4,771	2.21%	\$ 812,609	\$
Federal funds purchased							—	—	—%	6	
Subordinated debt	4,996	69	5.50%	4,995	70	5.50%	4,998	69	5.57%	4,995	
Junior subordinated debt	9,279	69	2.95%	9,279	68	2.91%	9,279	68	2.92%	9,279	
Other borrowings							50,000	576	4.63%	222	
Total interest-bearing liabilities	\$ 845,868	\$ 3,948	1.85%	\$ 861,542	\$ 1,065	0.49%	\$ 934,266	\$ 5,484	2.36%	\$ 827,111	\$
Non-interest bearing liabilities											
Demand deposits	391,342			425,630			375,445			409,777	
Other liabilities	4,909			3,795			5,273			4,817	
Total liabilities	<u>\$ 1,242,119</u>			<u>\$ 1,290,967</u>			<u>\$ 1,314,984</u>			<u>\$ 1,241,705</u>	
Shareholders' equity	113,059			102,341			116,628			109,924	
Total liabilities and Shareholders' equity	<u>\$ 1,355,178</u>			<u>\$ 1,393,308</u>			<u>\$ 1,431,612</u>			<u>\$ 1,351,629</u>	
Net interest income	\$ 10,764			\$ 11,809			\$ 10,931			\$	
Interest rate spread		2.73%			3.41%				2.50%		
Cost of funds		1.27%			0.33%				1.68%		
Interest expense as a percent of average earning assets		1.23%			0.32%				1.62%		
Net interest margin		3.35%			3.58%				3.24%		

(1) Income and yields are reported on a taxable-equivalent basis assuming a federal tax rate of 21%. The tax-equivalent adjustment was \$81 \$102 and \$82 thousand for the three months ended September 30, 2023 March 31, 2024 and 2022, respectively.

(2) Loans on non-accrual status are reflected in the balances.

	Nine Months Ended	
	September 30, 2023	September 30, 2022

	Average Balance	Interest Income/Expense	Yield/Rate	Average Balance	Interest Income/Expense	Yield/Rate
Assets						
Securities:						
Taxable	\$ 255,648	\$ 3,968	2.08 %	\$ 221,708	\$ 3,750	2.26 %
Tax-exempt (1)	54,134	1,161	2.87 %	57,359	1,166	2.72 %
Restricted	1,871	81	5.82 %	1,881	65	4.65 %
Total securities	\$ 311,653	\$ 5,210	2.24 %	\$ 280,948	\$ 4,981	2.37 %
Loans: (2)						
Taxable	\$ 927,525	\$ 36,038	5.19 %	\$ 858,150	\$ 30,202	4.70 %
Tax-exempt (1)	—	—	0.00 %	733	24	4.49 %
Total loans	\$ 927,525	\$ 36,038	5.19 %	\$ 858,883	\$ 30,226	4.70 %
Federal funds sold	—	—	—	—	—	0.00 %
Interest-bearing deposits with other institutions	38,957	1,441	4.95 %	125,677	701	0.75 %
Total earning assets	\$ 1,278,135	\$ 42,689	4.47 %	\$ 1,265,508	\$ 35,908	3.79 %
Less: allowance for credit losses on loans	(9,054)			(5,923)		
Total non-earning assets	90,669			155,714		
Total assets	\$ 1,359,750			\$ 1,415,299		
Liabilities and Shareholders' Equity						
Interest bearing deposits:						
Checking	\$ 270,076	\$ 3,253	1.61 %	\$ 294,386	\$ 671	0.31 %
Regular savings	178,924	165	12.00 %	207,302	108	0.07 %
Money market accounts	215,468	3,380	2.10 %	227,330	410	0.24 %
Time deposits	163,647	2,630	2.15 %	138,118	491	0.48 %
Total interest-bearing deposits	\$ 828,115	\$ 9,428	1.52 %	\$ 867,136	\$ 1,680	0.26 %
Federal funds purchased	2	—	0.00 %	1	—	0.00 %
Subordinated debt	4,997	207	5.56 %	5,494	208	5.05 %
Junior subordinated debt	9,279	203	2.91 %	9,279	202	2.91 %
Other borrowings	73	3	4.91 %	—	—	0.00 %
Total interest-bearing liabilities	\$ 842,466	\$ 9,841	1.56 %	\$ 881,910	\$ 2,090	0.32 %
Non-interest bearing liabilities						
Demand deposits	401,162			423,069		
Other liabilities	4,633			4,035		
Total liabilities	\$ 1,248,261			\$ 1,309,014		
Shareholders' equity	111,489			106,285		
Total liabilities and Shareholders' equity	\$ 1,359,750			\$ 1,415,299		
Net interest income		\$ 32,848			\$ 33,818	
Interest rate spread			2.90 %			3.48 %
Cost of funds			1.06 %			0.21 %
Interest expense as a percent of average earning assets			1.03 %			0.22 %
Net interest margin			3.44 %			3.57 %

(1) Income and yields are reported on a taxable-equivalent basis assuming a federal tax rate of 21%. The tax-equivalent adjustment was \$244 and \$245 thousand for the six months ended September 30, 2023 and 2022, respectively.

(2) Loans on non-accrual status are reflected in the balances.

Provision for Credit Losses

Three Month Period Ended September 30, 2023

The provision for credit losses totaled \$100 thousand \$1.0 million for the third first quarter of 2023, compared to \$200 thousand 2024. There was no provision for credit losses for the same period of the prior year. The provision was comprised of a \$120 \$991 thousand provision on loans, an \$8 thousand recovery on unfunded commitments, and a \$12 \$9 thousand recovery provision on held-to-maturity securities. The provision for credit losses on loans resulted primarily from growth of the loan portfolio, net charge-offs totaling \$362 thousand, and an increase in the specific reserve component of the allowance for credit losses, which were partially offset by a decrease in the general reserve component from lower expected loss rates and an adjustment to a qualitative factor.

Nine Month Period Ended September 30, 2023

The provision for credit losses totaled \$200 thousand for the nine-months ended September 30, 2023, compared to \$600 thousand for the same period of the prior year. The provision was comprised of a \$165 thousand provision on loans, a \$36 thousand provision on unfunded commitments, and a \$1 thousand net recovery on held-to-maturity securities. The provision for credit losses on loans resulted from growth of the loan portfolio, net charge-offs, and an increase in the specific reserve component of the allowance for credit losses, which were partially offset by a decrease in the general reserve component from lower expected loss rates and an adjustment to a qualitative factor.

Noninterest Income

Three Month Period Ended September 30, 2023

Noninterest income increased \$26 thousand, \$1.3 million, or 1% 46%, to \$3.1 million \$4.0 million for the third first quarter of 2023, 2024, compared to the same period of 2022. ATM and check card fees increased \$61 thousand, or 7%, 2023. The increase resulted from an increase in other operating income and wealth management fees. Other operating income increased primarily from a recovery on a loan that was acquired through a business combination in 2021. Wealth management fees increased \$72 \$107 thousand or 10%. These increases were partially offset by a \$58 thousand, or 32%, decrease in fees for other customer services, and a \$34 thousand, or 47%, decrease in brokered mortgage fees. The increases in ATM and check card fees were favorably impacted by an increase in customer transactions. The increase in wealth management fees resulted primarily from an increase in assets under management and from higher market values.

Nine Month Period Ended September 30, 2023

Total noninterest income increased \$197 thousand, or 2%, for the nine months ended September 30, 2023, compared to the same period of 2022. The increase resulted primarily from a \$162 thousand, or 7%, increase in ATM and check card fees, a \$150 thousand increase in other operating income, and a \$47 thousand, or 2%, increase in service charges on deposit accounts, which were partially offset by a \$151 thousand decrease in income from brokered mortgage fees. An increase in customer transactions favorably impacted ATM and check card fees. The increase in other operating income was attributable to a death benefit payment received from a bank-owned life insurance policy in 2023.

Noninterest Expense

Three Month Period Ended September 30, 2023

Noninterest expenses increased \$701 \$687 thousand, or 8%, to \$9.8 million \$9.9 million for the three-month period ended September 30, 2023 March 31, 2024, compared to the same period one year ago. The increase was primarily attributable to a \$331 \$525 thousand, or 6% 10%, increase in salaries and employee benefits, a \$78 \$109 thousand increase in legal and professional fees, and a \$108 thousand increase in ATM and check card expense, a \$52 \$71 thousand increase in FDIC assessment, and which were partially offset by a \$52 \$73 thousand increase decrease in equipment marketing expense.

Salaries and employee benefits increased primarily from an increase in the number of employees and annual increases in employee salaries and wages. Legal and professional fees increased from wealth management advisory expense. ATM and check expenses increased from higher volume of customer transactions. FDIC assessment increased from higher assessed rates during 2023. The increase in equipment expense resulted primarily from higher depreciation expense on software.

Nine Month Period Ended September 30, 2023

Noninterest expense increased \$1.5 million, or 6%, to \$28.1 million for the nine-month period ended September 30, 2023, compared to the same period one year ago. The increase was primarily attributable to a \$656 thousand, or 4% increase in salaries and employee benefits, a \$135 thousand, or 23%, increase in marketing, a \$283 thousand, or 29%, increase in ATM and check card expense, and a \$387 thousand, or 13%, increase in other operating expenses. These increases were partially offset by a \$284 thousand decrease in OREO expense, net, which resulted from gains on the sale of other real estate during 2023.

Salaries and employee benefits increased primarily from an annual increase in employee salaries and wages. Marketing expenses increased from additional advertising and active promotion initiatives. ATM and check card expense increased primarily from a higher volume of customer transactions. Other operating expenses increased primarily from higher recruiting expense, education and training expense, loan collection expense, and courier and armored services.2024.

Income Taxes

Three Month Period Ended September 30, 2023

Income tax expense decreased \$286 \$104 thousand for the third first quarter of 2023, 2024, compared to the same period one year ago. The effective tax rate for the second first quarter of 2023 2024 was 19.0% 20.1% compared to 18.6% 19.0% for the same period in 2022, 2023. The increased effective tax rate for 2023 2024 was the result of higher non-deductible expenses and lower nontaxable income in 2023 2024 compared to 2022, 2023. The Company's income tax expense differed from the amount of income tax determined by applying the U.S. federal income tax rate to pretax income for the three months ended September 30, 2023 March 31, 2024, and 2022, 2023. The difference was a result of net permanent tax deductions, primarily comprised of tax-exempt interest income, and income from bank owned life insurance. A more detailed discussion of the Company's tax

calculation is contained in Note 11 to the Consolidated Financial Statements included in the Company's Annual Report on Form 10-K for the year ended December 31, 2022 December 31, 2023.

Nine Month Period Ended September 30, 2023

Income tax expense decreased \$318 thousand, or 11.3%, for the first nine months of 2023 compared with the same period in 2022. The effective tax rate for the first nine months of 2023 was 19.3% compared with 19.0% for the same period in 2022. Like the three month period ended September 30, 2023, the increased effective tax rate for 2023 was also the result of lower non-deductible expenses in 2023 compared to 2022.

Financial Condition

General

Assets totaled \$1.4 billion on September 30, 2023 at March 31, 2024, which was a slight decrease an increase of \$3.2 million \$27.9 million or 8% (annualized) from December 31, 2022 December 31, 2023. The asset composition changed during the first nine three months of the year as cash and due from banks decreased by \$3.6 million, interest-bearing deposits in banks decreased increased by \$13.2 million, \$54.3 million and total securities decreased by \$14.7 million, while loans, net of the allowance for credit losses, increased by \$30.5 million \$2.9 million, while total securities decreased by \$27.6 million.

Total liabilities decreased increased by \$6.8 million \$26.4 million during the nine-month three-month period ended September 30, 2023 March 31, 2024, primarily from a \$6.2 million decrease \$25.4 million or 8% (annualized) increase in total deposits. Although total deposits decreased slightly, the from December 31, 2023. The composition of deposits changed was consistent during the first quarter as noninterest-bearing deposits, and savings and interest-bearing deposits, decreased \$23.6 million and \$30.2 million, respectively, while time deposits increased \$47.6 million \$4.9 million, \$15.3 million, and \$5.2 million, respectively from December 31, 2023. The change in composition of the deposit portfolio during the period was attributable to customers shifting deposits into products with higher interest rates.

Total shareholders' equity increased by \$3.6 million \$1.5 million during the first nine three months of 2023, 2024, primarily from a \$5.7 million \$2.3 million increase in retained earnings, which was partially offset by a \$2.2 million an \$811 thousand increase in accumulated other comprehensive loss. The increase in accumulated other comprehensive loss was attributable to higher unrealized losses in the available-for-sale securities portfolio. Retained earnings increased from \$10.5 million as \$3.2 million of net income which was partially offset by \$2.8 million \$941 thousand of cash dividends on common stock and a \$2.0 million decrease from the adoption of CECL on January 1, 2023, stock. The Bank's capital ratios continued to exceed the minimum capital requirements for regulatory purposes.

Loans

Loans totaled \$952.5 million \$973.0 million at September 30, 2023 March 31, 2024, which was a \$32.0 million \$3.5 million or 5% annualized, 2% (annualized) increase from December 31, 2022 December 31, 2023, and a \$46.0 million \$55.0 million, or 5% 6%, increase over September 30, March 31, 2023. The growth in loans over the periods did not have a significant impact on the composition of the loan portfolio. The loan portfolio was primarily comprised of loans secured by one-to-four family residential real estate, loans secured by commercial real estate, and commercial and industrial loans, which totaled 36%, 46%, and 12% of the loan portfolio, respectively, at September 30, 2023 March 31, 2024.

The loan portfolio includes loans that were acquired through business combinations and loans that were purchased through a third-party loan originator. Loans acquired through business combinations included unamortized discounts, net of unamortized premiums totaling \$1.8 million and \$1.9 million, as of March 31, 2024 and December 31, 2023, respectively. Loans purchased from a third-party that originated and serviced loans to health care professionals totaled \$23.6 million as of March 31, 2024, which included unamortized premiums totaling \$7.4 million, compared to loans totaling \$24.6 million as of December 31, 2023, which included unamortized premiums totaling \$7.9 million.

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or pay-off generally are reported at their outstanding unpaid principal balances less the allowance for credit losses and any deferred fees or costs on originated loans. Interest income is accrued and credited to income based on the unpaid principal balance. Loan origination fees, net of certain origination costs, are deferred and recognized as an adjustment of the related loan yield using the interest method. Interest income includes amortization of purchase premiums and discounts, recognized evenly over the life of the loans.

A loan's past due status is based on the contractual due date of the most delinquent payment due. Loans are generally placed on non-accrual status when the collection of principal or interest is 90 days or more past due, or earlier, if collection is uncertain based on an evaluation of the net realizable value of the collateral and the financial strength of the borrower. Loans greater than 90 days past due may remain on accrual status if management determines it has adequate collateral to cover the principal and interest. Loans greater than 90 days past due and still accruing totaled \$368 \$175 thousand and \$524 thousand at September 30, March 31, 2024 and 2023, There were no loans greater than 90 days past due and still accruing at December 31, 2022, respectively. For those loans that are carried on non-accrual status, payments are first applied to principal outstanding. A loan may be returned to accrual status if the borrower has demonstrated a sustained period of repayment performance in accordance with the contractual terms of the loan and there is reasonable assurance the borrower will continue to make payments as agreed. These policies are applied consistently across the loan portfolio.

All interest accrued but not collected for loans that are placed on non-accrual or charged off is reversed against interest income. The interest on these loans is accounted for on the cost-recovery method, until qualifying for return to accrual. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured. When a loan is returned to accrual status, interest income is recognized based on the new effective yield to maturity of the loan.

Any unsecured loan that is deemed uncollectible is charged-off in full. Any secured loan that is considered by management to be uncollectible is partially charged-off and carried at the fair value of the collateral less estimated selling costs. This charge-off policy applies to all loan segments.

Asset Quality

Management classifies non-performing assets as non-accrual loans and OREO. Non-performing assets totaled \$3.1 million \$8.0 million and \$2.9 million \$6.8 million at September 30, 2023 March 31, 2024 and December 31, 2022 December 31, 2023, representing approximately 0.23% 0.55% and 0.21% 0.48% of total assets, respectively. Nonaccrual loans totaled \$3.1 million \$8.0 million and \$2.7 million \$6.8 million at September 30, 2023 March 31, 2024 and December 31, 2022 December 31, 2023, respectively. There was no OREO totaled \$0 at March 31, 2024 and \$185 thousand at September 30, 2023 and December 31, 2022 December 31, 2023, respectively. OREO represents real property taken by the Bank when its customers do not meet the contractual obligation of their loans, either through foreclosure or through a deed in lieu thereof from the borrower and properties originally acquired for, or used in bank operations, but no longer intended to be used for that purpose. OREO is recorded at the lower of cost or fair value, less estimated selling costs, and is marketed by the Bank through brokerage channels. The Bank did not have any consumer mortgage loans secured by real estate properties for which formal foreclosure proceedings were in process as of September 30, 2023 March 31, 2024

On September 30, 2023 March 31, 2024 17.5% commercial and industrial loans comprised 90% of non-performing assets were comprised of and residential real estate loans loans comprised 10%. Non-performing assets could increase due to other loans identified by management as potential problem loans. Other potential problem loans are defined as performing loans that possess certain risks, including the borrower's ability to pay and the collateral value securing the loan, that management has identified that may result in the loans not being repaid in accordance with their terms. Other potential problem loans totaled \$1.7 million and \$2.3 million \$287 thousand at September 30, 2023 March 31, 2024 and December 31, 2022 December 31, 2023, respectively. The amount of other potential problem loans in future periods may be dependent on economic conditions and other factors influencing a customers' ability to meet their debt requirements.

The Company purchased commercial and industrial loans between October 2021 and October 2023 from a third-party finance company that originated and serviced loans to health care professionals. The finance company operated a program that historically provided credit support to the Company through, among other things, the repurchase of their loans and unamortized loan premiums when loans did not pay according to the loan agreements. On March 31, 2024, loans purchased from the finance company totaled \$23.6 million, which was comprised of \$16.2 million of loan balances and unamortized premiums totaling \$7.4 million. As of March 31, 2024, \$3.4 million of these loans were non-accrual including premiums totaling \$1.0 million and thus were individually evaluated. Specific reserves on these individually evaluated loans totaled \$2.4 million and were included in the Company's allowance for credit losses on loans. The remaining \$20.2 million of loans with premiums of \$6.4 million were considered performing and were included in the calculation of the general reserve component of the allowance for credit losses. Premiums are amortized over the life of the loans using the effective interest method. On March 31, 2024, there was a total of 171 loans purchased from the finance company included in the Company's loan portfolio with a weighted average maturity of 7.3 years.

Management believes, based upon its review and analysis, that the Bank has sufficient reserves to cover losses inherent within the loan portfolio. For each period presented, the provision for credit losses charged to expense was based on management's judgment after taking into consideration all factors connected with the collectability of the existing portfolio. Management considers economic conditions, historical losses, past due percentages, internally generated loan quality reports, and other relevant factors when evaluating the loan portfolio. There can be no assurance, however, that an additional provision for credit losses will not be required in the future, including as a result of changes in the qualitative factors underlying management's estimates and judgments, changes in accounting standards, adverse developments in the economy, on a national basis or in the Company's market area, loan growth, or changes in the circumstances of particular borrowers. For further discussion regarding the allowance for credit losses, see "Critical Accounting Policies" above.

Securities

The securities portfolio plays a primary role in the management of the Company's interest rate sensitivity and serves as a source of liquidity. The portfolio is used as needed to meet collateral requirements, such as those related to secure public deposits and balances with the Reserve Bank. The investment portfolio consists of held to maturity, available for sale, and restricted securities. Securities are classified as available for sale or held to maturity based on the Company's investment strategy and management's assessment of the intent and ability to hold the securities until maturity. Management determines the appropriate classification of securities at the time of purchase. If management has the intent and the Company has the ability at the time of purchase to hold the investment securities to maturity, they are classified as investment securities held to maturity and are stated at amortized cost, adjusted for amortization of premiums and accretion of discounts using the interest method. Investment securities which the Company may not hold to maturity are classified as investment securities available for sale, as management has the intent and ability to hold such investment securities for an indefinite period of time, but not necessarily to maturity. Securities available for sale may be sold in response to changes in market interest rates, changes in prepayment risk, increases in loan demand, general liquidity needs and other similar factors and are carried at estimated fair value. Restricted securities, including Federal Home Loan Bank, Federal Reserve Bank, and Community Bankers' Bank stock, are generally viewed as long-term investments because there is minimal market for the stock and are carried at cost.

On September 30, 2023 March 31, 2024 securities totaled \$300.2 million \$275.6 million, a decrease of \$17.8 million \$27.6 million, or 5.6% 9.1%, from \$318.0 million \$303.2 million at December 31, 2022 December 31, 2023. Investment securities are comprised of U.S. Treasury securities, U.S. agency and mortgage-backed securities, obligations of state and political subdivisions, corporate debt securities, and restricted securities. As of September 30, 2023 March 31, 2024, neither the Company nor the Bank held any derivative financial instruments in their respective investment security portfolios. Gross unrealized gains in the available for sale portfolio totaled \$64 \$51 thousand and \$99 \$61 thousand at September 30, 2023 March 31, 2024 and December 31, 2022 December 31, 2023, respectively. Gross unrealized losses in the available for sale portfolio totaled \$28.4 million \$22.2 million and \$24.0 million \$20.7 million at September 30, 2023 March 31, 2024 and December 31, 2022 December 31, 2023, respectively. There were no gross Gross unrealized gains in the held to maturity portfolio totaled \$40 thousand and \$107 thousand at September 30, 2023 March 31, 2024 and December 31, 2022 December 31, 2023, respectively. Gross unrealized losses in the held to maturity portfolio totaled \$15.2 million \$11.9 million and \$11.4 million \$10.8 million at September 30, 2023 March 31, 2024 and December 31, 2022 December 31, 2023, respectively. The change in the unrealized gains and losses of investment securities from December 31, 2022 December 31, 2023 to September 30, 2023 March 31, 2024 was related to changes in market interest rates and was not related to credit concerns of the issuers.

On September 1, 2022, the Bank transferred 24 securities designated as available for sale with a combined book value of \$82.2 million, market value of \$74.4 million, and an unrealized loss of \$7.8 million, to securities designated held to maturity. The unrealized loss is being amortized monthly over the life of the securities with an increase to the carrying value of securities and a decrease to the related accumulated other comprehensive loss, which is included in the shareholders' equity section of the Company's balance sheet. The amortization of the unrealized loss on the transferred securities totaled \$1.2 million, \$367 thousand, or \$972 \$290 thousand net of tax, for the first nine three months of 2023, 2024. Securities designated as held to maturity are carried on the balance sheet at amortized cost, while securities designated as available for sale are carried at fair market value.

Deposits

Deposits totaled \$1.2 billion \$1.3 billion on September 30, 2023 March 31, 2024, which was a \$6.2 million decrease \$25.4 million or 8% (annualized) increase from December 31, 2022 December 31, 2023. Noninterest-bearing deposits increased \$4.8 million, savings and interest-bearing deposits increased \$15.3 million, and a \$30.3 million, or 2%, decrease from September 30, 2022 time deposits increased \$5.2 million. The composition of the deposit portfolio has changed compared to remained consistent with the prior periods. Noninterest-bearing deposits, savings and interest-bearing deposits, and time deposits, totaled 33%, 52%, and 15%, of total deposits, respectively on September 30, 2023, compared to 34%, 55%, and 11% on December 31, 2022, and 34%, 55%, and 11%, on September 30, 2022. The change in deposit composition was attributable to deposits that shifted into products paying higher interest rates. period.

Liquidity

Liquidity sources available to the Bank, including interest-bearing deposits in banks, unpledged securities available for sale, at fair value, unpledged securities held-to-maturity, at par, eligible to be pledged to the Federal Reserve Bank through its Bank Term Funding Program, and available available lines of credit totaled \$532.1 million \$554.8 million on September 30, 2023, March 31, 2024 and \$417.2 million \$562.3 million on December 31, 2022 March 31, 2023.

The Bank maintains liquidity to fund loan growth and to meet the potential demand from its deposit customers, including potential volatile deposits. The estimated amount of uninsured customer deposits totaled \$346.9 million \$391.9 on September 30, 2023 March 31, 2024, \$368.2 million on December 31, 2023, and \$261.7 million \$407.5 million on December 31, 2022 March 31, 2023. Excluding Excluding municipal deposits, the estimated amount of uninsured customer customer deposits totaled \$268.4 million \$308.6 on September 30, 2023 March 31, 2024, \$293.7 million on December 31, 2023, and \$185.3 million \$330.4 million on December 31, 2022 March 31, 2023. The Bank also has access to off-balance sheet liquidity through its available lines of credit from other institutions, which totaled \$347.1 million at September 30, 2023, \$287.3 million at December 31, 2022, and \$379.0 million at September 30, 2023. The available lines of credit were comprised of secured and unsecured lines of credit. The Bank had no borrowings on the lines of credit at September 30, 2023, December 31, 2022, or September 30, 2023.

Capital Resources

The adequacy of the Company's capital is reviewed by management on an ongoing basis with reference to the size, composition, and quality of the Company's asset and liability levels and consistent with regulatory requirements and industry standards. Management seeks to maintain a capital structure that will assure an adequate level of capital to support anticipated asset growth and absorb potential losses. The Company meets eligibility criteria of a small bank holding company in accordance with the Federal Reserve Board's Small Bank Holding Company Policy Statement and is not obligated to report consolidated regulatory capital.

The Bank is subject to capital rules adopted by federal bank regulators that implemented the Basel III regulatory capital reforms adopted by the Basel Committee on Banking Supervision (the Basel Committee), and certain changes required by the Dodd-Frank Act.

The minimum capital level requirements applicable to the Bank under the final rules are as follows: a common equity Tier 1 capital ratio of 4.5%; a Tier 1 capital ratio of 6%; a total capital ratio of 8%; and a Tier 1 leverage ratio of 4% for all institutions. There is also a capital conservation buffer, which is 2.5% above the regulatory minimum capital requirements. If capital levels fall below the required minimum ratios plus the buffer, institutions are subject to limitations on paying dividends, engaging in share repurchases, and paying discretionary bonuses. These limitations establish a maximum percentage of eligible retained income that could be utilized for such actions. This results in the following minimum

capital ratios required to exceed the buffer: a common equity Tier 1 capital ratio of 7.0%, a Tier 1 capital ratio of 8.5%, and a total capital ratio of 10.5%. Management believes, as of **September 30, 2023** **March 31, 2024** and **December 31, 2022**, **December 31, 2023**, that the Bank met all capital adequacy requirements to which it is subject, including the capital conservation buffer.

The following table shows the Bank's regulatory capital ratios at **September 30, 2023** **March 31, 2024**:

	First Bank
Total capital to risk-weighted assets	14.80 14.45 %
Tier 1 capital to risk-weighted assets	13.86 13.20 %
Common equity Tier 1 capital to risk-weighted assets	13.86 13.20 %
Tier 1 capital to average assets	9.96 9.19 %
Capital conservation buffer ratio(1)	6.80 6.45 %

- (1) Calculated by subtracting the regulatory minimum capital ratio requirements from the Company's actual ratio for Common equity Tier 1, Tier 1, and Total risk based capital. The lowest of the three measures represents the Bank's capital conservation buffer ratio.

The prompt corrective action framework is designed to place restrictions on insured depository institutions if their capital levels begin to show signs of weakness. Under the prompt corrective action requirements, which are designed to complement the capital conservation buffer, insured depository institutions are required to meet the following capital level requirements in order to qualify as "well capitalized:" a common equity Tier 1 capital ratio of 6.5%; a Tier 1 capital ratio of 8%; a total capital ratio of 10%; and a Tier 1 leverage ratio of 5%. The Bank met the requirements to qualify as "well capitalized" as of **September 30, 2023** **March 31, 2024** and **December 31, 2022** **2023**.

During the fourth quarter of 2022, the Board of Directors of the Company authorized a stock repurchase plan pursuant to which the Company could repurchase up to \$5.0 million of its outstanding common stock through December 31, 2023. The Company repurchased 37,532 shares under this plan during the first nine months of 2023 at an average price of \$15.14 per share.

Contractual Obligations

There have been no material changes outside the ordinary course of business to the contractual obligations disclosed in the Company's Annual Report on Form 10-K for the year ended **December 31, 2022** **December 31, 2023**.

Off-Balance Sheet Arrangements

The Company, through the Bank, is a party to credit related financial instruments with risk not reflected in the consolidated financial statements in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit, standby letters of credit, and commercial letters of credit. Such commitments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the consolidated balance sheets. The Bank's exposure to credit loss is represented by the contractual amount of these commitments. The Bank follows the same credit policies in making commitments as it does for on-balance sheet instruments.

Commitments to extend credit, which amounted to **\$171.9 million** **\$214.7 million** at **September 30, 2023** **March 31, 2024**, and **\$158.3 million** **\$170.2 million** at **December 31, 2022** **March 31, 2023**, are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. The commitments for lines of credit may expire without being drawn upon. Therefore, the total commitment amounts do not necessarily represent future cash requirements. The amount of collateral obtained, if it is deemed necessary by the Bank, is based on management's credit evaluation of the customer.

Unfunded commitments under commercial lines of credit, revolving credit lines, and overdraft protection agreements are commitments for possible future extensions of credit to existing customers. These lines of credit are collateralized as deemed necessary and may or may not be drawn upon to the total extent to which the Bank is committed.

On January 1, 2023, the Company recorded an adjustment for unfunded commitments of \$153 thousand for the adoption of ASC Topic 326. The Company recorded an additional provision for credit losses for unfunded commitments of \$36 thousand during the nine months ended September 30, 2023. At September 30, 2023, the liability for credit losses on off-balance sheet exposures included in other liabilities was \$189 thousand.

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

necessary. At **September 30, 2023** **March 31, 2024** and December 31, **2022** **2023**, the Bank had **\$12.1 million** **\$17.0 million** and **\$18.0 million** **\$17.6 million** in outstanding standby letters of credit, respectively.

On April 21, 2020, the Company entered into interest rate swap agreements related to its outstanding junior subordinated debt. The Company uses derivatives to manage exposure to interest rate risk through the use of interest rate swaps. Interest rate swaps involve the exchange of fixed and variable rate interest payments between two parties, based on a common notional principal amount and maturity date with no exchange of underlying principal amounts.

The interest rate swaps qualified and are designated as cash flow hedges. The Company's cash flow hedges effectively modify the Company's exposure to interest rate risk by converting variable rates of interest on \$9.0 million of the Company's junior subordinated debt to fixed rates of interest. The cash flow hedges end and the junior subordinated debt matures between June 2034 and October 2036. The cash flow hedges' total notional amount is \$9.0 million. At **September 30, 2023** **March 31, 2024**, the cash flow hedges had a fair value of **\$3.1 million** **\$2.7 million**, which is recorded in other assets. The net gain/loss on the cash flow hedges is recognized as a component of other comprehensive (loss) income and reclassified into earnings in the same period(s) during which the hedged transactions affect earnings. The Company's derivative financial instruments are described more fully in Note 10 to the Consolidated Financial Statements.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Not required.

Item 4. Controls and Procedures

The Company maintains disclosure controls and procedures that are designed to provide assurance that information required to be disclosed by the Company in the reports that it files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized, and reported within the time periods required by the SEC and that such information is accumulated and communicated to management, including the Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure. An evaluation of the effectiveness of the design and operation of the Company's disclosure controls and procedures as of **September 30, 2023** **March 31, 2024** was carried out under the supervision and with the participation of management, including the Company's Chief Executive Officer and Chief Financial Officer. Based on and as of the date of such evaluation, the aforementioned officers concluded that the Company's disclosure controls and procedures were effective.

The Company's management is also responsible for establishing and maintaining adequate internal control over financial reporting. There were no changes in the Company's internal control over financial reporting identified in connection with the evaluation of it that occurred during the Company's last fiscal quarter that materially affected, or are reasonably likely to materially affect, internal control over financial reporting.

PART II – OTHER INFORMATION

Item 1. Legal Proceedings

There are no material pending legal proceedings, other than ordinary routine litigation incidental to the Company's business, to which the Company is a party or to which the property of the Company is subject.

Item 1A. Risk Factors

There Except for the following risks related to the acquisition of Touchstone, **there** were no material changes to the Company's risk factors as disclosed in its Annual Report on Form 10-K for the year ended **December 31, 2022** **December 31, 2023**.

Risks Related to the Acquisition of Touchstone

Combining Touchstone into the Company may be more difficult, costly or time-consuming than we expect.

The success of the Merger will depend, in part, on the Company's ability to realize the anticipated benefits and cost savings from combining the business of Touchstone into the business of the Company without materially disrupting the existing customer relationships of Touchstone or the Company. If the Company is not able to achieve these objectives, the anticipated benefits and cost savings of the Merger may not be realized fully, or at all, or may take longer to realize than expected.

The success of the Merger will depend, in part, on the Company's ability to successfully combine the businesses of the Company and Touchstone. To realize these anticipated benefits, the Company will integrate Touchstone's business into its own. The integration process in the Merger could result in the disruption of ongoing business, inconsistencies in standards, controls, procedures, and policies that affect adversely the Company's ability to maintain relationships with customers and employees or achieve the anticipated benefits of the Merger. If the Company experiences difficulties with the integration process, the anticipated benefits of the Merger may not be realized, fully or at all, or may take longer to realize than expected. As with any merger of financial institutions, there also may be disruptions that cause the Company to lose customers or cause customers to withdraw their

deposits from Touchstone or the Bank, or other unintended consequences that could have a material adverse effect on the Company's results of operations or financial condition after the Merger. These integration matters could have an adverse effect on the Company for an indeterminate period after consummation of the Merger.

The Company may not be able to effectively integrate the operations of Touchstone into the Bank.

The future operating performance of the Company and the Bank will depend, in part, on the success of the merger of Touchstone with and into the Bank. The success of the subsidiary bank merger will, in turn, depend on a number of factors, including the Company's ability to (i) integrate the operations and branches of Touchstone and the Bank, (ii) retain the deposits and customers of Touchstone and the Bank, (iii) control the incremental increase in noninterest expense arising from the Merger in a manner that enables the combined bank to improve its overall operating efficiencies, and (iv) retain and integrate the appropriate personnel of Touchstone into the operations of the Bank, and reduce overlapping bank personnel. The integration of Touchstone and the Bank will require the dedication of the time and resources of the Bank's management and may temporarily distract management's attention from the day-to-day business of the Bank. If the Bank is unable to successfully integrate Touchstone, the Bank may not be able to realize expected operating efficiencies and eliminate redundant costs.

Regulatory approvals may not be received, may take longer than expected, or may impose conditions that are not presently anticipated or that could have an adverse effect on the combined company following the Merger.

Before the Merger may be completed, the Company and the Bank must obtain approvals from the Federal Reserve and the Virginia Bureau of Financial Institutions. Other approvals, waivers or consents from regulators may also be required. These regulators may impose conditions on the completion of the Merger or require changes to the terms of the Merger. Such conditions or changes and the process of obtaining regulatory approvals could have the effect of delaying completion of the Merger and the subsidiary bank merger, imposing additional costs on the combined company or limiting the revenues of the combined company, any of which might have an adverse effect on the combined company following the Merger.

A significant delay in the completion of the Merger could have a material adverse effect on the Company and Touchstone as a combined company.

The merger agreement with Touchstone is subject to a number of conditions that must be fulfilled in order to complete the Merger. Those conditions include, among others: (1) approval of the Merger by the Company's and Touchstone's shareholders, (2) receipt of all required approvals from bank regulatory authorities and expiration of all applicable waiting periods, (3) absence of any law or order prohibiting or restricting the completion of the Merger, and (4) effectiveness of the Company's registration statement filed with the SEC. Certain costs relating to the Merger, such as legal, accounting and financial advisory fees, must be paid even if the Merger is not completed. If the Merger is not completed, the Company would have to recognize these expenses and its management would have committed substantial time and resources without realizing the expected benefits of the Merger. If these conditions to the completion of the Merger are not fulfilled when expected and, as a result, the completion of the Merger is delayed, the diversion of management attention from pursuing other opportunities, the constraints in the merger agreement on the ability to make significant changes to each company's ongoing business during the pendency of the Merger, the incurrence of additional merger related expenses, and other market and economic factors could have a material adverse effect on the combined company's business, financial condition and results of operations.

The Company and Touchstone will be subject to business uncertainties and contractual restrictions while the Merger is pending.

Uncertainty about the effect of the Merger on employees and customers may have an adverse effect on the Company and Touchstone. These uncertainties may impair the Company's and Touchstone's ability to attract, retain and motivate key personnel until the Merger is completed, and could cause customers and others that deal with the Company and Touchstone to seek to change existing business relationships with the Company and Touchstone. Retention of certain employees by the Company and Touchstone may be challenging while the Merger is pending, as certain employees may experience uncertainty about their future roles with the Company or Touchstone. If key employees depart because of issues relating to the uncertainty and difficulty of integration or a desire not to remain with the Company or Touchstone, the Company's or Touchstone's business, or the business of the combined company following the Merger, could be harmed. In addition, subject to certain exceptions, the Company and Touchstone have each agreed to operate its business in the ordinary course prior to closing and refrain from taking certain specified actions until the Merger occurs, which may prevent the Company from pursuing attractive business opportunities that may arise prior to the completion of the Merger.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

Issuer Purchases of Equity Securities

During the fourth quarter of 2022, the Board of Directors of the Company authorized a stock repurchase plan pursuant to which the Company could repurchase up to \$5.0 million of its outstanding common stock. The repurchase plan was publicly announced on October 23, 2022. Repurchases under the plan can be made through privately negotiated transactions or in the open market in accordance with Securities and Exchange Commission rules. The Company's Board of Directors authorized the purchase plan through December 31, 2023, unless the entire amount authorized to repurchase has been acquired before that date. **None**

The following table summarizes the Company's purchases of its common stock during the three months ended September 30, 2023 (dollars in thousands, except per share data):

	Total Number of Shares Purchased	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plan	Maximum Number (or Approximate Dollar Value) of Shares that May Yet Be Purchased Under the Plan	
				Shares	
				Shares	Shares
July 1, 2023 - July 31, 2023	1,078	\$ 16.54	1,078	\$ 4,475,675	
August 1, 2023 - August 31, 2023	1,196	17.05	1,196	4,455,279	

September 1, 2023 - September 30, 2023	1,400	16.74	1,400	4,431,843
	<u>3,674</u>	<u>\$ 16.78</u>	<u>3,674</u>	<u>\$ 4,431,843</u>

Item 3. Defaults upon Senior Securities

None

Item 4. Mine Safety Disclosures

None

Item 5. Other Information

None During the three months ended March 31, 2024, none of our directors or officers (as defined in Rule 16a-1(f) of the Exchange Act) informed us of the adoption or termination of any Rule 10b5-1 trading arrangement or non-Rule 10b5-1 trading arrangement (as such terms are defined in Item 408 of Regulation S-K).

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Item 6. Exhibits

The following documents are attached hereto as Exhibits:

- 10.12.1 [Form Agreement and Plan of Merger, dated as of March 25, 2024, by and between First National Corporation Restricted Stock Unit Agreement](#)
- 10.2 [Form of and Touchstone Bankshares, Inc. \(incorporated by reference to Exhibit 2.1 to First National Corporation Director Stock Award Agreement Corporation's Current Report on Form 8-K filed March 26, 2024\).](#)
- 31.1 [Certification of Chief Executive Officer, Section 302 Certification.](#)
- 31.2 [Certification of Chief Financial Officer, Section 302 Certification.](#)
- 32.1 [Certification of Chief Executive Officer Pursuant to 18 U.S.C. Section 1350.](#)
- 32.2 [Certification of Chief Financial Officer Pursuant to 18 U.S.C. Section 1350.](#)
- 101 The following materials from First National Corporation's Quarterly Report on Form 10-Q for the quarter ended **September 30, 2023** **March 31, 2024** formatted in Inline eXtensible Business Reporting Language (XBRL): (i) Consolidated Balance Sheets, (ii) Consolidated Statements of Income, (iii) Consolidated Statements of Comprehensive Income (Loss) (iv) Consolidated Statements of Cash Flows, (v) Consolidated Statements of Shareholders' Equity, and (vi) Notes to Consolidated Financial Statements.
- 104 The cover page from First National Corporation's Quarterly Report on Form 10-Q for the quarter ended **September 30, 2023** **March 31, 2024**, formatted in Inline XBRL (included with Exhibit 101).

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

FIRST NATIONAL CORPORATION
(Registrant)

/s/ Scott C. Harvard

Scott C. Harvard
President and Chief Executive Officer

November 13, 2023

May 14, 2024

Date

/s/ M. Shane Bell

M. Shane Bell
Executive Vice President and Chief Financial Officer

November 13, 2023 May 14, 2024

Date

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EXHIBIT 10.1

FIRST NATIONAL CORPORATION

RESTRICTED STOCK UNIT AGREEMENT

THIS RESTRICTED STOCK UNIT AGREEMENT (the "Agreement"), dated as of the _____ day of _____, 20____, by and between **FIRST NATIONAL CORPORATION**, a Virginia corporation (the "Company"), and _____ evidences the grant on _____, 20____ ("Award Date") by the Company of an award of restricted stock units (the "Restricted Stock Unit Award") to you and your acceptance of the Restricted Stock Unit Award.

The grant of this Restricted Stock Unit Award is made in accordance with the First National Corporation 2023 Stock Incentive Plan (the "Plan"), a copy of which is available from the Company upon request. The terms of the Plan are incorporated into this Agreement by reference. In the case of any inconsistency between the Plan and this Agreement, the terms of the Plan shall control. Any term used in this Agreement that is defined in the Plan shall have the same meaning given to that term in the Plan. References in this Agreement to the "Company" also shall mean and refer to any business entity that, directly or indirectly through one or more intermediaries, controls, is controlled by, or is under common control with the Company, unless the context otherwise requires.

1. Award of Restricted Stock Units.

a. The Board awards you _____ restricted stock units (the "Restricted Stock Units"). Each Restricted Stock Unit represents the right to receive one share of the common stock of the Company ("Company Stock"), subject to the vesting schedule in Section 2 and the other terms and conditions of this Agreement and the Plan.

b. The Restricted Stock Units shall be credited to a separate account maintained for you on the books and records of the Company (the "Account"). All amounts credited to the Account shall continue for all purposes to be part of the general assets of the Company.

2. **Vesting.** Except as otherwise provided herein, provided that you remain an employee of the Company or an Affiliate through the applicable vesting date, the Restricted Stock Units will vest in accordance with the following schedule (the period during which the restrictions apply, the "Restricted Period"):

Vesting Date	Number of Restricted Stock Units That Vest
_____	_____
_____	_____

Once vested, the Restricted Stock Units become "Vested Units" and shares of Company Stock representing the Vested Units will be issued in accordance with the settlement procedures set forth in Section 6.

3. Effect of Termination.

a. If your employment is terminated for any reason other than your death or Disability before the vesting dates, all Restricted Stock Units that are not then vested shall be automatically forfeited upon such termination of employment and neither the Company nor any Affiliate shall have any further obligation to you under this Agreement.

b. If you die or become Disabled while employed, all Restricted Stock Units that are not vested shall become Vested Units as of the date of your death or Disability.

4. **Restrictions.** Subject to any exceptions set forth in this Agreement or the Plan, during the Restricted Period and until such time as the Restricted Stock Units are settled in accordance with Section 6, the Restricted Stock Units or the rights relating thereto may not be assigned, alienated, pledged, attached, sold or otherwise transferred or encumbered by you. Any attempt to assign, alienate, pledge, attach, sell or otherwise transfer or encumber the Restricted Stock Units or the rights relating thereto shall be wholly ineffective and, if any such attempt is made, the Restricted Stock Units will be forfeited by you and all of your rights to such units shall immediately terminate without any payment or consideration by the Company. Notwithstanding any other provision in this Agreement to the contrary, no shares of Company Stock underlying the Restricted Stock Units may be sold until the expiration of six months from the Date of Grant.

5. Rights as a Shareholder.

a. You shall not have any rights of a shareholder with respect to the shares of Company Stock underlying the Restricted Stock Units unless and until the Restricted Stock Units vest and are settled by the issuance of such shares of Company Stock.

b. Upon and following the settlement of the Restricted Stock Units, you shall be the record owner of the shares of Company Stock underlying the Restricted Stock Units unless and until such shares are sold or otherwise disposed of, and as record owner shall be entitled to all rights of a shareholder of the Company (including voting rights).

6. **Settlement of Vested Restricted Stock Units.** Subject to Section 10, effective as of the vesting date the Company shall: (i) issue and deliver to you the number of shares of Company Stock equal to the number of Vested Units; and (ii) enter your name on the books of the Company as the shareholder of record with respect to the shares of Company Stock delivered to you.

7. **No Right to Continued Employment.** Neither the Plan nor this Agreement shall confer upon you any right to continued employment by the Company nor shall it interfere in any way with the right of the Company to terminate your employment at any time.

8. Change in Capital Structure; Change in Control. In the event of changes in the outstanding shares of Company Stock or in the capital structure of the Company by reason of any stock or extraordinary cash dividend, stock split, recapitalization, reorganization, merger, or other relevant change in capitalization occurring after the Award Date, the number and kind of shares of stock or securities of the Company to be issued shall be equitably adjusted as to the number, price or kind of consideration subject to this Restricted Stock Unit Award to the extent necessary to preserve the economic intent of the Restricted Stock Unit Award. If the adjustment would produce fractional shares, the Company may adjust appropriately the number of shares covered by this Restricted Stock Unit Award so as to eliminate the fractional shares. Further, in the event of a Change in Control, Section 15 of the Plan shall apply.

9. Governing Law. This Agreement is governed by the laws of the Commonwealth of Virginia.

10. Tax Liability and Withholding.

a. You shall be required to pay to the Company, and the Company shall have the right to deduct from any compensation paid to you pursuant to the Plan, the amount of any required withholding taxes in respect of the Restricted Stock Units and to take all such other action as the Committee deems necessary to satisfy all obligations for the payment of such withholding taxes. The Committee may permit you to satisfy any federal, state or local tax withholding obligation by any of the following means, or by a combination of such means:

i. tendering a cash payment;

ii. authorizing the Company to withhold shares of Company Stock from the shares of Company Stock otherwise issuable or deliverable to you as a result of the vesting of the Restricted Stock Units; provided, however, that no shares of Company Stock shall be withheld with a value exceeding the minimum amount of tax required to be withheld by law; or

iii. delivering to the Company previously owned and unencumbered shares of Company Stock.

b. Notwithstanding any action the Company takes with respect to any or all income tax, payroll tax, or other tax-related withholding ("Tax-Related Items"), the ultimate liability for all Tax-Related Items is and remains your responsibility and the Company: (i) makes no representation or undertakings regarding the treatment of any Tax-Related Items in connection with the grant, vesting or settlement of the Restricted Stock Units or the subsequent sale of any shares; and (ii) does not commit to structure the Restricted Stock Units to reduce or eliminate your liability for Tax-Related Items.

11. Acceptance of Award. By signing below, you confirm your acceptance of the Restricted Stock Unit Award and agreement to the terms and conditions set forth in this Agreement, which, together with the terms of the Plan, shall become the Company's Restricted Stock Unit Award Agreement with you. You also agree to all of the terms and conditions of the Plan. This Agreement will not be effective until it is signed and returned.

12. Entire Agreement, Amendment. This Agreement constitutes the entire agreement between the Company and you and shall be binding upon your legatees, distributees, and personal representatives and the successors of the Company. This Agreement may only be amended by a writing signed by both the Company and you.

13. Compliance with Law. The issuance and transfer of shares of Company Stock shall be subject to compliance by the Company and you with all applicable requirements of federal and state securities laws and with all applicable requirements of any stock exchange on which the Company's shares of common stock may be listed. No shares of Company Stock shall be issued or transferred unless and until any then applicable requirements of state and federal laws and regulatory agencies have been fully complied with to the satisfaction of the Company and its counsel.

14. Notices. Any notice required to be delivered to the Company under this Agreement shall be in writing and addressed to the President and Chief Executive Officer of the Company at the Company's principal corporate offices. Any notice required to be delivered to you under this Agreement shall be in writing and addressed to you at your address as shown in the records of the Company. Either party may designate another address in writing (or by such other method approved by the Company) from time to time.

15. Section 409A. This Agreement is intended to comply with Section 409A of the Internal Revenue Code of 1986, as amended (the "Code") or an exemption thereunder and shall be construed and interpreted in a manner that is consistent with the requirements for avoiding additional taxes or penalties under Section 409A of the Code. Notwithstanding the foregoing, the Company makes no representations that the payments and benefits provided under this Agreement comply with Section 409A of the Code and in no event shall the Company be liable for all or any portion of any taxes, penalties, interest or other expenses that may be incurred by you on account of non-compliance with Section 409A of the Code.

IN WITNESS WHEREOF, the parties hereto have executed this Agreement as of the date first written above.

FIRST NATIONAL CORPORATION

By

(Printed Name)

PARTICIPANT

By

(Printed Name)

EXHIBIT 10.2

FIRST NATIONAL CORPORATION

DIRECTOR STOCK AWARD AGREEMENT

This Stock Award Agreement (the "Agreement"), dated as of [_____._____._____.], by and between First National Corporation (the "Company") and [Recipient] evidences the grant on [_____._____._____.] (the "Grant Date") by the Company of an award of common stock (the "Stock Award") to you and your acceptance of the Stock Award.

The grant of this Stock Award is made in accordance with the First National Corporation 2023 Stock Incentive Plan (the "Plan"), a copy of which is available from the Company upon request. The terms of the Plan are incorporated into this Agreement by reference. In the case of any inconsistency between the Plan and this Agreement, the terms of the Plan shall control. Any term used in this Agreement that is defined in the Plan shall have the same meaning given to that term in the Plan. References in this Agreement to the "Company" also shall mean and refer to any business entity that, directly or indirectly through one or more intermediaries, controls, is controlled by, or is under common control with the Company, unless the context otherwise requires.

1. **Award of Stock.** The Company awards you [] shares of common stock of the Company ("Company Stock"), subject to the terms and conditions of this Agreement and the Plan.

2. **Rights as a Shareholder.**

- (a) You shall not have any rights of a shareholder with respect to the Company Stock until the issuance of such shares of Company Stock.
- (b) Upon and following the issuance of the Company Stock, you shall be the record owner of the shares of the Company Stock unless and until such Company Stock are sold or otherwise disposed of, and as record owner shall be entitled to all rights of a shareholder of the Company (including voting rights).

3. **Issuance of Shares.** Effective as of the Grant Date, the Company shall: (i) issue and deliver to you the number of shares of Company Stock granted by the Company; and (ii) enter your name on the books of the Company as the shareholder of record with respect to the shares of Company Stock delivered to you.

4. **Governing Law.** This Agreement is governed by the laws of the Commonwealth of Virginia.

5. **Tax Liability.** The ultimate liability for all income taxes associated with the Stock Award is and remains your responsibility and the Company: (i) makes no representation or undertakings regarding the treatment of any income tax related items in connection with the grant, or issuance of the Company Stock or the subsequent sale of any shares; and (ii) does not commit to structure the Stock Award to reduce or eliminate your liability for such income tax items.

6. **Acceptance of Award.** By signing below, you confirm your acceptance of the Stock Award and agreement to the terms and conditions set forth in this Agreement, which, together with the terms of the Plan, shall become the Company's Stock Award Agreement with you. You also agree to all of the terms and conditions of the Plan. This Agreement will not be effective until it is signed and returned.

7. **Entire Agreement, Amendment.** This Agreement constitutes the entire agreement between the Company and you and shall be binding upon your legatees, distributees, and personal representatives and the successors of the Company. This Agreement may only be amended by a writing signed by both the Company and you.

8. **Compliance with Law.** The issuance and transfer of shares of Company Stock shall be subject to compliance by the Company and you with all applicable requirements of federal and state securities laws and with all applicable requirements of any stock exchange on which the Company's shares of common stock may be listed. No shares of Company Stock shall be issued or transferred unless and until any then applicable requirements of state and federal laws and regulatory agencies have been fully complied with to the satisfaction of the Company and its counsel.

9. **Notices.** Any notice required to be delivered to the Company under this Agreement shall be in writing and addressed to the President and Chief Executive Officer of the Company at the Company's principal corporate offices. Any notice required to be delivered to you under this Agreement shall be in writing and addressed to you at your address as shown in the records of the Company. Either party may designate another address in writing (or by such other method approved by the Company) from time to time.

10. **Section 409A.** This Agreement is intended to comply with Section 409A of the Internal Revenue Code of 1986, as amended (the "Code") or an exemption thereunder and shall be construed and interpreted in a manner that is consistent with the requirements for avoiding additional taxes or penalties under Section 409A of the Code. Notwithstanding the foregoing, the Company makes no representations that the payments and benefits provided under this Agreement comply with Section 409A of the Code and in no event shall the Company be liable for all or any portion of any taxes, penalties, interest or other expenses that may be incurred by you on account of non-compliance with Section 409A of the Code.

Signatures appear on the following page.

IN WITNESS WHEREOF, the parties hereto have executed this Agreement as of the date first written above.

FIRST NATIONAL CORPORATION

By:

Scott C. Harvard

President and Chief Executive Officer

[Recipient Name]

[Chairman of the Board / Director]

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EXHIBIT 31.1

CERTIFICATION OF CHIEF EXECUTIVE OFFICER
SECTION 302 CERTIFICATION

I, Scott C. Harvard, certify that:

1. I have reviewed this quarterly report on Form 10-Q of First National Corporation for the period ended **September 30, 2023** **March 31, 2024**;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
- a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
- a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

November 13, 2023 May 14, 2024

Date

/s/ Scott C. Harvard

Scott C. Harvard

President and Chief Executive Officer

EXHIBIT 31.2

CERTIFICATION OF CHIEF FINANCIAL OFFICER
SECTION 302 CERTIFICATION

I, M. Shane Bell, certify that:

1. I have reviewed this quarterly report on Form 10-Q of First National Corporation for the period ended **September 30, 2023** **March 31, 2024**;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

- a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
- a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

November 13, 2023 May 14, 2024

Date

/s/ M. Shane Bell

M. Shane Bell

Executive Vice President and Chief Financial Officer

EXHIBIT 32.1

**CERTIFICATION OF CHIEF EXECUTIVE OFFICER
PURSUANT TO 18 U.S.C. SECTION 1350**

In connection with the Form 10-Q of First National Corporation for the period ended **September 30, 2023** **March 31, 2024**, I, Scott C. Harvard, President and Chief Executive Officer of First National Corporation, hereby certify pursuant to 18 U.S.C. §1350, as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002, that, to the best of my knowledge and belief:

- (1) such Form 10-Q for the period ended **September 30, 2023** **March 31, 2024**, fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) the information contained in such Form 10-Q for the period ended **September 30, 2023** **March 31, 2024**, fairly presents, in all material respects, the financial condition and results of operations of First National Corporation.

November 13, 2023 May 14, 2024

Date

/s/ Scott C. Harvard

Scott C. Harvard

President and Chief Executive Officer

EXHIBIT 32.2

CERTIFICATION OF CHIEF FINANCIAL OFFICER
PURSUANT TO 18 U.S.C. SECTION 1350

In connection with the Form 10-Q of First National Corporation for the period ended **September 30, 2023** **March 31, 2024**, I, M. Shane Bell, Executive Vice President and Chief Financial Officer of First National Corporation, hereby certify pursuant to 18 U.S.C. §1350, as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002, that, to the best of my knowledge and belief:

- (1) such Form 10-Q for the period ended **September 30, 2023** **March 31, 2024**, fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) the information contained in such Form 10-Q for the period ended **September 30, 2023** **March 31, 2024**, fairly presents, in all material respects, the financial condition and results of operations of First National Corporation.

November 13, 2023 **May 14, 2024**

Date

/s/ M. Shane Bell

M. Shane Bell

Executive Vice President and Chief Financial Officer

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