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 June 30, 2023
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: 0-15536

CODORUS VALLEY BANCORP, INC.

(Exact name of registrant as specified in its charter)

Pennsylvania	**23-2428543**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

105 Leader Heights Road, York, Pennsylvania 17403
(Address of principal executive offices)(Zip code)

717-747-1519
(Registrant's telephone number, including area code)

Not Applicable
(Former name, former address and former fiscal year,
if changed since the last report.)

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

Title of each class	Trading Symbol	Name of each exchange on which registered
Common Stock, $2.50 par value	CVLY	NASDAQ Global Market

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See 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 ☐	Accelerated filer ☐
Non-accelerated filer ☒	Smaller reporting company ☒
	Emerging growth company ☐

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

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

APPLICABLE ONLY TO CORPORATE ISSUERS

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date. On July 31, 2023, 9,611,110 shares of common stock, par value $2.50, were outstanding.

Codorus Valley Bancorp, Inc.
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PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

Codorus Valley Bancorp, Inc.
Consolidated Balance Sheets
(Unaudited)

(dollars in thousands, except per share data)		**June 30, 2023**		**December 31, 2022**
Assets				
Interest bearing deposits with banks	$	68,946	$	99,777
Cash and due from banks		20,670		20,662
Total cash and cash equivalents		89,616		120,439
Securities, available-for-sale, at fair value (amortized cost $389,292 net of allowance for credit losses of $0)		342,691		345,457
Restricted investment in bank stocks, at cost		3,917		955
Loans held for sale		428		154
Loans (net of deferred fees of $3,883 - 2023 and $3,813 - 2022)		1,681,688		1,632,857
Less-allowance for credit losses (1)		(20,681)		(20,736)
Net loans		1,661,007		1,612,121
Premises and equipment, net		19,672		21,136
Operating leases right-of-use assets		2,772		3,072
Goodwill		2,301		2,301
Other assets		93,313		89,417
Total assets	$	2,215,717	$	2,195,052
Liabilities				
Deposits				
Noninterest bearing	$	408,290	$	463,853
Interest bearing		1,474,383		1,479,366
Total deposits		1,882,673		1,943,219
Short-term borrowings		83,320		11,605
Long-term debt		11,535		11,550
Subordinate debentures - face amount $31,000 (less discount and debt issuance cost of $196 at June 30, 2023 and $236 at December 31, 2022)		30,804		30,764
Operating leases liabilities		2,892		3,204
Allowance for credit losses on off-balance sheet credit exposures		2,089		0
Other liabilities		16,535		17,410
Total liabilities		2,029,848		2,017,752
Shareholders' equity				
Preferred stock, par value $2.50 per share; 1,000,000 shares authorized; shares issued and outstanding: 0 at June 30, 2023 and 0 at December 31, 2022		0		0
Common stock, par value $2.50 per share; 30,000,000 shares authorized; shares issued: 9,883,660 at June 30, 2023 and December 31, 2022; and shares outstanding: 9,611,110 at June 30, 2023 and 9,581,230 at December 31, 2022		24,709		24,709
Additional paid-in capital		142,272		141,896
Retained earnings		60,532		52,146
Accumulated other comprehensive loss		(35,650)		(34,764)
Treasury stock shares outstanding, at cost: 272,550 shares at June 30, 2023 and 302,430 at December 31, 2022		(5,994)		(6,687)
Total shareholders' equity		185,869		177,300
Total liabilities and shareholders' equity	$	2,215,717	$	2,195,052

(1) Results of reporting periods beginning after January 1, 2023 are presented under ASC 326 while prior period amounts continue to be reported in accordance with previously applicable GAAP.

See accompanying notes.

Codorus Valley Bancorp, Inc.
Consolidated Statements of Income
(Unaudited)

(dollars in thousands, except per share data)	Three months ended June 30, 2023	Three months ended June 30, 2022	Six months ended June 30, 2023	Six months ended June 30, 2022
Interest income				
Loans, including fees	$ 24,803	$ 16,788	$ 47,837	$ 32,469
Investment securities:				
Taxable	2,492	1,732	4,949	3,012
Tax-exempt	99	105	200	204
Dividends	51	10	68	19
Other	545	648	1,229	876
Total interest income	27,990	19,283	54,283	36,580
Interest expense				
Deposits	7,077	1,010	12,214	2,072
Federal funds purchased and other short-term borrowings	437	12	475	22
Long-term debt	30	83	58	188
Subordinated debentures	547	439	1,082	858
Total interest expense	8,091	1,544	13,829	3,140
Net interest income	19,899	17,739	40,454	33,440
(Recovery of) provision for credit losses - loans (1)	(31)	2,974	461	4,001
(Recovery of) provision for credit losses - off-balance sheet credit exposures (1)	(46)	0	200	0
Net interest income after (recovery of) provision for credit losses	19,976	14,765	39,793	29,439
Noninterest income				
Trust and investment services fees	1,275	1,137	2,477	2,299
Income from mutual fund, annuity and insurance sales	323	345	692	675
Service charges on deposit accounts	1,541	1,368	3,026	2,650
Income from bank owned life insurance	329	308	651	619
Other income	587	532	1,449	951
(Loss) gain on sales of loans held for sale	(4)	221	6	579
Gain on sales of assets held for sale	0	0	118	0
Loss on sales of securities	0	0	(388)	0
Total noninterest income	4,051	3,911	8,031	7,773
Noninterest expense				
Personnel	9,489	8,491	18,531	16,881
Occupancy of premises, net	880	922	1,858	1,901
Furniture and equipment	878	812	1,716	1,699
Professional and legal	379	1,055	846	1,914
Marketing	387	433	663	833
FDIC insurance	244	188	494	427
Debit card processing	432	385	910	767
Charitable donations	899	885	931	915
External data processing	1,043	1,018	2,053	1,839
(Recovery of) impaired loan carrying costs	(238)	157	(336)	295
Other	1,083	1,877	2,621	3,428
Total noninterest expense	15,476	16,223	30,287	30,899
Income before income taxes	8,551	2,453	17,537	6,313
Provision for income taxes	1,940	500	3,934	1,307
Net income	$ 6,611	$ 1,953	$ 13,603	$ 5,006
Net income per share, basic	$ 0.69	$ 0.20	$ 1.42	$ 0.53
Net income per share, diluted	$ 0.69	$ 0.20	$ 1.42	$ 0.52

(1) Results of reporting periods beginning after January 1, 2023 are presented under ASC 326 while prior amounts continue to be reported in accordance with previously applicable GAAP.

See accompanying notes.

Codorus Valley Bancorp, Inc.
Consolidated Statements of Comprehensive Income (Loss)
(Unaudited)

	Three months ended June 30,	
(dollars in thousands)	**2023**	**2022**
Net income	$ 6,611	$ 1,953
Other comprehensive income (loss):		
Securities available for sale:		
Net unrealized holding losses arising during the period (net of tax benefit of $1,252 and $3,497, respectively)	(4,709)	(9,505)
Net unrealized loss	(4,709)	(9,505)
Comprehensive income (loss)	$ 1,902	$ (7,552)

	Six months ended June 30,	
(dollars in thousands)	**2023**	**2022**
Net income	$ 13,603	$ 5,006
Other comprehensive income (loss):		
Securities available for sale:		
Net unrealized holding losses arising during the period (net of tax benefit of $363 and $7,163, respectively)	(1,183)	(23,298)
Reclassification adjustment for losses included in net income (net of tax benefit of $91 and $0, respectively) (a) (b)	297	0
Net unrealized losses	(886)	(23,298)
Comprehensive income (loss)	$ 12,717	$ (18,292)

(a) Amounts are included in net gain (loss) on sales of securities on the Consolidated Statements of Income within noninterest income.
(b) Income tax amounts are included in the provision (benefit) for income taxes on the Consolidated Statements of Income.

See accompanying notes.

Codorus Valley Bancorp, Inc.
Consolidated Statements of Cash Flows
(Unaudited)

(dollars in thousands)	Six months ended June 30, 2023	2022
Cash flows from operating activities		
Net income	$ 13,603	$ 5,006
Adjustments to reconcile net income to net cash provided by operations:		
Depreciation/software amortization	1,176	1,260
Net amortization expense	(308)	(757)
Net change in operating lease liabilities	(312)	(305)
Provision for credit losses on off-balance sheet credit exposures	200	0
Provision for credit losses on loans	461	4,001
Provision for losses on foreclosed real estate	36	0
Deferred income tax expense	(667)	0
Increase in bank owned life insurance	(651)	(619)
Originations of loans held for sale	(2,110)	(15,121)
Proceeds from sales of loans held for sale	1,842	22,415
Gain on sales of loans held for sale	(6)	(579)
(Gain) loss on disposal of premises and equipment	(118)	9
Loss on sales of securities, available-for-sale	388	0
Stock-based compensation	730	497
Decrease (increase) in interest receivable	244	(369)
(Increase) decrease in other assets	(1,934)	617
Increase (decrease) in interest payable	490	(45)
Decrease in other liabilities	(1,566)	(663)
Net cash provided by operating activities	11,498	15,347
Cash flows from investing activities		
Purchases of securities, available-for-sale	(19,211)	(126,719)
Maturities, repayments and calls of securities, available-for-sale	15,975	21,074
Sales of securities, available-for-sale	4,253	0
Purchase of restricted investment in bank stock	(5,362)	0
Redemption of restricted investment in bank stock	2,400	356
Net increase in loans made to customers	(49,808)	(67,870)
Proceeds from sale of commercial loans held for sale	1,336	10,298
Purchases of premises and equipment	(1,014)	(867)
Proceeds from sale of fixed assets	685	0
Net cash used in investing activities	(50,746)	(163,728)
Cash flows from financing activities		
Net decrease in demand and savings deposits	(105,155)	(53,835)
Net increase (decrease) in time deposits	44,609	(50,355)
Net increase in short-term borrowings	71,715	3,488
Repayment of long-term debt	0	(10,000)
Net change in finance lease liabilities	(15)	(14)
Cash dividends paid to shareholders	(3,068)	(2,849)
Payment of taxes related to stock withheld	(139)	(70)
Treasury stock reissued	857	525
Treasury stock repurchased	0	(34)
Proceeds from issuance of stock, net	(379)	0
Net cash provided by (used in) financing activities	8,425	(113,144)
Net decrease in cash and cash equivalents	(30,823)	(261,525)
Cash and cash equivalents at beginning of year	120,439	545,494
Cash and cash equivalents at end of period	$ 89,616	$ 283,969

See accompanying notes.

Codorus Valley Bancorp, Inc.
Consolidated Statements of Changes in Shareholders' Equity
(Unaudited)

(dollars in thousands, except per share data)	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Treasury Stock	Total
Balance, January 1, 2023	$ 24,709	$ 141,896	$ 52,146	$ (34,764)	$ (6,687)	$ 177,300
Cumulative change in adoption of accounting principle ASC 326 as discussed in Note 1			(2,149)			(2,149)
Balance, January 1, 2023 (as adjusted for change in accounting principle)	$ 24,709	$ 141,896	$ 49,997	$ (34,764)	$ (6,687)	$ 175,151
Net income			6,992			6,992
Other comprehensive income, net of tax				3,823		3,823
Cash dividends ($0.16 per share)			(1,533)			(1,533)
Stock-based compensation		454				454
Forfeiture of restricted stock and withheld shares - 8,039 shares		25			(164)	(139)
Issuance and reissuance of stock:						
6,079 shares under the dividend reinvestment and stock purchase plan		15			137	152
3,131 shares under the employee stock option plan		(25)			71	46
11,816 shares of stock-based compensation awards		(267)			267	0
Balance, March 31, 2023	$ 24,709	$ 142,098	$ 55,456	$ (30,941)	$ (6,376)	$ 184,946
Balance, April 1, 2023	$ 24,709	$ 142,098	$ 55,456	$ (30,941)	$ (6,376)	$ 184,946
Net income			6,611			6,611
Other comprehensive loss, net of tax				(4,709)		(4,709)
Cash dividends ($0.16 per share)			(1,535)			(1,535)
Stock-based compensation		276				276
Issuance and reissuance of stock:						
9,021 shares under the dividend reinvestment and stock purchase plan		(55)			204	149
7,872 shares under employee stock purchase plan		(47)			178	131
Balance, June 30, 2023	$ 24,709	$ 142,272	$ 60,532	$ (35,650)	$ (5,994)	$ 185,869
Balance, January 1, 2022	$ 24,708	$ 142,067	$ 37,769	$ (164)	$ (8,875)	$ 195,505
Net income			3,053			3,053
Other comprehensive loss, net of tax				(13,793)		(13,793)
Cash dividends ($0.15 per share)			(1,421)			(1,421)
Stock-based compensation		289				289
Repurchased stock - 1,535 shares					(34)	(34)
Withheld stock - 3,177 shares					(70)	(70)
Issuance and reissuance of stock:						
6,734 shares under the dividend reinvestment and stock purchase plan		20			126	146
3,137 shares under the employee stock option plan		(15)			59	44
50,559 shares of stock-based compensation awards		(952)			952	0
Balance, March 31, 2022	$ 24,708	$ 141,409	$ 39,401	$ (13,957)	$ (7,842)	$ 183,719
Balance, April 1, 2022	$ 24,708	$ 141,409	$ 39,401	$ (13,957)	$ (7,842)	$ 183,719
Net income			1,953			1,953
Other comprehensive income, net of tax				(9,505)		(9,505)
Cash dividends ($0.15 per share)			(1,428)			(1,428)
Stock-based compensation		208				208
Forfeiture of restricted stock and withheld shares		91			(91)	0
Issuance and reissuance of stock:						
6,348 shares under the dividend reinvestment and stock purchase plan		22			120	142
5,769 shares under the stock option plan		(48)			109	61
7,223 shares under employee stock purchase plan		(4)			136	132
Balance, June 30, 2022	$ 24,708	$ 141,678	$ 39,926	$ (23,462)	$ (7,568)	$ 175,282

See accompanying notes.

Note 1—Summary of Significant Accounting Policies

Nature of Operations and Basis of Presentation
The accompanying consolidated balance sheet at December 31, 2022 has been derived from audited financial statements, and the unaudited interim consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information, the instructions to Form 10-Q, and Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 270. Accordingly, the interim financial statements do not include all of the financial information and notes required by generally accepted accounting principles for complete financial statements. In the opinion of management, the interim consolidated financial statements include all adjustments necessary to present fairly the financial condition and results of operations for the reported periods, and all such adjustments are of a normal and recurring nature.

Codorus Valley Bancorp, Inc. (“Corporation” or “Codorus Valley”) is a bank holding company headquartered in York, Pennsylvania that provides a full range of banking services through its subsidiary, PeoplesBank, A Codorus Valley Company (“PeoplesBank” or “Bank”). As of June 30, 2023, PeoplesBank operates one wholly-owned subsidiary, Codorus Valley Financial Advisors, Inc. d/b/a PeoplesWealth Advisors, which sells nondeposit investment products. In addition, PeoplesBank may periodically create nonbank subsidiaries for the purpose of temporarily holding foreclosed properties pending the liquidation of these properties. PeoplesBank operates under a state charter and is subject to regulation by the Pennsylvania Department of Banking and Securities, and the Federal Deposit Insurance Corporation. The Corporation is subject to regulation by the Board of Governors of the Federal Reserve System and the Pennsylvania Department of Banking and Securities.

The consolidated financial statements include the accounts of Codorus Valley and its wholly-owned bank subsidiary, PeoplesBank, and a wholly-owned nonbank subsidiary, SYC Realty Company, Inc. SYC Realty was inactive during the period ended June 30, 2023. The accounts of CVB Statutory Trust No. I and No. II are not included in the consolidated financial statements as discussed in Note 6—Short-Term Borrowings and Long-Term Debt. All significant intercompany account balances and transactions have been eliminated in consolidation. The accounting and reporting policies of Codorus Valley and subsidiaries conform to accounting principles generally accepted in the United States of America and have been followed on a consistent basis.

These consolidated statements should be read in conjunction with the notes to the audited consolidated financial statements contained in the Corporation’s Annual Report on Form 10-K for the year ended December 31, 2022.

The results of operations for the three and six months ended June 30, 2023 are not necessarily indicative of the results to be expected for the full year.

In accordance with FASB ASC 855, the Corporation evaluated the events and transactions that occurred after the balance sheet date of June 30, 2023 and through the date these consolidated financial statements were issued, for items of potential recognition or disclosure.

Allowance for Credit Losses—Available-for-Sale Securities
For available-for-sale debt securities in an unrealized loss position, the Corporation first assesses whether it intends to sell, or it is more likely than not that it will be required to sell the security before recovery of its amortized cost basis. If either of the criteria regarding intent or requirement to sell is met, the security’s amortized cost basis is written down to fair value through income. For debt securities available-for-sale that do not meet the aforementioned criteria, the Corporation evaluates whether the decline in fair value has resulted from credit losses or other factors. In making this assessment, management considers the extent to which fair value is less than amortized cost, any changes to the rating of the security by a rating agency and adverse conditions specifically related to the security, among other factors. If this assessment indicates that a credit loss exists, the present value of cash flows expected to be collected from the security are compared to the amortized cost basis of the security. If the present value of cash flows expected to be collected is less than the amortized cost basis, a credit loss exists and an allowance for credit losses is recorded, limited by the amount that the fair value is less than the amortized cost basis. Any impairment that has not been recorded through an allowance for credit loss is recognized in other comprehensive income.

Changes in the allowance for credit losses are recorded as provision for credit loss expense (or reversal). Losses are charged against the allowance when management believes the uncollectibility of an available-for-sale security is confirmed or when either of the criteria regarding intent or requirement to sell is met. Accrued interest receivable on available-for-sale debt securities, which totaled $1.4 million as of June 30, 2023, is excluded from the estimate of credit losses.

Loans
Loans that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are reported at amortized cost, net of the allowance for credit losses. Amortized cost is the principal balance outstanding, net of deferred loan fees and costs. Accrued interest receivable totaled $5.0 million at June 30, 2023 and was reported in other assets on the consolidated balance sheets and is excluded from the estimate of credit losses. Interest income is accrued on the unpaid principal balance. Loan origination fees, net of certain direct origination costs, are deferred and recognized in interest income using the level-yield method without anticipating prepayments. The loans receivable portfolio is disaggregated into segments. The segments include commercial,

commercial real estate – construction, commercial real estate – owner occupied, commercial real estate – non-owner occupied, residential real estate – construction, residential real estate – revolving, residential real estate – multi family, residential real estate - other, and consumer loans.

Interest income on mortgage and commercial loans is discontinued and placed on nonaccrual status at the time the loan is 90 days delinquent unless the loan is well secured and in process of collection. Mortgage loans are charged off at 180 days past due, and commercial loans are charged off to the extent principal or interest is deemed uncollectible. Consumer loans continue to accrue interest until they are charged off no later than 120 days past due unless the loan is in the process of collection. Past due status is based on the contractual terms of the loan. In all cases, loans are placed on nonaccrual or charged off at an earlier date if collection of principal or interest is considered doubtful.

All interest accrued but not received for loans placed on nonaccrual is reversed against interest income. Interest received on such loans is accounted for on the cash-basis or cost-recovery method, until qualifying for return to accrual. Under the cost-recovery method, interest income is not recognized until the loan balance is reduced to zero. Under the cash-basis method, interest income is recorded when the payment is received in cash. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

As disclosed in Note 4—Loans and Allowance for Credit Losses, the Corporation engages in commercial and consumer lending. Loans are made within the Corporation's primary market area and surrounding areas, and include the purchase of whole loan or participation interests in loans from other financial institutions. Commercial loans, which pose the greatest risk of loss to the Corporation, whether originated or purchased, are generally secured by real estate.

Allowance for credit losses – loans
The allowance for credit losses ("ACL") is a valuation account that is deducted from the loans' amortized cost basis to present the net amount expected to be collected on the loans. Loans are charged off against the allowance when management believes the uncollectibility of a loan balance is confirmed. Expected recoveries do not exceed the aggregate of amounts previously charged-off and expected to be charged-off.

Management estimates the allowance balance using relevant available information from both internal and external sources, relating to past events, current conditions and reasonable and supportable forecasts. Historical credit loss experience provides the basis for the estimation of expected credit losses. Adjustments to historical loss information are made for differences in current loan-specific risk characteristics such as differences in underwriting standards, portfolio mix, delinquency level, or term as well as changes in environmental conditions, such as changes in unemployment rates, property values, or other relevant factors. These adjustments are commonly known as the Qualitative Framework.

In addition to the estimated quantitative credit loss for loans evaluated collectively, qualitative factors that may not be fully captured in the quantitative results are also evaluated. These include changes in lending policy, the nature and volume of the portfolio, overall business conditions in the economy, credit concentrations, competition, model imprecision, and legal and regulatory requirements. Qualitative adjustments are judgmental and are based on management's knowledge of the portfolio and the markets in which the Corporation operates. Qualitative adjustments are evaluated and approved on a quarterly basis. Additionally, the ACL includes other allowance categories that are not directly incorporated in the quantitative results including loans in process.

The allowance for credit losses is measured on a collective (pool) basis when similar risk characteristics exist. Loans evaluated collectively for expected credit losses include loans on accrual status and loans initially evaluated individually but determined to not to have enhanced credit risk characteristics. The Corporation has identified the following portfolio segments:

- Commercial loans
- Commercial real estate – construction
- Commercial real estate – owner occupied
- Commercial real estate – non-owner occupied
- Residential real estate – construction
- Residential real estate – revolving
- Residential real estate – multi family
- Residential real estate – other
- Consumer loans

The Corporation measures the allowance for credit losses using the following methods.

- Loans are aggregated into pools based on similar risk characteristics.
- The Probability of Default (PD) and Loss Given Default (LGD) CECL model components are determined based on loss estimates driven by historical experience at the input level.
- The PD model component uses "through the economic cycle transition" matrices based on the Corporation's and peer group historical loan and transaction data across each pool of loans.

- The LGD model component calculates a lifetime estimate across each pool of loans utilizing a nonparametric loss curve modeling approach.
- Reasonable and supportable forecasts are incorporated into the PD model component that are based on different economic forecasts and scenarios sourced from external parties. A future loss forecast over the reasonable and supportable forecast period of one year is based on the projected performance of specific economic variables that statistically correlate with the PD and LGD pools. After the reasonable and supportable forecast period, credit loss estimates revert over four quarters to input-level.
- Cash flow assumptions are established for each loan using maturity date, amortization schedule and interest rate.
- A constant prepayment rate is calculated for each loan pool in the CECL model.

Loans that do not share similar risk characteristics are evaluated on an individual basis. Loans evaluated individually are not also included in the collective evaluation. When management determines that foreclosure is probable or when the borrower is experiencing financial difficulty at the reporting date and repayment is expected to be provided substantially through the operation or sale of the collateral expected credit losses are based on the fair value of the collateral at the reporting date, adjusted for selling costs as appropriate.

Loans are modified if the Corporation grants borrowers experiencing financial difficulties concessions that it would not otherwise consider. Concessions granted under a modification may involve a reduction of the interest rate, forgiveness of principal, extension of the term of the loan, and/or other-than-insignificant payment delays.

Allowance for credit losses – off-balance sheet credit exposures

Effective January 1, 2023, the Corporation adopted ASC 326, at which time the Corporation estimated expected credit losses over the contractual period in which the Corporation is exposed to credit risk via a contractual obligation to extend credit, unless that obligation is unconditionally cancellable by the Corporation. The allowance represents management's estimate of expected losses in unfunded loan commitments and other noncancellable off-balance sheet credit exposures, such as letters of credit. The ACL specific to unfunded commitments is determined by estimating future draws and applying the expected loss rates on those draws. Future draws are based on historical averages of utilization rates, i.e., the likelihood of draws taken. Adjustments to the reserve for unfunded off-balance sheet credit exposures are recorded in provision for credit losses - unfunded off-balance sheet credit exposures in the Consolidated Statements of Income.

Loan-Level Interest Rate Swaps

PeoplesBank enters into loan-level interest rate swaps ("swaps") to facilitate certain client transactions and to meet their financing needs. These swaps qualify as derivatives, but are not designated as hedging instruments, which would be accounted for using hedge accounting. A loan-level interest rate swap is a contract in which the series of interest rate flows (fixed and variable) are exchanged over the term of a loan with certain qualifying commercial loan clients, and PeoplesBank simultaneously enters into an interest rate swap with a dealer counterparty with identical notional amounts and terms. The net result of these swaps is that the client pays a fixed interest rate and PeoplesBank receives a floating interest rate. The swap positions with clients are equally offset with the dealer counterparties to minimize the potential impact on PeoplesBank's financial statements.

Pursuant to agreements with the dealer counterparties, PeoplesBank may receive collateral or may be required to post collateral based upon mark-to-market positions. Beyond unsecured threshold levels, collateral in the form of cash or securities may be made available to counterparties of interest rate swap transactions. Based upon the current positions and related future collateral requirements relating to them, PeoplesBank believes any effect on its cash flow or liquidity position to be immaterial.

Derivatives contain an element of credit risk, including the possibility that PeoplesBank will incur a loss because a party to the agreements, which may be a dealer counterparty or a client, fails to meet its contractual obligations. Derivative contracts may only be executed with dealer counterparties as approved by the Board of Directors. Similarly, derivatives with clients may only be executed with clients within credit exposure limits approved by the Board of Directors.

Interest rate swaps, recorded at fair value, are included in other assets on the Consolidated Balance Sheets. Additional information is provided in Note 14 – Interest Rate Swaps.

Bank Premises and Equipment Held for Sale

Bank premises and equipment designated as held for sale are carried at the lower of cost or fair value, and, at June 30, 2023 consisted of a banking property totaling $1,269,000 and is included in other assets on the Consolidated Balance Sheets. The balance of $567,000 at December 31, 2022 consisted of one retail banking property, which closed in the second quarter of 2022. Bank premises and equipment designated as held for sale is included in other assets on the Consolidated Balance Sheets.

Foreclosed Real Estate

Foreclosed real estate, included in other assets, is comprised of property acquired through a foreclosure proceeding or property that is acquired through in-substance foreclosure. Foreclosed real estate is initially recorded at fair value minus estimated costs to sell at the date of foreclosure, establishing a new cost basis. Any difference between the carrying value and the new cost basis is charged against the allowance for loan losses. Appraisals, obtained from an independent third party, are generally used to determine fair value. After foreclosure, management reviews valuations at least quarterly and adjusts the asset to the lower of cost or fair value minus estimated costs to sell through a valuation allowance or a write-down. Costs related to the improvement of foreclosed real estate are generally capitalized until the real estate reaches a saleable condition subject to fair value limitations. Revenue and expense from operations and changes in the valuation allowance are included in noninterest expense. When a foreclosed real estate asset is ultimately sold, any gain or loss on the sale is included in the income statement as a component of noninterest expense. At June 30, 2023 there was $442,000 of foreclosed commercial real estate compared to $479,000 at December 31, 2022. As of June 30, 2023, there was $241,000 consumer mortgage loans secured by residential real estate properties, for which formal foreclosure proceedings were in process according to local requirements of the applicable jurisdiction, compared to $124,000 as of December 31, 2022.

Mortgage Servicing Rights
Mortgage servicing rights (MSRs) associated with sold loans are included in other assets on the consolidated balance sheets at an amount equal to the estimated fair value of the contractual rights to service the mortgage loans. The MSR asset is amortized as a reduction to servicing income. The MSR asset is evaluated periodically for impairment and carried at the lower of amortized cost or fair value. An independent third party firm calculates fair value by discounting the estimated cash flows from servicing income using a rate consistent with the risk associated with these assets and an estimate of future net servicing income of the underlying loans. In the event that the amortized cost of the MSR asset exceeds the fair value of the asset, a valuation allowance would be established through a charge against servicing income. Subsequent fair value evaluations may determine that impairment has been reduced or eliminated, in which case the valuation allowance would be reduced through a credit to earnings. At June 30, 2023, the balance of residential mortgage loans serviced for third parties was $52,982,000 compared to $55,708,000 at December 31, 2022.

	Three months ended June 30,		Six months ended June 30,	
(dollars in thousands)	**2023**	**2022**	**2023**	**2022**
Amortized cost:				
Balance at beginning of period	$ 258	$ 345	$ 279	$ 380
Originations of mortgage servicing rights	0	1	0	6
Amortization expense	(10)	(31)	(31)	(71)
Balance at end of period	$ 248	$ 315	$ 248	$ 315

Goodwill and Core Deposit Intangible Assets
Goodwill arising from acquisitions is not amortized, but is subject to an annual impairment test. This test consists of a qualitative analysis. If the Corporation determines events or circumstances indicate that it is more likely than not that goodwill is impaired, a quantitative analysis must be completed. Analyses may also be performed between annual tests. Significant judgment is applied when goodwill is assessed for impairment. This judgment includes developing cash flow projections, selecting appropriate discount rates, identifying relevant market comparables, incorporating general economic and market conditions, and selecting an appropriate control premium. The Corporation completes its annual goodwill impairment test on October 1st of each year. Based upon a qualitative analysis of goodwill, the Corporation concluded that the amount of recorded goodwill was not impaired as of October 1, 2022. There were no conditions or events that would trigger an analysis or impairment since October 1, 2022.

Core deposit intangibles represent the value assigned to demand, interest checking, money market, and savings accounts acquired as part of an acquisition. The core deposit intangible value represents the future economic benefit of potential cost savings from acquiring core deposits as part of an acquisition compared to the cost of alternative funding sources and the alternative cost to grow a similar core deposit base. The core deposit intangible asset resulting from the merger with Madison Bancorp, Inc. was determined to have a definite life and is being amortized using the sum of the years' digits method over ten years. All intangible assets must be evaluated for impairment if certain events or changes in circumstances occur. Any impairment write-downs would be recognized as expense on the consolidated statements of income.

Revenue from Contracts with Customers
Revenue from contracts with customers that are required to be recognized under FASB ASC Topic 606 - Revenue from Contracts with Customers (ASC 606) is measured based on consideration specified in a contract with a customer, and excludes any sales incentives and amounts collected on behalf of third parties. The Corporation recognizes revenue when it satisfies a performance obligation by transferring control over a product or service to a customer.

The majority of the Corporation's revenue-generating transactions are not within the scope of ASC 606, including revenue generated from financial instruments, such as our loans, letters of credit, derivatives and investment securities, as well as revenue related to our mortgage servicing activities, as these activities are subject to other U.S. Generally Accepted Accounting Principles (GAAP) discussed elsewhere within our disclosures. Descriptions of our revenue-generating activities that are within the scope of ASC 606, which are presented in our consolidated statements of income as components of non-interest income are as follows:

Trust and investment service fees: The Corporation provides trust, investment management custody and irrevocable life insurance trust services to clients. Such services are rendered in accordance with the underlying contracts for which fees are earned. The Corporation's performance obligations are generally satisfied, and the related revenue recognized, over the period in which the service is provided. Payment for services rendered is primarily received in the following month.

Income from mutual fund, annuity and insurance sales: The Corporation sells mutual funds, annuity and insurance products to its clients. The Corporation's performance obligation is met upon the signing of the product agreement and, in certain cases, a time component may exist when the client has the right to rescind the agreement with or without penalty. The Corporation recognizes revenues upon delivery of the product or service unless there is a time component in which case revenues are recognized utilizing the expected value method. Payment for services rendered is primarily received in the following month.

Service charges on deposits accounts: These represent general service fees for monthly account maintenance and activity- or transaction based fees and consist of transaction-based revenue, time-based revenue (service period), item-based revenue or some other individual attribute-based revenue. Other service charges include revenue from processing wire transfers, cashier's checks and other services. Revenue is recognized when the performance obligation is completed which is generally monthly for account maintenance services or when a transaction has been completed. Payment for service charges on deposit accounts is primarily received immediately or in the following month through a direct charge to the clients' accounts.

Other noninterest income: The Corporation evaluated individual components of other noninterest income, such as credit card merchant fees, credit and gift card fees and ATM fees. Debit card income is primarily comprised of interchange fees earned whenever the Corporation's debit cards are processed through payment networks, such as Visa. Credit and gift card income is realized through a third party provider who issues cards as private label in the Corporation's name. ATM fees are primarily generated when a non-Corporation cardholder uses a Corporation ATM. The income is primarily comprised as a percentage of interchange fees earned whenever the issuer's card is processed through card payment networks, such as Visa or Pulse. Merchant services income is realized through a referral agreement with a third party service provider. Amounts paid to the Corporation under the agreement are from fees charged to merchants for processing their debit card transactions. The Corporation's performance obligation for these fees are largely satisfied, and related revenue recognized, when the services are rendered or upon completion. Payment is typically received within a one to three day lag or in the following month.

Per Share Data

The computation of net income per share is provided in the table below.

	Three months ended June 30,		Six months ended June 30,	
(in thousands, except per share data)	**2023**	**2022**	**2023**	**2022**
Net income	$ 6,611	$ 1,953	$ 13,603	$ 5,006
Weighted average shares outstanding (basic)	9,600	9,532	9,593	9,509
Effect of dilutive stock options	10	33	19	32
Weighted average shares outstanding (diluted)	9,610	9,565	9,612	9,541
Basic earnings per share	$ 0.69	$ 0.20	$ 1.42	$ 0.53
Diluted earnings per share	$ 0.69	$ 0.20	$ 1.42	$ 0.52

Comprehensive Income

Accounting principles generally accepted in the United States require that recognized revenue, expenses, gains and losses be included in net income. Although certain changes in assets and liabilities, such as unrealized gains and losses on available-for-sale securities, are reported as a separate component of the shareholders' equity section of the balance sheet, such items, along with net income, are components of comprehensive income.

Cash Flow Information

For purposes of the consolidated statements of cash flows, the Corporation considers interest bearing deposits with banks, cash and due from banks, and federal funds sold to be cash and cash equivalents.

Supplemental cash flow information is provided in the table below.

(dollars in thousands)	Six months ended June 30, 2023	2022
Cash paid during the period for:		
Income taxes	$ 6,310	$ 393
Interest	$ 13,339	$ 3,184
Noncash investing and financing activities:		
Transfer of loans to foreclosed real estate	$ 0	$ 479
Transfer of loans to held for sale	$ 2,018	$ 16,617
Initial recognition of operating lease right-of-use assets	$ 0	$ 2,061
Initial recognition of operating lease liabilities	$ 0	$ 2,061

Recent Accounting Pronouncements

Pronouncements Adopted in 2023

On January 1, 2023, the Corporation adopted ASU 2016-13 Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments, which replaces the incurred loss methodology with an expected loss methodology that is referred to as the current expected credit loss (CECL) methodology. The measurement of expected credit losses under the CECL methodology is applicable to financial assets measured at amortized cost, including loan receivables and held-to-maturity debt securities. It also applies to off-balance sheet credit exposures not accounted for as insurance (loan commitments, standby letters of credit, financial guarantees, and other similar instruments) and net investments in leases recognized by a lessor in accordance with Topic 842 on leases. In addition, ASC 326 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 management does not intend to sell or believes that it is more likely than not they will be required to sell. The Corporation adopted ASC 326 using the modified retrospective method for all financial assets measured at amortized cost and off-balance-sheet (OBS) credit exposures. Results for reporting periods beginning after January 1, 2023 are presented under ASC 326 while prior period amounts continue to be reported in accordance with previously applicable GAAP. The Corporation recorded a net decrease to retained earnings of $2.1 million as of January 1, 2023 for the cumulative effect of adopting ASC 326. The transition adjustment included a $927,000 increase to ACL for loans, a $1.9 million increase in the ACL for unfunded commitments and a $667,000 increase in deferred tax assets.

At adoption, the Corporation changed the way the loan portfolio is segmented and now segments the portfolio based on collateral. Previously the Corporation segmented the loan portfolio based on industry.

The following table illustrates the impact of ASC 326.

(dollars in thousands)	Pre-CECL Adoption	January 1, 2023 Reclassification to CECL Portfolio Segmentation	Post-CECL Adoption Portfolio Segmentation
Loans:			
Builder & developer	$ 128,327	$ (128,327)	$ 0
Commercial real estate investor	367,366	(367,366)	0
Commercial real estate-construction	0	144,782	144,782
Commercial real estate-owner occupied	0	344,941	344,941
Commercial real estate-non-owner occupied	0	445,408	445,408
Residential real estate investor	263,262	(263,262)	0
Residential real estate-construction	0	26,055	26,055
Residential real estate-revolving	0	103,509	103,509
Residential real estate-multi family	0	118,141	118,141
Residential real estate-other	0	243,092	243,092
Commercial	0	191,665	191,665
Hotel/Motel	94,471	(94,471)	0
Wholesale & retail	60,672	(60,672)	0
Manufacturing	86,593	(86,593)	0
Agriculture	91,449	(91,449)	0
Service	73,094	(73,094)	0
Commercial other	209,116	(209,116)	0
Consumer	0	15,264	15,264
Residential mortgage	135,340	(135,340)	0
Home equity	98,030	(98,030)	0
Consumer other	25,137	(25,137)	0
Total	$ 1,632,857	$ 0	$ 1,632,857

In March 2022, the FASB issued ASU 2022-02, Financial Instruments – Credit Losses (Topic 326): Troubled Debt Restructurings and Vintage Disclosures. ASU 2022-02 eliminates the accounting guidance for troubled debt restructurings (TDRs), while enhancing disclosure requirements for certain loan refinancings and restructurings by creditors when a borrower is experiencing financial difficulty. ASU 2022-02 is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2022. ASU 2022-02 did not have a material impact on the Corporation's consolidated financial statements.

Note 2 – Securities

A summary of securities available-for-sale at June 30, 2023 and December 31, 2022 is provided below. The securities available-for-sale portfolio is generally comprised of high quality debt instruments, principally obligations of the United States government or agencies thereof, investments in the obligations of states and municipalities and selected corporate securities, including subordinated debt. At June 30, 2023 and December 31, 2022, there were no holdings of securities of any one issuer, other than the US Government and its agencies, in an amount greater than 10% of shareholders' equity.

(dollars in thousands)	Amortized Cost	Allowance for Credit Losses	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
June 30, 2023					
Debt securities:					
U.S. Treasury notes	$ 19,765	$ 0	$ 0	$ (652)	$ 19,113
U.S. agency	14,004	0	0	(1,399)	12,605
U.S. agency mortgage-backed, residential	282,728	0	12	(32,934)	249,806
State and municipal	35,082	0	41	(5,565)	29,558
Corporates	37,713	0	0	(6,104)	31,609
Total debt securities	$ 389,292	$ 0	$ 53	$ (46,654)	$ 342,691

(dollars in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
December 31, 2022				
Debt securities:				
U.S. Treasury notes	$ 19,688	$ 0	$ (588)	$ 19,100
U.S. agency	12,750	0	(1,470)	11,280
U.S. agency mortgage-backed, residential	283,436	43	(33,377)	250,102
State and municipal	35,517	37	(6,155)	29,399
Corporates	39,531	0	(3,955)	35,576
Total debt securities	$ 390,922	$ 80	$ (45,545)	$ 345,457

The proceeds from sales of securities and the associated gains and losses are listed below. Realized gains and losses are computed on the basis of specific identification of the adjusted cost of each security and are shown net as a separate line item in the income statement.

	Three months ended June 30,		Six months ended June 30,	
(dollars in thousands)	2023	2022	2023	2022
Proceeds	$ 0	$ 0	$ 4,253	$ 0
Gross gains	0	0	0	0
Gross losses	0	0	(388)	0
Tax benefit	0	0	91	0

The amortized cost and estimated fair value of debt securities at June 30, 2023 by contractual maturity are shown below. Actual maturities may differ from contractual maturities if call options on select debt issues are exercised in the future. Mortgage-backed securities are included in the maturity categories based on average expected life.

	Available-for-sale	
(dollars in thousands)	Amortized Cost	Fair Value
Due in one year or less	$ 2,821	$ 2,757
Due after one year through five years	118,527	110,451
Due after five years through ten years	224,397	192,490
Due after ten years	43,547	36,993
Total debt securities	$ 389,292	$ 342,691

Investment securities having a carrying value of $185,776,000 and $204,887,000 on June 30, 2023 and December 31, 2022, respectively, were pledged to secure public and trust deposits, repurchase agreements and other short-term borrowings.

The table below shows gross unrealized losses and fair value, aggregated by investment category and length of time, for securities that have been in a continuous unrealized loss position, for which an allowance for credit losses has not been recorded, at June 30, 2023 and December 31, 2022.

	Less than 12 months			12 months or more			Total		
(dollars in thousands)	Number of Securities	Fair Value	Unrealized Losses	Number of Securities	Fair Value	Unrealized Losses	Number of Securities	Fair Value	Unrealized Losses
June 30, 2023									
Debt securities:									
U.S. Treasury notes	3	$ 14,359	$ (469)	1	$ 4,754	$ (183)	4	$ 19,113	$ (652)
U.S. agency	4	3,450	(54)	8	9,155	(1,345)	12	12,605	(1,399)
U.S. agency mortgage-backed, residential	82	69,911	(2,411)	157	177,137	(30,523)	239	247,048	(32,934)
State and municipal	5	1,635	(42)	33	25,719	(5,523)	38	27,354	(5,565)
Corporates	4	3,808	(386)	27	26,301	(5,718)	31	30,109	(6,104)
Total temporarily impaired debt securities, available-for-sale	98	$ 93,163	$ (3,362)	226	$ 243,066	$ (43,292)	324	$ 336,229	$ (46,654)
December 31, 2022									
Debt securities:									
U.S. Treasury notes	4	$ 19,100	$ (588)	0	$ 0	$ 0	4	$ 19,100	$ (588)
U.S. agency	7	$ 7,594	$ (656)	3	$ 3,685	$ (814)	10	$ 11,279	$ (1,470)
U.S. agency mortgage-backed, residential	147	140,409	(11,071)	72	102,061	(22,284)	219	242,470	(33,355)
State and municipal	6	2,334	(210)	35	25,121	(5,945)	41	27,455	(6,155)
Corporates	11	11,610	(831)	20	20,665	(3,124)	31	32,275	(3,955)
Total temporarily impaired debt securities, available-for-sale	175	$ 181,047	$ (13,356)	130	$ 151,532	$ (32,167)	305	$ 332,579	$ (45,523)

Securities available-for-sale are analyzed quarterly for impairment. The analysis considers, among other factors: 1) whether the Corporation has the intent to sell its securities prior to market recovery or maturity; 2) whether it is more likely than not that the Corporation will be required to sell its securities prior to market recovery or maturity; 3) default rates/history by security type; 4) third-party securities ratings; 5) third-party guarantees; 6) subordination; 7) payment delinquencies; 8) nature of the issuer; and 9) current financial news.

As of June 30, 2023, the Corporation's security portfolio consisted of 331 securities, 324 of which were in an unrealized loss position. Through June 30, 2023 the Corporation has collected all interest and principal on its investment securities as scheduled. The majority of the unrealized losses are related to the Corporation's mortgage-backed securities, as discussed below:

Mortgage-Backed Securities

At June 30, 2023, 100% of the mortgage-baked securities held by the Corporation were issued by U.S. government-sponsored entities and agencies. The decline in fair value is attributable to changes in interest rates and illiquidity, and not credit quality, and because the Corporation does not have the intent to sell these mortgage-backed securities and it is likely that it will not be required to sell the securities before their anticipated recovery, the Corporation does not consider these securities to have credit impairment at June 30, 2023.

Note 3—Restricted Investment in Bank Stocks

Restricted stock, which represents required investments in the common stock of correspondent banks, is carried at cost and, as of June 30, 2023 and December 31, 2022, consisted primarily of the common stock of the Federal Home Loan Bank of Pittsburgh ("FHLBP") and, to a lesser degree, Atlantic Community Bancshares, Inc. ("ACBI"), the parent company of Atlantic Community Bankers Bank ("ACBB"). Under the FHLBP's Capital Plan, member banks, including PeoplesBank, are required to maintain a minimum stock investment. The FHLBP uses a formula to determine the minimum stock investment, which is based on the volume of loans outstanding, unused borrowing capacity and other factors.

The FHLBP paid dividends during the periods ended June 30, 2023 and 2022. The FHLBP restricts the repurchase of the excess capital stock of member banks. The amount of excess capital stock that can be repurchased from any member is currently the lesser of five percent of the member's total capital stock outstanding or its excess capital stock outstanding.

Management evaluates the restricted stock for impairment in accordance with FASB ASC Topic 942. Management's determination of whether these investments are impaired is based on their assessment of the ultimate recoverability of the cost rather than by recognizing temporary declines in value. Using the FHLBP as an example, the determination of whether a decline affects the ultimate recoverability of cost is influenced by criteria such as: (1) the significance of the decline in net assets of the FHLBP as compared to the capital stock amount for the FHLBP and the length of time this situation has persisted; (2) commitments by the FHLBP to make payments required by law or regulation and the level of such payments in relation to the operating performance of the FHLBP; and (3) the impact of legislative and regulatory changes on institutions and, accordingly, on the customer base of the FHLBP. Management believes no impairment charge was necessary related to the restricted stock during the periods ended June 30, 2023 and 2022.

Note 4—Loans and Allowance for Credit Losses

On January 1, 2023, the Corporation adopted ASU 2016-13 Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments, which replaces the incurred loss methodology with an expected loss methodology that is referred to as the current expected credit loss (CECL) methodology. This change replaced the incurred loss model with a lifetime expected credit loss model.

At adoption, the Corporation changed the way the loan portfolio is segmented and now segments the portfolio based on collateral using federal call code targeting similar risk characteristics. Previously the Corporation segmented the loan portfolio based on industry. Management selected national civilian unemployment rates, housing price index and real gross domestic product (GDP) as the drivers of the quantitative portion of the collectively evaluated reserves. These third party supplied economic driver forecasts are updated within the model quarterly to calculate expected life and related loan default rates.

Loans that do not share similar risk characteristics are evaluated in an individual basis and are excluded from the quantitative calculations for the ACL. Loans that are individually evaluated under CECL will include loans in nonaccrual status and may include accruing loans that do not share similar risk characteristics within the evaluation. All individually evaluated loans in the current period were in nonaccrual status.

The ACL also includes a qualitative adjustment for risk factors that are not considered within the quantitative component or where the Company's risk factors differ from the utilized peer data. Management may consider additional or reduced reserves to be warranted based on current and expected conditions. During the current quarter factors that were considered relevant by management in determining expected credit losses beyond the qualitative assessment include changes in:

- Differences in lending policies, procedures, underwriting standards, charge off and recovery practices;
- Changes in the nature and volume of the portfolio and terms of loans;
- Changes in the experience, depth, and ability of lending management;
- Delinquency trends;
- Quality of the loan review system;
- Value of underlying collateral;
- Existance and effect of concentrations of credit and changes in the levels of such concentrations; and
- The effect of other external factors including legal, competition, local economic and their impact on credit losses.

The qualitative adjustments and projected impact are reviewed and considered by the Company's Chief Credit Officer in discussion with the appropriate finance and executive personnel. While multiple areas of risk beyond the quantitative risk have been identified within the model, no changes were considered warranted in the allocated reserve ratios within the current quarter.

Loan Portfolio Composition

The table below provides the composition of the loan portfolio at June 30, 2023. The portfolio is comprised of nine segments, commercial, commercial real estate construction, commercial real estate owner occupied, commercial real estate non-owner occupied, residential real estate construction, residential real estate revolving, residential real estate multi family, residential real estate other and consumer as presented in the table below. Certain portfolio segments are further disaggregated for the purpose of estimating credit losses. The Corporation has not engaged in sub-prime residential mortgage originations.

(dollars in thousands)		**June 30, 2023**	**% Total Loans**
Commercial loans	$	169,384	10.0
Commercial real estate:			
Construction		177,995	10.6
Owner occupied		343,850	20.4
Non-owner occupied		458,388	27.3
Residential real estate:			
Construction		27,961	1.7
Revolving		102,674	6.1
Multi family		123,823	7.4
Other		264,314	15.7
Consumer		13,299	0.8
Gross Loans		1,681,688	100.0
Less: Allowance for credit losses		20,681	
Net Loans	$	1,661,007	

The table below provides the composition of the loan portfolio at December 31, 2022. The portfolio is comprised of two segments, commercial and consumer loans. The commercial loan segment is disaggregated by industry class which allows the Corporation to monitor risk and performance.

Those industries representing the largest dollar investment and most risk are listed separately. The “Other” commercial loans category is comprised of various industries. The consumer related segment is comprised of residential mortgages, home equity and other consumer loans.

(dollars in thousands)		**December 31, 2022**	**% Total Loans**
Builder & developer	$	128,327	7.9
Commercial real estate investor		367,366	22.5
Residential real estate investor		263,262	16.1
Hotel/Motel		94,471	5.8
Wholesale & retail		60,672	3.7
Manufacturing		86,593	5.3
Agriculture		91,449	5.6
Service		73,094	4.5
Other		209,116	12.8
Total commercial related loans		1,374,350	84.2
Residential mortgages		135,340	8.3
Home equity		98,030	6.0
Other		25,137	1.5
Total consumer related loans		258,507	15.8
Total loans	$	1,632,857	100.0

Management estimates the allowance balance using relevant available information from both internal and external sources, relating to past events, current conditions and reasonable and supportable forecasts. Historical credit loss experience provides the basis for the estimation of expected credit losses. Adjustments to historical loss information are made for differences in current loan-specific risk characteristics such as differences in underwriting standards, portfolio mix, delinquency level, or term as well as changes in environmental conditions, such as changes in unemployment rates, property values, or other relevant factors. These adjustments are commonly known as the Qualitative Framework.

In addition to the estimated quantitative credit loss for loans evaluated collectively, qualitative factors that may not be fully captured in the quantitative results are also evaluated. These include changes in lending policy, the nature and volume of the portfolio, overall business conditions in the economy, credit concentrations, competition, model imprecision, and legal and regulatory requirements. Qualitative adjustments are judgmental and are based on management's knowledge of the portfolio and the markets in which the Corporation operates. Qualitative adjustments are evaluated and approved on a quarterly basis. Additionally, the ACL includes other allowance categories that are not directly incorporated in the quantitative results including loans in process.

The following tables presents the activity in the allowance for credit losses by segment as of and for the three and six months ended June 30, 2023.

(dollars in thousands)	**Balance, April 1, 2023**	**Impact of adopting ASC 326**	**Provision for credit losses**	**Loan charge-offs**	**Loan recoveries**	**Balance, June 30, 2023**
Commercial loans	$ 3,697	$ 0	$ 305	$ (994)	$ 33	$ 3,041
Commercial real estate:						
Construction	3,539	0	3	0	0	3,542
Owner occupied	3,956	0	(86)	0	7	3,877
Non-owner occupied	6,168	0	(43)	0	0	6,125
Residential real estate:						
Construction	79	0	14	0	0	93
Revolving	641	0	(298)	0	133	476
Multi family	1,424	0	483	0	0	1,907
Other	1,859	0	(416)	0	5	1,448
Consumer	181	0	7	(20)	4	172
Total	$ 21,544	$ 0	$ (31)	$ (1,014)	$ 182	$ 20,681

(dollars in thousands)	**Balance, January 1, 2023**	**Impact of adopting ASC 326**	**Provision for credit losses**	**Loan charge-offs**	**Loan recoveries**	**Balance, June 30, 2023**
Commercial loans	$ 4,783	$ (235)	$ (598)	$ (1,058)	$ 149	$ 3,041
Commercial real estate:						
Construction	1,829	1,121	592	0	0	3,542
Owner occupied	4,341	(69)	248	(683)	40	3,877
Non-owner occupied	6,387	(468)	206	0	0	6,125
Residential real estate:						
Construction	230	(144)	7	0	0	93
Revolving	417	192	(239)	(27)	133	476
Multi family	1,205	194	508	0	0	1,907
Other	1,511	169	(250)	0	18	1,448
Consumer	33	167	(13)	(24)	9	172
Total	$ 20,736	$ 927	$ 461	$ (1,792)	$ 349	$ 20,681

The following table presents the activity in and the composition of the allowance for loan losses in accordance with previously applicable GAAP by loan segment and class detail as of and for the three and six months ended June 30, 2022.

	Allowance for Loan Losses				
(dollars in thousands)	April 1, 2022 Balance	Charge-offs	Recoveries	Provision	June 30, 2022 Balance
Builder & developer	$ 2,275	$ 0	$ 0	$ 15	$ 2,290
Commercial real estate investor	5,082	0	0	684	5,766
Residential real estate investor	3,202	0	3	278	3,483
Hotel/Motel	565	(1,659)	0	2,356	1,262
Wholesale & retail	1,983	0	0	(1,465)	518
Manufacturing	999	0	0	(141)	858
Agriculture	1,205	0	0	249	1,454
Service	976	(488)	0	339	827
Other commercial	5,112	0	5	819	5,936
Total commercial related loans	21,399	(2,147)	8	3,134	22,394
Residential mortgage	363	0	0	(151)	212
Home equity	190	(4)	1	8	195
Other consumer	73	(1)	7	(4)	75
Total consumer related loans	626	(5)	8	(147)	482
Unallocated	2	0	0	(13)	(11)
Total	$ 22,027	$ (2,152)	$ 16	$ 2,974	$ 22,865

	Allowance for Loan Losses				
(dollars in thousands)	January 1, 2022 Balance	Charge-offs	Recoveries	Provision	June 30, 2022 Balance
Builder & developer	$ 2,408	$ 0	$ 0	$ (118)	$ 2,290
Commercial real estate investor	5,647	(1,227)	0	1,346	5,766
Residential real estate investor	3,493	0	9	(19)	3,483
Hotel/Motel	968	(1,659)	0	1,953	1,262
Wholesale & retail	1,989	0	0	(1,471)	518
Manufacturing	883	0	0	(25)	858
Agriculture	1,307	(535)	0	682	1,454
Service	981	(488)	0	334	827
Other commercial	4,656	(3)	24	1,259	5,936
Total commercial related loans	22,332	(3,912)	33	3,941	22,394
Residential mortgage	186	0	0	26	212
Home equity	191	(49)	2	51	195
Other consumer	74	(3)	11	(7)	75
Total consumer related loans	451	(52)	13	70	482
Unallocated	(1)	0	0	(10)	(11)
Total	$ 22,782	$ (3,964)	$ 46	$ 4,001	$ 22,865

Non-accrual Loans
The table below presents a summary of non-accrual loans at June 30, 2023. An allowance is established for those individual loans where the Corporation has doubt as to the full recovery of the outstanding principal balance. Typically, individually evaluated consumer related loans are partially or fully charged-off eliminating the need for specific allowance. Interest income on loans with no related allowance is the result of interest collected on a cash basis.

	With a	Without a	Related	Interest Income	
(dollars in thousands)	**Related Allowance**	**Related Allowance**	**Allowance**	**Three months ended**	**Six months ended**
June 30, 2023					
Commercial loans	$ 1,727	$ 4,354	$ 1,172	$ 0	$ 245
Commercial real estate:					
Construction	0	42	0	0	107
Owner occupied	0	2,124	0	11	53
Non-owner occupied	0	54	0	0	0
Residential real estate:					
Construction	0	0	0	36	36
Revolving	0	484	0	20	27
Multi family	0	0	0	0	0
Other	0	845	0	38	38
Consumer	0	0	0	0	0
Total	$ 1,727	$ 7,903	$ 1,172	$ 105	$ 506

The table below presents a summary of impaired loans at December 31, 2022 . Generally, impaired loans are all loans risk rated nonaccrual or classified troubled debt restructuring. An allowance is established for those individual loans where the Corporation has doubt as to the full recovery of the outstanding principal balance. Typically, impaired consumer related loans are partially or fully charged-off, eliminating the need for specific allowance. The recorded investment represents outstanding unpaid principal loan balances adjusted for payments collected on a non-cash basis and charged-offs.

	With No Allowance		With A Related Allowance			Total	
(dollars in thousands)	**Recorded Investment**	**Unpaid Principal**	**Recorded Investment**	**Unpaid Principal**	**Related Allowance**	**Recorded Investment**	**Unpaid Principal**
December 31, 2022							
Builder & developer	$ 1,901	$ 2,644	$ 44	$ 44	$ 44	$ 1,945	$ 2,688
Commercial real estate investor	500	500	0	0	0	500	500
Residential real estate investor	647	665	209	215	152	856	880
Hotel/Motel	0	0	0	0	0	0	0
Wholesale & retail	0	0	0	0	0	0	0
Manufacturing	2,783	2,877	182	183	33	2,965	3,060
Agriculture	164	210	748	930	655	912	1,140
Service	0	0	0	0	0	0	0
Other commercial	1,836	3,037	1,600	2,338	1,600	3,436	5,375
Total impaired commercial related loans	7,831	9,933	2,783	3,710	2,484	10,614	13,643
Residential mortgage	1,112	1,115	0	0	0	1,112	1,115
Home equity	457	512	0	0	0	457	512
Other consumer	0	0	0	0	0	0	0
Total impaired consumer related loans	1,569	1,627	0	0	0	1,569	1,627
Total impaired loans	$ 9,400	$ 11,560	$ 2,783	$ 3,710	$ 2,484	$ 12,183	$ 15,270

The tables below presents a summary of average impaired loans and related interest income that was included for the three and six months ended June 30, 2022. Interest income on loans with no related allowance is the result of interest collected on a cash basis.

	With No Related Allowance		With A Related Allowance		Total	
(dollars in thousands)	Average Recorded Investment	Total Interest Income	Average Recorded Investment	Total Interest Income	Average Recorded Investment	Total Interest Income
Three months ended June 30, 2022						
Builder & developer	$ 986	$ 0	$ 760	$ 0	$ 1,746	$ 0
Commercial real estate investor	3,153	14	0	0	3,153	14
Residential real estate investor	466	0	107	0	573	0
Hotel/Motel	6,037	0	0	0	6,037	0
Wholesale & retail	0	0	0	0	0	0
Manufacturing	4,495	16	0	0	4,495	16
Agriculture	1,409	315	374	0	1,783	315
Service	0	0	486	0	486	0
Other commercial	181	62	4,243	0	4,424	62
Total impaired commercial related loans	16,727	407	5,970	0	22,697	407
Residential mortgage	468	7	559	8	1,027	15
Home equity	467	27	0	0	467	27
Other consumer	90	0	0	0	90	0
Total impaired consumer related loans	1,025	34	559	8	1,584	42
Total impaired loans	$ 17,752	$ 441	$ 6,529	$ 8	$ 24,281	$ 449

	With No Related Allowance		With A Related Allowance		Total	
(dollars in thousands)	Average Recorded Investment	Total Interest Income	Average Recorded Investment	Total Interest Income	Average Recorded Investment	Total Interest Income
Six months ended June 30, 2022						
Builder & developer	$ 988	$ 0	$ 507	$ 0	$ 1,495	$ 0
Commercial real estate investor	3,047	14	626	0	3,673	14
Residential real estate investor	404	23	72	0	476	23
Hotel/Motel	8,090	0	0	0	8,090	0
Wholesale & retail	0	0	0	0	0	0
Manufacturing	4,705	37	0	0	4,705	37
Agriculture	1,842	501	779	0	2,621	501
Service	0	0	647	0	647	0
Other commercial	1,328	177	3,412	0	4,740	177
Total impaired commercial related loans	20,404	752	6,043	0	26,447	752
Residential mortgage	333	7	372	8	705	15
Home equity	457	27	0	0	457	27
Other consumer	91	0	0	0	91	0
Total impaired consumer related loans	881	34	372	8	1,253	42
Total impaired loans	$ 21,285	$ 786	$ 6,415	$ 8	$ 27,700	$ 794

As of June 30, 2023 and December 31, 2022, there were approximately $7,900,000 and $9,400,000, respectively, of non-accrual loans that did not have a related allowance for credit losses. The estimated fair value of the collateral securing these loans exceeded their carrying amount, or the loans were previously charged down to realizable collateral values. Accordingly, no specific allowance was considered to be necessary.

The table below shows the allowance amount required for loans individually evaluated for impairment and the amount required for loans collectively evaluated for December 31, 2022.

	Allowance for Loan Losses			Loans		
(dollars in thousands)	Individually Evaluated For Impairment	Collectively Evaluated For Impairment	Balance	Individually Evaluated For Impairment	Collectively Evaluated For Impairment	Balance
December 31, 2022						
Builder & developer	$ 44	$ 1,725	$ 1,769	$ 1,945	$ 126,382	$ 128,327
Commercial real estate investor	0	4,858	4,858	500	366,866	367,366
Residential real estate investor	152	2,661	2,813	856	262,406	263,262
Hotel/Motel	0	1,658	1,658	0	94,471	94,471
Wholesale & retail	0	488	488	0	60,672	60,672
Manufacturing	33	897	930	2,965	83,628	86,593
Agriculture	655	990	1,645	912	90,537	91,449
Service	0	1,064	1,064	0	73,094	73,094
Other commercial	1,600	3,352	4,952	3,436	205,680	209,116
Total commercial related	2,484	17,693	20,177	10,614	1,363,736	1,374,350
Residential mortgage	0	270	270	1,112	134,228	135,340
Home equity	0	207	207	457	97,573	98,030
Other consumer	0	82	82	0	25,137	25,137
Total consumer related	0	559	559	1,569	256,938	258,507
Unallocated	0	0	0	0	0	0
Total	$ 2,484	$ 18,252	$ 20,736	$ 12,183	$ 1,620,674	$ 1,632,857

Asset Quality

The Corporation's internal risk rating system follows regulatory guidance as to risk classifications and definitions. Every approved loan is assigned a risk rating. Generally, risk ratings for commercial related loans are determined by a formal evaluation of risk factors performed by the Corporation's underwriting staff. For consumer and residential mortgage loans, the bank follows the Uniform Retail Credit Classification guidance. Commercial loans up to $500,000 may be scored using a third-party credit scoring software model for risk rating purposes. The loan portfolio is monitored on a continuous basis by loan officers, loan review personnel and senior management. Adjustments of loan risk ratings within the Watch, Criticized and Classified categories are generally performed by the Watch and Special Asset Committees, which includes senior management. The Committees, which typically meet at least quarterly, make changes, as appropriate, to these risk ratings. In addition to review by the Committees, existing loans are monitored by the primary loan officer and loan portfolio risk management officer to determine if any changes, upward or downward, in risk ratings are appropriate. Primary loan officers may recommend a change to a risk rating and internal loan review officers may downgrade existing loans, except to non-accrual status. Only the President/CEO or CFO may approve a downgrade of a loan to non-accrual status. The Special Asset Committee or President/CEO may upgrade a loan that is criticized or classified.

The Corporation uses eleven risk ratings to grade commercial loans. The first six ratings are considered "pass" ratings. A pass rating is a satisfactory credit rating, which applies to a loan that is expected to perform in accordance with the loan agreement and has a low probability of loss. A loan rated "special mention" has a potential weakness which may, if not corrected, weaken the loan or inadequately protect the Corporation's position at some future date. A loan rated "substandard" is inadequately protected by the current net worth or paying capacity of the obligor, or of the collateral pledged. A "substandard" loan has a well-defined weakness or weaknesses that could jeopardize liquidation of the loan, which exposes the Corporation to potential loss if the deficiencies are not corrected. When circumstances indicate that collection of the loan is doubtful, the loan is risk-rated "nonaccrual," the accrual of interest income is discontinued, and any unpaid interest previously credited to income is reversed.

The following table summarizes designated internal risk rating categories by portfolio segment, by origination year, in the current period. It does not include the regulatory classification of "doubtful," nor does it include the regulatory classification of "loss", because the Corporation promptly charges off loan losses.

	Term Loans Amortized Cost Basis by Origination Year								
(dollars in thousands)	2023	2022	2021	2020	2019	Prior	Revolving Loans Amortized Cost Basis	Revolving Loans converted to Term Loans Amortized Cost Basis	Total
Commercial loans									
Pass	$ 11,432	$ 45,118	$ 17,630	$ 5,281	$ 11,451	$ 13,426	$ 44,720	$ 0	$ 149,058
Special Mention	0	431	2,148	0	595	147	2,480	0	5,801
Substandard	0	256	962	0	31	1,209	5,986	0	8,444
Nonaccrual	0	2,443	618	0	637	0	2,383	0	6,081
Total	11,432	48,248	21,358	5,281	12,714	14,782	55,569	0	169,384
Gross charge-offs	0	(26)	0	(15)	0	(968)	(49)	0	(1,058)
Commercial real estate:									
Construction									
Pass	$ 31,026	$ 67,244	$ 44,868	$ 14,418	$ 8,055	$ 8,572	$ 0	$ 0	$ 174,183
Special Mention	0	577	0	1,693	0	0	1,500	0	3,770
Substandard	0	0	0	0	0	0	0	0	0
Nonaccrual	0	0	0	0	0	42	0	0	42
Total	31,026	67,821	44,868	16,111	8,055	8,631	1,483	0	177,995
Gross charge-offs	0	0	0	0	0	0	0	0	0
Owner occupied									
Pass	$ 24,110	$ 61,416	$ 71,217	$ 25,071	$ 35,182	$ 97,614	$ 11,805	$ 0	$ 326,415
Special Mention	0	0	0	2,391	0	4,741	0	0	7,132
Substandard	250	0	1,286	0	0	6,369	274	0	8,179
Nonaccrual	0	0	1,855	0	0	269	0	0	2,124
Total	24,360	61,416	74,358	27,462	35,182	108,993	12,079	0	343,850
Gross charge-offs	0	0	0	0	0	(683)	0	0	(683)
Non-owner occupied									
Pass	$ 26,642	$ 120,462	$ 106,635	$ 63,632	$ 11,683	$ 121,079	$ 1,544	$ 0	$ 451,677
Special Mention	0	0	0	0	0	960	0	0	960
Substandard	0	0	0	0	0	5,697	0	0	5,697
Nonaccrual	0	0	0	54	0	0	0	0	54
Total	26,642	120,462	106,635	63,686	11,683	127,736	1,544	0	458,388
Gross charge-offs	0	0	0	0	0	0	0	0	0
Residential real estate:									
Construction									
Pass	$ 6,872	$ 11,935	$ 2,873	$ 709	$ 1,569	$ 1,216	$ 2,787	$ 0	$ 27,961
Special Mention	0	0	0	0	0	0	0	0	0
Substandard	0	0	0	0	0	0	0	0	0
Nonaccrual	0	0	0	0	0	0	0	0	0
Total	6,872	11,935	2,873	709	1,569	1,216	2,787	0	27,961
Gross charge-offs	0	0	0	0	0	0	0	0	0
Revolving									
Pass	$ 7,847	$ 17,118	$ 1,424	$ 347	$ 671	$ 2,720	$ 71,973	$ 0	$ 102,100
Special Mention	0	0	0	0	0	0	0	0	0
Substandard	0	0	0	0	0	0	90	0	90
Nonaccrual	0	0	0	0	0	0	484	0	484
Total	7,847	17,118	1,424	347	671	2,720	72,547	0	102,674
Gross charge-offs	0	0	0	0	0	(8)	(19)	0	(27)

Multi family								
Pass	$ 5,133	$ 26,899	$ 33,242	$ 19,764	$ 24,102	$ 13,779	$ 904	$ 0	$ 123,823
Special Mention	0	0	0	0	0	0	0	0	0
Substandard	0	0	0	0	0	0	0	0	0
Nonaccrual	0	0	0	0	0	0	0	0	0
Total	5,133	26,899	33,242	19,764	24,102	13,779	904	0	123,823
Gross charge-offs	0	0	0	0	0	0	0	0	0
Other									
Pass	$ 36,768	$ 63,554	$ 43,758	$ 39,264	$ 18,597	$ 59,694	$ 414	$ 0	$ 262,049
Special Mention	0	0	0	53	0	1,022	42	0	1,117
Substandard	0	0	0	131	0	172	0	0	303
Nonaccrual	0	0	296	0	0	549	0	0	845
Total	36,768	63,554	44,054	39,448	18,597	61,437	456	0	264,314
Gross charge-offs	0	0	0	0	0	0	0	0	0
Consumer									
Pass	$ 2,892	$ 4,162	$ 1,950	$ 239	$ 143	$ 329	$ 3,584	$ 0	$ 13,299
Special Mention	0	0	0	0	0	0	0	0	0
Substandard	0	0	0	0	0	0	0	0	0
Nonaccrual	0	0	0	0	0	0	0	0	0
Total	2,892	4,162	1,950	239	143	329	3,584	0	13,299
Gross charge-offs	0	0	0	(2)	0	(1)	(21)	0	(24)
Total Loans									
Pass	$ 152,722	$ 417,908	$ 323,597	$ 168,725	$ 111,453	$ 318,446	$ 137,714	$ 0	$ 1,630,565
Special Mention	0	1,008	2,148	4,137	595	6,870	4,022	0	18,780
Substandard	250	256	2,248	131	31	13,447	6,350	0	22,713
Nonaccrual	0	2,443	2,769	54	637	860	2,867	0	9,630
Total	152,972	421,615	330,762	173,047	112,716	339,623	150,953	0	1,681,688
Total Gross Charge-Offs	$ 0	$ (26)	$ 0	$ (17)	$ 0	$ (1,660)	$ (89)	$ 0	$ (1,792)

(dollars in thousands)	**Pass**	**Special Mention**	**Substandard**	**Nonaccrual**	**Total**
December 31, 2022					
Builder & developer	$ 124,572	$ 1,010	$ 972	$ 1,773	$ 128,327
Commercial real estate investor	367,144	0	0	222	367,366
Residential real estate investor	262,406	0	0	856	263,262
Hotel/Motel	89,710	0	4,761	0	94,471
Wholesale & retail	59,930	56	686	0	60,672
Manufacturing	81,552	1,444	632	2,965	86,593
Agriculture	87,896	2,260	381	912	91,449
Service	68,373	384	4,337	0	73,094
Other	192,194	4,934	8,552	3,436	209,116
Total commercial related loans	1,333,777	10,088	20,321	10,164	1,374,350
Residential mortgage	134,850	0	141	349	135,340
Home equity	97,573	0	0	457	98,030
Other	25,137	0	0	0	25,137
Total consumer related loans	257,560	0	141	806	258,507
Total loans	$ 1,591,337	$ 10,088	$ 20,462	$ 10,970	$ 1,632,857

The performance and credit quality of the loan portfolio is also monitored by using an aging schedule that shows the length of time a loan is past due. The table below presents a summary of past due loans, nonaccrual loans and current loans by class segment at June 30, 2023.

(dollars in thousands)	30-59 Days Past Due	60-89 Days Past Due	≥ 90 Days Past Due and Accruing	Nonaccrual	Total Past Due and Nonaccrual	Current	Total Loans
June 30, 2023							
Commercial loans	$ 10	$ 0	$ 0	$ 6,081	$ 6,091	$ 163,293	$ 169,384
Commercial real estate:							
Construction	309	0	1,693	42	2,044	175,951	177,995
Owner occupied	425	0	0	2,124	2,549	341,301	343,850
Non-owner occupied	0	155	0	54	209	458,179	458,388
Residential real estate:							
Construction	0	0	0	0	0	27,961	27,961
Revolving	799	0	0	484	1,283	101,391	102,674
Multi family	0	0	0	0	0	123,823	123,823
Other	0	0	0	845	845	263,469	264,314
Consumer	7	0	0	0	7	13,292	13,299
Total	$ 1,550	$ 155	$ 1,693	$ 9,630	$ 13,028	$ 1,668,660	$ 1,681,688

The performance and credit quality of the loan portfolio is also monitored by using an aging schedule that shows the length of time a loan is past due. The table below presents a summary of past due loans, nonaccrual loans and current loans by class segment at December 31, 2022.

(dollars in thousands)	30-59 Days Past Due	60-89 Days Past Due	≥ 90 Days Past Due and Accruing	Nonaccrual	Total Past Due and Nonaccrual	Current	Total Loans
December 31, 2022							
Builder & developer	$ 3,500	$ 0	$ 0	$ 1,773	$ 5,273	$ 123,054	$ 128,327
Commercial real estate investor	0	0	0	222	222	367,144	367,366
Residential real estate investor	0	0	0	856	856	262,406	263,262
Hotel/Motel	0	0	0	0	0	94,471	94,471
Wholesale & retail	0	0	0	0	0	60,672	60,672
Manufacturing	0	0	0	2,965	2,965	83,628	86,593
Agriculture	8	0	0	912	920	90,529	91,449
Service	0	0	0	0	0	73,094	73,094
Other	0	0	0	3,436	3,436	205,680	209,116
Total commercial related loans	3,508	0	0	10,164	13,672	1,360,678	1,374,350
Residential mortgage	207	0	0	349	556	134,784	135,340
Home equity	345	94	0	457	896	97,134	98,030
Other	7	42	0	0	49	25,088	25,137
Total consumer related loans	559	136	0	806	1,501	257,006	258,507
Total loans	$ 4,067	$ 136	$ 0	$ 10,970	$ 15,173	$ 1,617,684	$ 1,632,857

Collateral Dependent Loans

A loan is considered to be collateral-dependent when the debtor is experiencing financial difficulty and repayment is expected to be provided substantially through the sale or operation of the collateral. For all classes of loans deemed collateral-dependent, the Corporation elected the practical expedient to estimate expected credit losses based on the collateral's fair value less cost to sell. In most cases, the Corporation records a partial charge-off to reduce the loan's carrying value to the collateral's fair value less cost to sell. Substantially all of the collateral supporting collateral-dependent financial assets consists of various types of real estate, including residential properties, commercial properties, such as retail centers, office buildings, lodging, agriculture land, and vacant land. At June 30, 2023 collateral dependent loans totaled $9,600,000.

Modifications

Occasionally, the Corporation modifies loans to borrowers in financial distress by providing principal forgiveness, other-than-insignificant payment delay, term extension or interest rate reduction. When principal forgiveness is provided, the amount of forgiveness is charged-off against the allowance for credit losses.

In some cases, the Corporation provides multiple types of concessions on one loan. 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 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, an other-than-insignificant payment delay and/or an interest rate reduction.

The following table presents the amortized costs basis of loans at June 30, 2023 that were both experiencing financial difficulty and modified during the prior 3 months, by segment and type of modification. The percentage of the amortized costs basis of loans that were modified to borrowers in financial distress as compared to the amortized cost basis of each class of loan is also presented below:

(dollars in thousands)	**Term Extension**	**Total Loan Class**
June 30, 2023		
Commercial loans	$ 831	$ 0.49 %
Commercial real estate:		
Owner occupied	1,855	0.54
Total	$ 2,686	$ 0.16 %

The following table presents the amortized costs basis of loans at June 30, 2023 that were both experiencing financial difficulty and modified during the prior 6 months, by segment and type of modification. The percentage of the amortized costs basis of loans that were modified to borrowers in financial distress as compared to the amortized cost basis of each class of loan is also presented below:

(dollars in thousands)	**Term Extension**	**Interest Rate Reduction**	**Total Loan Class**
June 30, 2023			
Commercial loans	$ 1,707	$ 2,074	2.23 %
Commercial real estate:			
Owner occupied	1,855	0	0.54
Total	$ 3,562	$ 2,074	0.34 %

The following table presents the financial effect of the loan modifications presented above to borrowers experiencing financial difficulty for the three months ended June 30, 2023:

(dollars in thousands)	Weighted-Average Term Extension (months)
June 30, 2023	
Commercial loans	4
Commercial real estate:	
Owner occupied	4

The Corporation has not committed to lend additional amounts to the borrowers included in the previous table.

The following table presents the financial effect of the loan modifications presented above to borrowers experiencing financial difficulty for the six months ended June 30, 2023:

(dollars in thousands)	Weighted-Average Interest Rate Reduction	Weighted-Average Interest Rate Reduction Range	Weighted-Average Term Extension (months)
June 30, 2023			
Commercial loans	3.15 %	3.15-3.15%	8
Commercial real estate:			
Owner occupied	0	0	8

The Corporation has committed to lend additional amounts totaling $23,000 to the borrowers included in the previous table.

The Corporation closely monitors the performance of loans that are modified to borrowers experiencing financial difficulty to understand the effectiveness of its modification efforts. None of the loans that have been modified in the last three and six months were past due or had a payment default at June 30, 2023.

Note 5—Deposits

The composition of deposits as of June 30, 2023 and December 31, 2022 is shown below. The aggregate amount of demand deposit overdrafts that were reclassified as loans is $190,000 at June 30, 2023, compared to $122,000 at December 31, 2022.

(dollars in thousands)		**June 30, 2023**		**December 31, 2022**
Noninterest bearing demand	$	408,290	$	463,853
Interest bearing demand		271,263		289,298
Money market		628,318		646,702
Savings		148,054		161,228
Time deposits less than $100		221,779		210,331
Time deposits $100 to $250		139,443		123,002
Time deposits $250 or more		65,526		48,805
Total deposits	$	1,882,673	$	1,943,219

Note 6—Short-Term Borrowings and Long-Term Debt

Short-term borrowings consist of securities sold under agreements to repurchase, federal funds purchased and other borrowings. At June 30, 2023, the balance of securities sold under agreements to repurchase was $13,320,000 compared to $11,605,000 at December 31, 2022. At June 30, 2023, the balance of other short-term borrowing was $70,000,000 compared to $0 at December 31, 2022. Short-term borrowings at June 30, 2023 consisted of FHLB Open Repo Line of Credit advances at a variable rate. The rate at June 30, 2023 was 5.394 percent.

The following table presents a summary of long-term debt as of June 30, 2023 and December 31, 2022.

(dollars in thousands)		**June 30, 2023**		**December 31, 2022**
Codorus Valley Bancorp, Inc. obligations:				
Junior subordinated debt				
Due 2034, 7.57%, floating rate based on 3 month LIBOR plus 2.02%, callable quarterly		3,093		3,093
Due 2036, 6.80% floating rate based on 3 month LIBOR plus 1.54%, callable quarterly		7,217		7,217
Due 2030, 4.50% fixed rate, callable on or after December 2025		30,804		30,764
Total junior subordinated debt	$	41,114	$	41,074
Lease obligations included in long-term debt:				
Finance lease liabilities		1,225		1,240
Total long-term debt	$	42,339	$	42,314

In June 2006, Codorus Valley formed CVB Statutory Trust No. II, a wholly-owned special purpose entity whose sole purpose was to facilitate a pooled trust preferred debt issuance of $7,217,000. In November 2004, Codorus Valley formed CVB Statutory Trust No. I to facilitate a pooled trust preferred debt issuance of $3,093,000. The Corporation owns all of the common stock of these nonbank entities, and the debentures are the sole assets of the Trusts. The accounts of both Trusts are not consolidated for financial reporting purposes in accordance with FASB ASC 810. For regulatory capital purposes, all of the Corporation's trust preferred securities qualified as Tier 1 capital for all reported periods. Trust preferred securities are subject to capital limitations under the FDIC's risk-based capital guidelines. The Corporation used the net proceeds from these offerings to fund its operations.

In December 2020, Codorus Valley issued subordinated notes in the amount of $31,000,000. The Corporation may redeem the subordinated notes, in whole or in part, in a principal amount with integral multiples of $10,000, on or after December 9, 2025 and prior to the maturity date at 100% of the principal amount, plus accrued and unpaid interest. The subordinated notes mature on December 9, 2030. The subordinated notes are also redeemable in whole or in part from time to time, upon the occurrence of specific events defined within the Note Purchase Agreements. The subordinated notes may be included in Tier 2 capital (with certain limitations applicable) under current regulatory guidelines and interpretations. The subordinated notes have a fixed rate of interest equal to 4.50% until December 30, 2025. After that term, the variable rate of interest is equal to the then current 90-Day Average SOFR (Secured Overnight Financing Rate) plus 404 basis points.

Note 7—Leases

A lease is defined as a contract, or part of a contract, that conveys the right to control the use of identified property, plant or equipment for a period of time in exchange for consideration. Substantially all of the leases in which the Corporation is the lessee are comprised of real estate property, ATM locations, and office space. Substantially all of our leases are classified as operating leases, and therefore, were previously not recognized on the Corporation's consolidated statements of condition. With the adoption of Topic 842, operating lease agreements are required to be recognized on the consolidated statements of condition as right-of-use ("ROU") assets and corresponding lease liabilities. The Corporation also has one finance lease for one financial center.

Leases with an initial term of 12 months or less are not recorded on the consolidated statement of condition. All other leases have remaining lease terms of 1 year to 25 years, some of which include options to extend. Upon opening a new financial center, we typically install brand-specific leasehold improvements which are depreciated over the shorter of the useful life or length of the lease. To the extent that the initial lease term of the related lease is less than the useful life of the leasehold improvements and, taking into consideration the dollar amount of the improvements, we conclude that it is reasonably certain that a renewal option will be exercised, the renewal period is included in the lease term, and the related payments are reflected in the ROU asset and lease liability. Regarding the discount rate, Topic 842 requires the use of the rate implicit in the lease whenever this rate is readily determinable. As this rate is rarely determinable, the Corporation utilizes its incremental borrowing rate at lease inception, on an amortizing and collateralized basis, over a similar term.

All of our leases include fixed rental payments. We commonly enter into leases under which the lease payments increase at pre-determined dates based on the change in the consumer price index. While the majority of our leases are gross leases, we also have a number of leases in which we make separate payments to the lessor based on the lessor's property and casualty insurance cost and the property taxes assessed on the property, as well as a portion of the common area maintenance associated with the property. We have elected the practical expedient not to separate lease and nonlease components for all of our building leases.

The components of lease expense were as follows:

	Three months ended June 30,	
(dollars in thousands)	**2023**	**2022**
Operating lease cost	$ 174	$ 195
Finance lease cost:		
Amortization of right-of-use assets	$ 12	$ 12
Interest on lease liability	11	12
Total finance lease cost	$ 23	$ 24
Total lease cost	$ 197	$ 219

	Six months ended June 30,	
(dollars in thousands)	**2023**	**2022**
Operating lease cost	$ 348	$ 391
Finance lease cost:		
Amortization of right-of-use assets	$ 24	$ 24
Interest on lease liability	22	24
Total finance lease cost	$ 46	$ 48
Total lease cost	$ 394	$ 439

Supplemental cash flow information related to leases was as follows:

	Six months ended June 30, 2023	Six months ended June 30, 2022
Operating cash flows from operating leases	$ 359	$ 346
Operating cash flows from financing leases	23	24
Financing cash flows from financing leases	15	14
Right-of-use assets obtained in exchange for lease obligations:		
Operating leases	0	2,061
Finance leases	0	0

Amounts recognized as right-of-use assets related to finance leases are included in fixed assets in the accompanying statement of financial position, while related lease liabilities are included in long-term debt. Supplemental balance sheet information related to leases was as follows:

	June 30, 2023	December 31, 2022
Assets:		
Operating leases right-of-use assets	$ 2,772	$ 3,072
Finance leases assets	970	994
Total lease assets	$ 3,742	$ 4,066
Liabilities:		
Operating	$ 2,892	$ 3,204
Financing	1,225	1,240
Total lease liabilities	$ 4,117	$ 4,444
Weighted Average Remaining Lease Term (years)		
Operating leases	6.7	6.9
Finance leases	20.7	21.2
Weighted Average Discount Rate		
Operating leases	2.10%	2.14%
Finance leases	3.69%	3.69%

Future minimum payments for financing leases and operating leases as of June 30, 2023 and December 31, 2022 were as follows:

(dollars in thousands:)	**June 30, 2023**	
Year Ending December 31,	**Operating Leases**	**Finance Leases**
2023	$ 343	$ 38
2024	638	75
2025	430	79
2026	324	80
2027	314	80
Thereafter	1,037	1,428
Total lease payments	3,086	1,780
Less imputed interest	(194)	(555)
Total	$ 2,892	$ 1,225

(dollars in thousands:)	December 31, 2022	
Year Ending December 31,	**Operating Leases**	**Finance Leases**
2023	$ 701	$ 75
2024	638	75
2025	417	79
2026	324	80
2027	314	80
Thereafter	1,036	1,429
Total lease payments	3,430	1,818
Less imputed interest	(226)	(578)
Total	$ 3,204	$ 1,240

Note 8—Regulatory Matters

The Corporation is subject to restrictions on the payment of dividends to its shareholders pursuant to the Pennsylvania Business Corporation Law of 1988, as amended ("BCL"). The BCL prohibits the making of a dividend payment if such payment would render the Corporation insolvent or result in it having negative net worth. Federal and state banking regulations also place certain restrictions on dividends paid and loans or advances made by PeoplesBank to the Corporation. The amount of total dividends, which may be paid at any date, is generally limited to the retained earnings of PeoplesBank. Furthermore, dividend payments would be prohibited if the effect would be to cause PeoplesBank's capital to fall below applicable minimum capital requirements as discussed below. Loans and advances by PeoplesBank to affiliates, including the Corporation, are limited to 10 percent of PeoplesBank's capital stock and contributed capital on a secured basis.

Banks are also subject to regulatory capital requirements administered by federal banking agencies. Capital adequacy guidelines and, additionally for banks, prompt corrective action regulations, involve quantitative measures of assets, liabilities, and certain off balance sheet items calculated under regulatory accounting practices. Capital amounts and classifications are also subject to qualitative judgments by regulators. Failure of a bank to meet capital requirements can cause bank regulators to initiate certain regulatory actions. The net unrealized gain or loss on available for sale securities is not included in computing regulatory capital. Management believes as of June 30, 2023, the Bank met all capital adequacy requirements to which it is subject.

Prompt corrective action regulations provide five classifications: well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized, and critically undercapitalized, although these terms are not used to represent overall financial condition. If adequately capitalized, regulatory approval is required to accept brokered deposits. If undercapitalized, capital distributions are limited, as is asset growth and expansion, and capital restoration plans are required. At June 30, 2023 and December 31, 2022, the most recent regulatory notifications categorized PeoplesBank as well capitalized under the regulatory framework for prompt corrective action. There are no conditions or events since that notification that management believes have changed the institution's category.

The table below sets for the Corporation's and PeoplesBank's capital positive relative to its respective regulatory capital requirements at June 30, 2023 and December 31, 2022.

(dollars in thousands)	Actual (1)		Required for Capital Adequacy Purposes (2) (3)		To Be Well Capitalized Under Prompt Corrective Action Provisions (2)	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
Codorus Valley Bancorp, Inc. (consolidated)						
at June 30, 2023						
Capital ratios:						
Common equity Tier 1	$ 218,994	12.37 %	$ 123,897	7.00 %	$ n/a	n/a %
Tier 1 risk based	228,994	12.94	150,447	8.50	n/a	n/a
Total risk based	280,459	15.85	185,846	10.50	n/a	n/a
Leverage	228,994	10.38	88,207	4.00	n/a	n/a
at December 31, 2022						
Capital ratios:						
Common equity Tier 1	$ 209,540	12.04 %	$ 121,871	7.00 %	$ n/a	n/a %
Tier 1 risk based	219,540	12.61	147,986	8.50	n/a	n/a
Total risk based	271,040	15.57	182,806	10.50	n/a	n/a
Leverage	219,540	9.77	89,863	4.00	n/a	n/a
PeoplesBank, A Codorus Valley Company						
at June 30, 2023						
Capital ratios:						
Common equity Tier 1	$ 255,998	14.49 %	$ 123,666	7.00 %	$ 114,833	6.50 %
Tier 1 risk based	255,998	14.49	150,166	8.50	141,333	8.00
Total risk based	276,679	15.66	185,499	10.50	176,666	10.00
Leverage	255,998	11.63	88,076	4.00	110,095	5.00
at December 31, 2022						
Capital ratios:						
Common equity Tier 1	$ 245,896	14.15 %	$ 121,667	7.00 %	$ 112,976	6.50 %
Tier 1 risk based	245,896	14.15	147,738	8.50	139,048	8.00
Total risk based	266,632	15.34	182,500	10.50	173,810	10.00
Leverage	245,896	10.96	89,705	4.00	112,131	5.00

(1) Net unrealized gains and losses on securities available-for-sale, net of taxes, are disregarded for capital ratio computation purposes in accordance with federal regulatory banking guidelines.
(2) The Corporation is currently not subject to the regulatory capital requirements imposed by Basel III on bank holding companies because the Corporation's consolidated assets did not exceed $3.0 billion as of June 30, 2023 and therefore qualified as a small bank holding company.
(3) Ratio includes Capital Conservation Buffer of 2.50%, except Leverage Ratio, for which the Capital Conservation Buffer does not apply.

Note 9—Shareholders' Equity

Share Repurchase

The Corporation's Board of Directors approved share repurchase programs in August 2021 ($5 million) and January 2022 ($5 million). In 2022 a total of 1,535 shares were purchased at an average price of $22.00 under the program approved in August 2021. There was no activity under the program approved in January 2022, which expired by its own terms in December 2022.

The Corporation's Board of Directors approved a Share Repurchase Program ("Program") in January 2023. Under the approved Program, the Corporation is authorized to repurchase up to $5 million of the Corporation's issued and outstanding common stock. All shares of the common stock repurchased pursuant to the Program shall be held as treasury shares and be available for use and reissuance for the purpose as and when determined by the Board of Directors including, without limitation pursuant to the Corporation's Dividend Reinvestment and Stock Purchase Plan and its equity compensation plan. There was no activity under the Program during the three and six months ended June 30, 2023.

Note 10—Contingent Liabilities

The Corporation is involved in pending and threatened claims and other legal proceedings from time to time in the ordinary course of its business activities. Management evaluates the possible impact of these matters taking into consideration the most recent information available. A loss reserve is established for any matter for which it is believed that a loss is both probable and reasonably estimable. Once established, the reserve is adjusted as appropriate to reflect any subsequent developments. Actual losses with respect to any such matter may be more or less than the amount estimated. For any matter for which a loss is not probable, or the amount of the loss cannot reasonably be estimated, no loss reserve is established.

In addition, the Corporation may be involved in legal proceedings in the form of investigations or regulatory or governmental inquiries covering a range of possible issues. These could be specific to the Corporation, or part of more wide-spread inquires by regulatory authorities. These inquiries or investigations could lead to administrative, civil or criminal proceedings involving the Corporation and could result in fines, penalties, restitution, or other types of sanctions, or the need for the Corporation to undertake remedial actions, or to alter its business, financial or accounting practices.

Management believes that any liabilities, individually or in the aggregate, that may result from the final outcomes of pending or threatened legal proceedings will not have a material adverse effect on the financial condition of the Corporation or upon its results of operations.

Note 11—Guarantees

Codorus Valley does not issue any guarantees that would require liability recognition or disclosure, other than its standby letters of credit. Standby letters of credit are written conditional commitments issued by PeoplesBank to guarantee the performance of a client to a third party. Generally, all letters of credit, when issued, have expiration dates within one year. The credit risk involved in issuing letters of credit is essentially the same as those that are involved in extending loan facilities to clients. The Corporation generally holds collateral and/or personal guarantees supporting these commitments. The Corporation had $18,101,000 of standby letters of credit outstanding on June 30, 2023, compared to $23,601,000 on December 31, 2022. Management believes that the proceeds obtained through a liquidation of collateral and the enforcement of guarantees would be sufficient to cover the potential amount of future payments required under the corresponding letters of credit. The amount of the liability as of June 30, 2023 and December 31, 2022, for guarantees under standby letters of credit issued, was not material. Many of the commitments are expected to expire without being drawn upon and, therefore, generally do not present significant liquidity risk to the Corporation or PeoplesBank.

Note 12—Fair Value of Assets and Liabilities

The Corporation uses its best judgment in estimating the fair value of the Corporation's assets and liabilities; however, there are inherent weaknesses in any estimation technique. The estimated fair value amounts have been measured as of their respective period-ends and have not been re-evaluated or updated for purposes of these financial statements subsequent to those respective dates. As such, the estimated fair values subsequent to the respective reporting dates may be different than the amounts reported at each period end.

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in the principal or most advantageous market for an asset or liability in an orderly transaction (that is, not a forced liquidation or distressed sale) between market participants at the measurement date. GAAP establishes a fair value hierarchy that prioritizes the use of inputs used in valuation methodologies into the following three levels:

Level 1: Inputs to the valuation methodology are quoted prices, unadjusted, for identical assets or liabilities in active markets. A quoted price in an active market provides the most reliable evidence of fair value and shall be used to measure fair value whenever available.

Level 2: Inputs to the valuation methodology include quoted prices for similar assets or liabilities in active markets; inputs to the valuation methodology include quoted prices for identical or similar assets or liabilities in markets that are not active; or inputs to the valuation methodology that utilize model-based techniques for which all significant assumptions are observable in the market.

Level 3: Inputs to the valuation methodology are unobservable and significant to the fair value measurement; inputs to the valuation methodology that utilize model-based techniques for which significant assumptions are not observable in the market; or inputs to the valuation methodology that require significant management judgment or estimation, some of which may be internally developed.

Since management maximizes the use of observable inputs and minimizes the use of unobservable inputs when determining fair value, an asset's or liability's level within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement. Management reviews and updates the fair value hierarchy classifications on a quarterly basis.

Assets Measured at Fair Value on a Recurring Basis

Securities available-for-sale

The fair values of investment securities were measured using information from a third-party pricing service. The pricing service uses quoted market prices on nationally recognized securities exchanges (Level 1), or matrix pricing (Level 2), which is a mathematical technique, used widely in the industry to value debt securities without relying exclusively on quoted market prices for the specific securities, but rather, by relying on the securities' relationship to other benchmark quoted prices.

Interest rate swap agreements

Interest rate swap agreements are measured by alternative pricing sources with reasonable levels of price transparency in markets that are not active. Based on the complex nature of interest rate swap agreements, the markets these instruments trade in are not as efficient and are less liquid than that of the more mature Level 1 markets. These markets do, however, have comparable, observable inputs in which an alternative pricing source values these assets in order to arrive at a fair market value. These characteristics classify interest rate swap agreements as Level 2.

		Fair Value Measurements		
(dollars in thousands)	**Total**	**(Level 1) Quoted Prices in Active Markets for Identical Assets**	**(Level 2) Significant Other Observable Inputs**	**(Level 3) Significant Other Unobservable Inputs**
June 30, 2023				
Securities available-for-sale:				
U.S. Treasury notes	$ 19,113	$ 19,113	$ 0	$ 0
U.S. agency	12,605	0	12,605	0
U.S. agency mortgage-backed, residential	249,806	0	249,806	0
State and municipal	29,558	0	29,558	0
Corporates	31,609	0	31,609	0
Other assets:				
Loan-level interest rate swaps	81	0	81	0
December 31, 2022				
Securities available-for-sale:				
U.S. Treasury notes	$ 19,100	$ 19,100	$ 0	$ 0
U.S. agency	$ 11,280	$ 0	$ 11,280	$ 0
U.S. agency mortgage-backed, residential	250,102	0	250,102	0
State and municipal	29,399	0	29,399	0
Corporates	35,576	0	35,576	0
Other assets:				
Loan-level interest rate swaps	8	0	8	0

Assets Measured at Fair Value on a Nonrecurring Basis

Individually evaluated loans
Individually evaluated loans are those that are accounted for under FASB ASC Topic 310, in which the Corporation has measured impairment generally based on the fair value of the loan's collateral. Fair value is generally determined based upon independent third-party appraisals of the properties, or discounted cash flows based upon the expected proceeds. These loans are generally included as Level 3 fair values, based on the lowest level of input that is significant to the fair value measurements. At June 30, 2023, the fair value of individually evaluated loans with a valuation allowance or partial charge-off was $1,560,000, net of valuation allowances of $1,172,000 and charge-offs of $584,000. At December 31, 2022 the fair value of impaired loans with a valuation allowance or charge-off was $2,742,000, net of valuation allowances of $2,484,000 and charge-offs of $1,916,000.

Foreclosed real estate
Other real estate property acquired through foreclosure is initially recorded at fair value of the property at the transfer date less estimated selling cost. Subsequently, other real estate owned is carried at the lower of its carrying value or the fair value less estimated selling cost. Fair value is usually determined based on an independent third-party appraisal of the property or occasionally on a recent

sales offer. At June 30, 2023 the fair value of foreclosed real estate assets was $442,000, net of a write-down down of $525,000. At December 31, 2022 the fair value of foreclosed real estate assets was $479,000, net of a write-down of $488,000.

Mortgage servicing rights
Mortgage servicing rights are initially recorded at fair value upon the sale of residential mortgage loans to secondary market investors. The fair value of servicing rights is based on the present value of estimated future cash flows on pools of mortgages stratified by rate and original time to maturity. Mortgage servicing rights are subsequently evaluated for impairment by an independent third party on a quarterly basis. Significant inputs to the valuation include expected cash flow, expected net servicing income, a cash flow discount rate and the expected life of the underlying loans.

		Fair Value Measurements		
(dollars in thousands)	**Total**	**(Level 1) Quoted Prices in Active Markets for Identical Assets**	**(Level 2) Significant Other Observable Inputs**	**(Level 3) Significant Other Unobservable Inputs**
June 30, 2023				
Individually evaluated commercial loans	$ 1,493	$ 0	$ 0	$ 1,493
Individually evaluated residential real estate:				
Individually evaluated other	67	0	0	67
Impaired other real estate owned	442	0	0	442
December 31, 2022				
Impaired builder & developer loans	$ 1,194	$ 0	$ 0	$ 1,194
Impaired residential real estate investor loans	57	0	0	57
Impaired agriculture loans	228	0	0	228
Impaired manufacture loans	150	0	0	150
Impaired other loans	1,114	0	0	1,114
Impaired other real estate owned	479	0	0	479

The following table presents additional quantitative information about assets measured at fair value on a nonrecurring basis and for which the Corporation has utilized Level 3 inputs to determine fair value:

	Quantitative Information about Level 3 Fair Value Measurements				
(dollars in thousands)	Fair Value Estimate	Valuation Techniques	Unobservable Input	Range	Weighted Average
June 30, 2023					
Individually evaluated commercial loans	$ 1,072	Appraisal (1)	Appraisal adjustments (2)	7%-9%	8%
Individually evaluated residential real estate:					
Individually evaluated other	67	Appraisal (1)	Appraisal adjustments (2)	16%-16%	16%
Individually evaluated commercial loans	421	Business asset valuation (3)	Business asset valuation adjustments (4)	0%-48%	48%
Impaired other real estate owned	442	Appraisal (1)	Appraisal adjustments (2)	20%-25%	22%
December 31, 2022					
Impaired builder & developer loans	$ 1,194	Appraisal (1)	Appraisal adjustments (2)	2%-22%	5%
Impaired residential real estate investor loans	57	Appraisal (1)	Appraisal adjustments (2)	6%-10%	8%
Impaired agriculture loans	228	Appraisal (1)	Appraisal adjustments (2)	5%-13%	9%
Impaired manufacturer loans	150	Appraisal (1)	Appraisal adjustments (2)	67%-67%	67%
Impaired other loans	1,114	Appraisal (1)	Appraisal adjustments (2)	0%-25%	5%
Impaired other real estate owned	479	Appraisal (1)	Appraisal adjustments (2)	0%-25%	22%

(1) Fair value is generally determined through independent appraisals, which generally include various level 3 inputs that are not identifiable.
(2) Appraisal amounts may be adjusted downward by the Corporation's management for qualitative factors such as economic conditions and estimated liquidation expenses.
(3) Fair value is generally determined through customer-provided financial statements and bankruptcy court documents.
(4) Business asset valuation may be adjusted downward by the corporation’s management qualitative factors such as economic conditions and estimated liquidation expenses. The range of liquidation expenses adjustments are presented as a percent of the financial statement book value.

The following presents the carrying amounts and estimated fair values of the Corporation's financial instruments as of June 30, 2023 and December 31, 2022.

(dollars in thousands)	Carrying Amount	Estimated Fair Value	Fair Value Estimates (Level 1) Quoted Prices in Active Markets for Identical Assets	(Level 2) Significant Other Observable Inputs	(Level 3) Significant Other Unobservable Inputs
June 30, 2023					
Financial assets					
Cash and cash equivalents	$ 89,616	$ 89,616	$ 89,616	$ 0	$ 0
Securities available-for-sale	342,691	342,691	19,113	323,578	0
Restricted investment in bank stocks	3,917	N/A	N/A	N/A	N/A
Loans held for sale	428	466	0	466	0
Loans, net	1,661,007	1,559,773	0	0	1,559,773
Interest receivable	6,380	6,380	0	1,362	5,018
Financial liabilities					
Deposits	$ 1,882,673	$ 1,874,692	$ 0	$ 1,874,692	$ 0
Short-term borrowings	83,320	83,320	0	83,320	0
Long-term debt (1)	10,310	8,993	0	0	8,993
Subordinated debentures	30,804	28,219	0	28,219	0
Interest payable	982	982	0	982	0
Off-balance sheet instruments	0	0	0	0	0
December 31, 2022					
Financial assets					
Cash and cash equivalents	$ 120,439	$ 120,439	$ 120,439	$ 0	$ 0
Securities available-for-sale	345,457	345,457	19,100	326,357	0
Restricted investment in bank stocks	955	N/A	N/A	N/A	N/A
Loans held for sale	154	157	0	157	0
Loans, net	1,612,121	1,503,440	0	0	1,503,440
Interest receivable	6,624	6,624	0	948	5,676
Financial liabilities					
Deposits	$ 1,943,219	$ 1,932,689	$ 0	$ 1,932,689	$ 0
Short-term borrowings	11,605	11,605	0	11,605	0
Long-term debt (1)	10,310	10,165	0	0	10,165
Subordinated debentures	30,764	29,145	0	29,145	0
Interest payable	492	492	0	492	0
Off-balance sheet instruments	0	0	0	0	0

(1) Exclude leases included in Long-term debt

Note 13—Assets and Liabilities Subject to Offsetting

Securities Sold Under Agreements to Repurchase

PeoplesBank enters into agreements with clients in which it sells securities subject to an obligation to repurchase the same securities ("repurchase agreements"). The contractual maturity of the repurchase agreement is overnight and continues until either party terminates the agreement. These repurchase agreements are accounted for as a collateralized financing arrangement (i.e., secured borrowings) and not as a sale and subsequent repurchase of securities. The obligation to repurchase the securities is reflected as a liability (short-term borrowings) in the Corporation's consolidated financial statements of condition, while the securities underlying the repurchase agreements are appropriately segregated for safekeeping purposes and remain in the respective securities asset accounts. Thus, there is no offsetting or netting of the securities with the repurchase agreement liabilities.

				Gross amounts Not Offset in the Statements of Condition			
				Financial Instruments			
(dollars in thousands)	Gross Amounts of Recognized Liabilities	Gross Amounts Offset in the Statements of Condition	Net Amounts of Liabilities Presented in the Statements of Condition	U.S. agency mortgage-backed, residential	U.S. agency	Cash Collateral Pledged	Net Amount
June 30, 2023							
Repurchase Agreements	$ 13,320	$ 0	$ 13,320	$ (12,987)	$ 0	$ 0	$ 333
December 31, 2022							
Repurchase Agreements	$ 11,605	$ 0	$ 11,605	$ (13,767)	$ 0	$ 0	$ (2,162)

Note 14 – Interest Rate Swaps

Loan Level Interest Rate Swaps

PeoplesBank enters into loan-level interest rate swaps with certain qualifying, creditworthy commercial loan clients to provide a loan pricing structure that meets the interest rate risk management needs of both PeoplesBank as well as the client. PeoplesBank simultaneously enters into offsetting interest rate swaps with dealer counterparties, with identical notional amounts and terms. The net results of the offsetting client and deal counterparty swap agreements is that the client pays a fixed rate of interest and PeoplesBank receives a floating rate. PeoplesBank's loan-level interest rate swaps are considered derivatives but are not accounted for using hedge accounting.

The fair value and notional amount related to loan-level interest rate swaps are presented below:

	June 30, 2023		December 31, 2022	
(dollars in thousands)	Notional Amount	Asset (Liability) Fair Value	Notional Amount	Asset (Liability) Fair Value
Interest Rate Swap with Customers				
Positive Fair Values	$ 25,232	$ 81	$ 5,992	$ 0
Interest Rate Swaps with Counterparties				
Negative Fair Values	$ 25,232	$ (81)	$ 5,992	$ 0

The gross amounts of loan-level interest rate swaps, the amounts offset and the carrying values in the Consolidated Balance Sheets, and the collateral pledged to support such agreements are presented below.

(dollars in thousands)	June 30, 2023	December 31, 2022
Interest Rate Swap Contracts - Commercial Loans:		
Gross amounts recognized	$ 81	$ 8
Gross amounts offset	81	8
Net amounts presented in the Consolidated Balance Sheets	$ 0	$ 0
Gross amounts not offset:		
Cash Collateral	$ 0	$ 0
Net amounts	$ 0	$ 0

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

Management's discussion and analysis of the significant changes in the results of operations, capital resources and liquidity presented in the accompanying consolidated financial statements for Codorus Valley Bancorp, Inc. ("Codorus Valley" or "the Corporation"), a bank holding company, and its wholly-owned subsidiary, PeoplesBank, A Codorus Valley Company ("PeoplesBank"), are provided below. Codorus Valley's consolidated financial condition and results of operations consist almost entirely of PeoplesBank's financial condition and results of operations. Current performance does not guarantee, and may not be indicative of, similar performance in the future.

Cautionary Note Regarding Forward-looking Statements

Management of the Corporation has made forward-looking statements in this Form 10-Q. Forward-looking statements may include information concerning the financial condition, results of operations and business of the Corporation and its subsidiaries and include, but are not limited to, statements regarding expectations or predictions of future financial or business performance or conditions relating to the Corporation and its operations. These forward-looking statements may include statements with respect to the Corporation's beliefs, plans, objectives, goals, expectations, anticipations, estimates and intentions, that are subject to significant risks and uncertainties, and are subject to change based on various factors (some of which are beyond the Corporation's control). Forward-looking statements may also include, but are not limited to, discussions of strategy, financial projections and estimates and their underlying assumptions, statements regarding plans, objectives, goals, expectations or consequences, and statements about future performance, expenses, operations, or products and services of the Corporation and its subsidiaries. Forward-looking statements can be identified by the use of words such as "may," "should," "will," "could," "believes," "plans," "expects," "estimates," "intends," "anticipates," "strives to," "seeks," "intends," "anticipates" or similar words or expressions.

Forward-looking statements are not historical facts, nor should they be relied upon as providing assurance of future performance. Forward-looking statements are based on current beliefs, expectations and assumptions regarding the future of the Corporation's business, future plans and strategies, projections, anticipated events and trends, the economy and other future conditions. Because forward-looking statements relate to the future, they are subject to inherent uncertainties, risks, and changes in circumstances that are difficult to predict and many of which are outside of the Corporation's control. Note that many factors, some of which are discussed elsewhere in this report and in the documents that are incorporated by reference, could affect the future financial results of the Corporation and its subsidiaries, both individually and collectively, and could cause those results to differ materially from those expressed in the forward-looking statements contained or incorporated by reference in this Form 10-Q. Actual results could differ materially from those indicated in forward-looking statements due to, among others, the following factors:

- changes in market interest rates and the persistence of the current inflationary environment in the U.S. and our market areas and the potential for an economic downturn or recession;
- the effects of financial challenges at other banking institutions that could lead to depositor concerns that spread within the banking industry causing disruptive deposit outflows and other destabilizing results;
- legislative and regulatory changes, and the uncertain impact of new laws and regulations;
- monetary and fiscal policies of the federal government;
- the effects of changes in accounting policies and practices;
- ineffectiveness of the Corporation's business strategy due to changes in current or future market conditions;
- changes in deposit flows, the cost of funds, demand for loan products and the demand for financial services;
- the effects of the COVID-19 pandemic, including on the Corporation's credit quality and operations as well as its impact on general economic conditions;
- competition; market volatility, market downturns, changes in consumer behavior, business closures;
- adverse changes in the quality or composition of the Corporation's loan, investment and mortgage-backed securities portfolios, including from the effects of the current inflationary environment;
- geographic concentration of the Corporation's business;
- deterioration of commercial real estate values;
- the adequacy of loan loss reserves and the Corporation's transition to the Current Expected Credit Loss (CECL) method of reserving for losses in its loan portfolio;
- deterioration in the credit quality of borrowers;
- the Company's ability to attract and retain key personnel;
- the impact of operational risks, including the risk of human error, failure or disruption of internal processes and systems, including of the Corporation's information and other technology systems;
- uncertainty surrounding the transition from LIBOR to an alternate reference rate;
- failure or circumvention of our internal controls;
- the Corporation's ability to keep pace with technological changes;
- breaches of security or failures of the Corporation to identify and adequately address cybersecurity and data breaches;

- changes in government regulation and supervision and the potential for negative consequences resulting from regulatory examinations, investigations and violations;
- the effects of adverse outcomes from claims and litigation;
- occurrence of natural or man-made disasters or calamities, including health emergencies, the spread of infectious diseases, epidemics or pandemics, an outbreak or escalation of hostilities or other geopolitical instabilities, the effects of climate change or extraordinary events beyond the Corporation's control, and the Corporation’s ability to deal effectively with disruptions caused by the foregoing; and
- economic, competitive, governmental and technological factors affecting the Corporation’s operations, markets, products, services and fees.

For a discussion of other risks and uncertainties that could affect the Corporation, please refer to the “Risk Factors” section of the Corporation’s Annual Report on Form 10-K for the year-ended December 31, 2022, and in its current and periodic reports that are, or will be, filed with the Securities and Exchange Commission (“SEC”) and available on the SEC’s website at *www.sec.gov* or in the Investor Relations section of the Corporation’s website at *www.peoplesbanknet.com.* The Corporation undertakes no obligation, other than as required by law, to update or revise any forward-looking statement to reflect new information, events occurring after the date of this Form 10-Q or otherwise.

Critical Accounting Policies

The Corporation’s critical accounting policies, as summarized in Note 1—Summary of Significant Accounting Policies, include those related to the allowance for credit losses which requires management to make significant judgments, estimates and assumptions that have a material impact on the carrying value of certain assets and liabilities. For this Form 10-Q, there were material changes made to the Corporation’s critical accounting policies, which were described in Item 7 of the Corporation’s previously filed Annual Report on Form 10-K for the year ended December 31, 2022 below.

On January 1, 2023, the Corporation adopted ASU 2016-13 Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments, which replaces the incurred loss methodology with an expected loss methodology that is referred to as the current expected credit loss (CECL) methodology. The measurement of expected credit losses under the CECL methodology is applicable to financial assets measured at amortized cost, including loan receivables and held-to-maturity debt securities. It also applies to off-balance sheet credit exposures not accounted for as insurance (loan commitments, standby letters of credit, financial guarantees, and other similar instruments) and net investments in leases recognized by a lessor in accordance with Topic 842 on leases. In addition, ASC 326 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 management does not intend to sell or believes that it is more likely than not they will be required to sell. The Corporation adopted ASC 326 using the modified retrospective method for all financial assets measured at amortized cost and off-balance-sheet (OBS) credit exposures. Results for reporting periods beginning after January 1, 2023 are presented under ASC 326 while prior period amounts continue to be reported in accordance with previously applicable GAAP. The Corporation recorded a net decrease to retained earnings of $2,100,000 as of January 1, 2023 for the cumulative effect of adopting ASC 326. The transition adjustment included a $927,000 increase to the allowance for credit losses for loans, a $1,900,000 increase in the allowance for credit losses for unfunded commitments and a $667,000 increase in deferred tax assets.

<u>Allowance for credit losses – loans</u>
The allowance for credit losses (“ACL”) is a valuation account that is deducted from the loans’ amortized cost basis to present the net amount expected to be collected on the loans. Loans are charged off against the allowance when management believes the uncollectibility of a loan balance is confirmed. Expected recoveries do not exceed the aggregate of amounts previously charged-off and expected to be charged-off.

Management estimates the allowance balance using relevant available information from both internal and external sources, relating to past events, current conditions and reasonable and supportable forecasts. Historical credit loss experience provides the basis for the estimation of expected credit losses. Adjustments to historical loss information are made for differences in current loan-specific risk characteristics such as differences in underwriting standards, portfolio mix, delinquency level, or term as well as changes in environmental conditions, such as changes in unemployment rates, property values, or other relevant factors. These adjustments are commonly known as the Qualitative Framework.

In addition to the estimated quantitative credit loss for loans evaluated collectively, qualitative factors that may not be fully captured in the quantitative results are also evaluated. These include changes in lending policy, the nature and volume of the portfolio, overall business conditions in the economy, credit concentrations, competition, model imprecision, and legal and regulatory requirements. Qualitative adjustments are judgmental and are based on management’s knowledge of the portfolio and the markets in which the Corporation operates. Qualitative adjustments are evaluated and approved on a quarterly basis. Additionally, the ACL includes other allowance categories that are not directly incorporated in the quantitative results including loans in process.

The allowance for credit losses is measured on a collective (pool) basis when similar risk characteristics exist. Loans evaluated collectively for expected credit losses include loans on accrual status and loans initially evaluated individually but determined to not to have enhanced credit risk characteristics. The Corporation has identified the following portfolio segments:

- Commercial loans
- Commercial real estate – construction
- Commercial real estate – owner occupied
- Commercial real estate – non-owner occupied
- Residential real estate – construction
- Residential real estate – revolving
- Residential real estate – multi family
- Residential real estate – other
- Consumer loans

The Corporation measures the allowance for credit losses using the following methods.

- Loans are aggregated into pools based on similar risk characteristics.
- The Probability of Default (PD) and Loss Given Default (LGD) CECL model components are determined based on loss estimates driven by historical experience at the input level.
- The PD model component uses "through the economic cycle transition" matrices based on the Corporation's and peer group historical loan and transaction data across each pool of loans.
- The LGD model component calculates a lifetime estimate across each pool of loans utilizing a nonparametric loss curve modeling approach.
- Reasonable and supportable forecasts are incorporated into the PD model component that are based on different economic forecasts and scenarios sourced from an external party. A future loss forecast over the reasonable and supportable forecast period is based on the projected performance of specific economic variables that statistically correlate with the PD and LGD pools. After the reasonable and supportable forecast period, loss estimates naturally revert to input-level reversion.
- Cash flow assumptions are established for each loan using maturity date, amortization schedule and interest rate.
- A constant prepayment rate is calculated for each loan pool in the CECL model.

Loans that do not share risk characteristics are evaluated on an individual basis. Loans evaluated individually are not also included in the collective evaluation. When management determines that foreclosure is probable or when the borrower is experiencing financial difficulty at the reporting date and repayment is expected to be provided substantially through the operation or sale of the collateral expected credit losses are based on the fair value of the collateral at the reporting date, adjusted for selling costs as appropriate.

Loans are modified if the Corporation grants borrowers experiencing financial difficulties concessions that it would not otherwise consider. Concessions granted under a modification may involve a reduction of the interest rate, forgiveness of principal, extension of the term of the loan, and/or other-than-insignificant payment delays.

Three Months Ended June 30, 2023 vs. Three Months Ended June 30, 2022

The schedule below presents selected performance metrics for the second quarter of both 2023 and 2022.

	Three months ended June 30, 2023	Three months ended June 30, 2022
Basic earnings per share	$ 0.69	$ 0.20
Diluted earnings per share	$ 0.69	$ 0.20
Cash dividend payout ratio	23.22 %	73.17 %
Return on average assets	1.22 %	0.34 %
Return on average equity	14.17 %	4.31 %
Net interest margin (tax equivalent basis)	3.81 %	3.18 %
Net overhead ratio	2.10 %	2.11 %
Efficiency ratio	64.19 %	74.43 %
Average equity to average assets	8.58 %	7.78 %

The Corporation's net income (earnings) was $6,611,000 for the quarter ended June 30, 2023, as compared to $1,953,000 for the quarter ended June 30, 2022, an increase of $4,658,000 or 239 percent.

INCOME STATEMENT ANALYSIS

Net Interest Income

Unless otherwise noted, this section discusses interest income and interest expense amounts as reported in the Consolidated Statements of Income, which are not presented on a tax equivalent basis.

Net interest income for the quarter ended June 30, 2023 was $19,899,000, an increase of $2,160,000 or 12 percent compared to net interest income of $17,739,000 for the second quarter 2022.

The Corporation's net interest margin, computed as interest income (tax-equivalent basis) annualized as a percentage of average interest earning assets, was 3.81 percent for the second quarter 2023 compared to 3.18 percent for the second quarter 2022. The net interest margin expansion was primarily the result of higher rates on commercial loans. Net interest margin also benefited from higher rates on interest bearing deposits with banks and investment securities. Higher rates on interest bearing demand deposits and time deposits partially offset the margin expansion.

Total interest income for the second quarter 2023 totaled $27,990,000, an increase of $8,707,000 or 45 percent above the amount of total interest income for the second quarter 2022. The change was primarily a result of higher rates on interest bearing deposits with banks and commercial loans and higher volume and rates of investment securities.

Interest and dividend income on investments increased $692,000 or 28 percent in the second quarter 2023 compared to the same period in 2022. The average balance of the investment securities portfolio increased $49,476,000 or 14 percent when comparing the second quarter 2023 to the same period in 2022. The tax-equivalent yield on investments for the second quarter 2023 was 2.72 percent or 53 basis points higher than the 2.19 percent realized in the second quarter 2022. The average balance of interest bearing deposits with banks decreased $288,329,000 or 87 percent in the second quarter 2023 compared to the second quarter 2022. The yield on the interest bearing deposits with banks increased 430 basis points when comparing the second quarter 2023 to the same period in 2022.

Interest income on loans increased $8,015,000 or 48 percent in the second quarter 2023 compared to the same period in 2022. The average balance of outstanding loans, primarily commercial loans, increased $93,373,000 or 6 percent comparing the second quarter 2023 to the same period in 2022. Higher rates on commercial loans was the primary driver of the increase in interest income on loans. The tax-equivalent yield on loans for the second quarter 2023 was 5.98 percent or 169 basis points higher than the 4.29 percent experienced in the second quarter 2022.

Total interest expense for the second quarter 2023 was $8,091,000, an increase of $6,547,000 or 424 percent as compared to total interest expense of $1,544,000 for the second quarter 2022. The change was primarily the result of the higher cost of interest bearing demand, time deposits and short-term borrowings.

Interest expense on deposits increased $6,067,000 or 601 percent in the second quarter 2023 compared to the same period in 2022. The average rate paid on interest bearing deposits was 1.94 percent in the second quarter 2023 or 168 basis points higher than the average rate paid of 0.26 percent in the second quarter 2022. The average balance of interest bearing deposits for the second quarter 2023 decreased by $107,642,000 or 7 percent compared to the second quarter 2022. Also, noninterest-bearing deposits decreased, with the average volume for the second quarter 2023 decreasing 17 percent to $418,504,000 as compared to $503,211,000 for the second quarter 2022.

For the second quarter 2023 interest expense on all borrowings increased $480,000 or 90 percent compared to the second quarter 2022. Short-term borrowings consisting of repurchase agreements and other short-term borrowings, which includes borrowings from the Federal Home Loan Bank of Pittsburgh (FHLBP) Open Repo Line of Credit averaged $44,139,000 for the second quarter 2023, compared to an average balance of $12,080,000 for the second quarter 2022. The rate on average short-term borrowings for the second quarter 2023 was 3.97 percent, an increase as compared to a rate of 0.40 percent for the second quarter 2022. Long-term debt, which includes junior subordinated trust preferred securities, finance leases and long-term FHLBP borrowings, averaged $14,520,000 for the second quarter 2023 and $21,828,000 for the second quarter 2022. The decrease was attributable to FHLBP advances totaling $10,000,000 which matured and were repaid in the second quarter of 2022. For the second quarter 2023, the rate on average long-term debt was 5.76 percent, an increase of 295 basis points as compared to a rate of 2.81 percent for the second quarter 2022. Subordinated debentures, issued in December 2020 by the Corporation, averaged $30,798,000 for the second quarter 2023 and $30,717,000 for the second quarter 2022.

Table 1-Average Balances and Interest Rates (tax equivalent basis)

	Three months ended June 30,					
	2023			2022		
(dollars in thousands)	Average Balance	Interest	Yield/ Rate	Average Balance	Interest	Yield/ Rate
Assets						
Interest bearing deposits with banks	$ 43,006	$ 545	5.08 %	$ 331,335	$ 648	0.78 %
Investment securities:						
Taxable	370,345	2,543	2.75	317,889	1,742	2.20
Tax-exempt	22,581	121	2.15	25,561	132	2.07
Total investment securities	392,926	2,664	2.72	343,450	1,874	2.19
Loans:						
Taxable (1)	1,644,775	24,630	6.01	1,557,857	16,648	4.29
Tax-exempt	22,292	214	3.85	15,837	176	4.46
Total loans	1,667,067	24,844	5.98	1,573,694	16,824	4.29
Total earning assets	2,102,999	28,053	5.35	2,248,479	19,346	3.45
Other assets (2)	72,796			82,763		
Total assets	$ 2,175,795			$ 2,331,242		
Liabilities and Shareholders' Equity						
Deposits:						
Interest bearing demand	$ 899,474	$ 4,612	2.06 %	$ 981,025	$ 431	0.18 %
Savings	151,143	12	0.03	165,245	12	0.03
Time	411,309	2,453	2.39	423,298	567	0.54
Total interest bearing deposits	1,461,926	7,077	1.94	1,569,568	1,010	0.26
Short-term borrowings	44,139	437	3.97	12,080	12	0.40
Long-term debt	14,520	208	5.75	21,828	153	2.81
Subordinated debentures	30,798	369	4.81	30,717	369	4.82
Total interest bearing liabilities	1,551,383	8,091	2.09	1,634,193	1,544	0.38
Noninterest bearing deposits	418,504			503,211		
Other liabilities	19,277			12,531		
Shareholders' equity	186,631			181,307		
Total liabilities and shareholders' equity	$ 2,175,795			$ 2,331,242		
Net interest income (tax equivalent basis)		$ 19,962			$ 17,802	
Net interest margin (3)			3.81 %			3.18 %
Tax equivalent adjustment		(63)			(63)	
Net interest income		$ 19,899			$ 17,739	

(1) Average balance includes average nonaccrual loans of $7,004,000 for 2023 and $30,986,000 for 2022. Interest includes net loan fees of $869,000 for 2023 and $1,218,000 for 2022.
(2) Average balance includes average bank owned life insurance and foreclosed real estate.
(3) Net interest income (tax equivalent basis) annualized as a percentage of average earning assets.

Table 2-Rate/Volume Analysis of Changes in Net Interest Income (tax equivalent basis)

	Three months ended June 30, 2023 vs. 2022		
	Increase (decrease) due to change in*		
(dollars in thousands)	**Volume**	**Rate**	**Net**
Interest Income			
Interest bearing deposits with banks	$ (564)	$ 461	$ (103)
Investment securities:			
Taxable	283	518	801
Tax-exempt	(15)	4	(11)
Loans:			
Taxable	761	7,221	7,982
Tax-exempt	72	(34)	38
Total interest income	537	8,170	8,707
Interest Expense			
Deposits:			
Interest bearing demand	(25)	4,206	4,181
Savings	(1)	1	0
Time	(15)	1,901	1,886
Short-term borrowings	1	424	425
Long-term debt	(53)	108	55
Subordinated debentures	1	(1)	0
Total interest expense	(92)	6,639	6,547
Net interest income (tax equivalent basis)	$ 629	$ 1,531	$ 2,160

*Changes which are due to both volume and rate are allocated in proportion to their relationship to the amount of change attributed directly to volume or rate.

Provision for Credit Losses

The provision for credit losses is an expense charged to earnings to cover the estimated losses attributable to uncollected loans. The provision reflects management's judgment of an appropriate level for the allowance for credit losses. Total provision for credit losses, including off-balance sheet exposures, for the second quarter 2023 was a recovery of $77,000. The leading components of the second quarter's net recovery was a successful collection of $1,500,000 on a fully reserved loan offset by a $1,000,000 allocation and charged offs on individual credits. The remaining net provision in the second quarter resulted from changes in the ACL related to net loan growth and credit loss factor changes. The allowance as a percentage of total loans was 1.23 percent at June 30, 2023, as compared to 1.27 percent at December 31, 2022 and 1.44 percent at June 30, 2022.

More information about the allowance for credit losses can be found in this report under the caption Allowance for Credit Losses on page 56.

Noninterest Income

The following table presents the components of total noninterest income for the second quarter 2023, compared to the second quarter 2022.

Table 3 - Noninterest income

(dollars in thousands)	Three months ended June 30, 2023	2022	Change Increase (Decrease) $	%
Trust and investment services fees	$ 1,275	$ 1,137	$ 138	12 %
Income from mutual fund, annuity and insurance sales	323	345	(22)	(6)
Service charges on deposit accounts	1,541	1,368	173	13
Income from bank owned life insurance	329	308	21	7
Other income	587	532	55	10
(Loss) gain on sales of loans held for sale	(4)	221	(225)	(102)
Total noninterest income	$ 4,051	$ 3,911	$ 140	4 %

The discussion that follows addresses changes in selected categories of noninterest income.

Service changes on deposit accounts—The $173,000 or 13 percent increase in service charges on deposit accounts is due to higher insufficient funds fees and early withdrawal penalties assessed on time deposits.

(Loss) gain on sales of loans held for sale—The $225,000 or 102 percent decrease in gain on sales of loans was due to the sale of a smaller volume of mortgage loans to the secondary market during the second quarter 2023 compared to the second quarter 2022, impacted by increasing market rates.

Noninterest Expense

The following table presents the components of total noninterest expense for the second quarter 2023, compared to the second quarter 2022.

Table 4 - Noninterest expense

(dollars in thousands)	Three months ended June 30, 2023	2022	Change Increase (Decrease) $	%
Personnel	$ 9,489	$ 8,491	$ 998	12 %
Occupancy of premises, net	880	922	(42)	(5)
Furniture and equipment	878	812	66	8
Professional and legal	379	1,055	(676)	(64)
Marketing	387	433	(46)	(11)
FDIC insurance	244	188	56	30
Debit card processing	432	385	47	12
Charitable donations	899	885	14	2
External data processing	1,043	1,018	25	2
(Recovery of) impaired loan carrying costs	(238)	157	(395)	(252)
Other	1,083	1,877	(794)	(42)
Total noninterest expense	$ 15,476	$ 16,223	$ (747)	(5)%

The discussion that follows addresses changes in selected categories of noninterest expense.

Personnel—The $998,000 or 12 percent increase in personnel expense is attributed to higher variable compensation accruals in the second quarter 2023.

Professional and legal—The $676,000 or 64 percent decrease in professional and legal expense is attributed to higher legal fees associated with corporate matters in the second quarter 2022.

Marketing—The $46,000 or 11 percent decrease in marketing expense is related to the marketing campaigns related to the new Hunt Valley Connections Center in the second quarter 2022.

FDIC insurance—The $56,000 or 30 percent increase in FDIC insurance expense is attributed to higher assessment rates during the current period.

(Recovery of) impaired loan carrying costs—The $395,000 or 252 percent decrease in impaired loan carrying costs is attributed to the recovery of costs of prior periods during the current quarter.

Oher—The $794,000 or 42 percent decrease in other expense is associated with corporate matters in the second quarter 2022.

Provision for Income Taxes

The provision for income taxes for the second quarter 2023 was $1,940,000 an increase of $1,440,000 or 288 percent as compared to the second quarter 2022. The increase was attributed to higher pre-tax net income for the second quarter 2023 compared to the second quarter 2022. The effective tax rate for the three months ended June 30, 2023 and June 30, 2022 was 22.7 percent and 20.4 percent, respectively. The effective tax rate differs from the statutory tax rate primarily due to the impact of certain elements with specific tax benefits, including tax-exempt income, such as income from tax-exempt investments, tax-exempt loans, and bank-owned life insurance.

Six Months Ended June 30, 2023 vs. Six Months Ended June 30, 2022

The Corporation's net income (earnings) was $13,603,000 for the first six months of 2023 compared to $5,006,000 for the first six months of 2023, an increase of $8,597,000 or 172 percent.

The schedule below presents selected performance metrics for the first six months of both 2023 and 2022.

	Six months ended June 30, 2023	Six months ended June 30, 2022
Basic earnings per share	$ 1.42	$ 0.53
Diluted earnings per share	$ 1.42	$ 0.52
Cash dividend payout ratio	22.56 %	56.93 %
Return on average assets	1.25 %	0.42 %
Return on average equity	14.80 %	5.35 %
Net interest margin (tax equivalent basis)	3.90 %	2.98 %
Net overhead ratio	2.02 %	1.96 %
Efficiency ratio	61.57 %	74.47 %
Average equity to average assets	8.48 %	7.93 %

A more detailed analysis of the factors and trends affecting the Corporation's earnings and financial position follows.

INCOME STATEMENT ANALYSIS

Net Interest Income

Net interest income for the six months ended June 30, 2023 was $40,454,000, an increase of $7,014,000 or 21 percent compared to net interest income of $33,440,000 for the first six months of 2022. The primary contributor to the increase was higher rates on commercial loans. Also contributing to the increase was higher nterest rates on interest bearing deposits with banks, higher volume and rates on investment securities, partially offset by higher cost of interest bearing demand deposits and time deposits.

The Corporation's net interest margin, computed as interest income (tax-equivalent basis) annualized as a percentage of average interest earning assets, was 3.90 percent for the first six months of 2023, representing an increase compared to the 2.98 percent net interest margin for the first six months of 2022. The net interest margin expansion was a predominantly the result of higher rates on commercial loans, partially offset by higher rates on interest bearing demand deposits and time deposits.

Total interest income for the first six months of 2023 totaled $54,283,000, an increase of $17,703,000 or 48 percent above the amount of total interest income for the first six months of 2022. The change was primarily a result of higher rates on commercial loans and higher volume and rates on investment securities. Higher rates on interest bearing deposits with banks were mostly offset by a lower volume of such deposits.

Interest income on loans increased $15,368,000 or 47 percent in the first six months of 2023 compared to the same period in 2022. The average balance of outstanding loans increased $100,994,000 or 7 percent in the first six months of 2023 compared to the first six months of 2022.

Investment income for the first six months of 2023 increased $1,982,000 or 61 percent compared to the first six months of 2022. The average balance of investment securities increased $79,572,000 or 25 percent in the first six months of 2023 compared to the first six months of 2022, reflecting the change in mix of earning assets from interest bearing deposits with banks to investment securities. The tax-equivalent yield on investments for the first six months of 2023 was 2.70 percent or 58 basis points higher than the 2.12 percent experienced during the first six months of 2022. The average balance of interest bearing deposits with banks decreased $355,426,000 or 87 percent in the first six months of 2023 compared to the first six months of 2022. The yield on interest bearing deposits with banks was 4.80 percent for the first six months of 2023, an increase of 437 basis points from 0.43 percent in the first six months of 2022.

Total interest expense for the first six months of 2023 was $13,829,000, an increase of $10,689,000 or 340 percent as compared to total interest expense of $3,140,000 for the first six months of 2022. The change in interest expense was primarily a result of an increase in the cost of interest bearing demand deposits and time deposits.

Interest expense on deposits increased $10,142,000 or 489 percent in the first six months of 2023 compared to the same period in 2022. The change was due primarily to an increase in the cost of interest bearing demand deposits and time deposits. The average balance of interest-bearing deposits for the first six months of 2023 decreased by $127,602,000 or 8 percent compared to the average for the first six months of 2022. The average rate paid on interest-bearing deposits in the first six months of 2023 was 1.69 percent, an increase from the average rate of 0.26 percent paid on interest-bearing deposits during the first six months of 2022. Also, noninterest-bearing deposits decreased, with the average volume for the second quarter 2023 decreasing 15 percent to $431,394,000 as compared to $507,162,000 for the second quarter 2022.

Interest expense on total borrowings for the first six months of 2023 increased 51 percent compared to the first six months of 2022, primarily due to a higher volume of short-term borrowings. Short-term borrowings consisting of repurchase agreements and other short-term borrowings, which includes borrowings from the Federal Home Loan Bank of Pittsburgh (FHLBP) Open Repo Line of Credit averaged $28,603,000 for the first six months of 2023, compared to an average balance of $11,029,000 for the first six months of 2022. The rate on average short-term borrowings for the first half of 2023 was 3.35 percent, an increase as compared to a rate of 0.40 percent for the same period in 2022. Long-term debt, which includes junior subordinated trust preferred securities, finance leases and long-term FHLBP borrowings, averaged $14,605,000 for the first six months of 2023 and $22,591,000 for the first six months of 2022. The decrease was attributable to FHLBP advances totaling $10,000,000 which matured and were repaid in the second quarter of 2022. For the first six months of 2023, the rate on average long-term debt was 5.55 percent, an increase of 280 basis points as compared to a rate of 2.75 percent for the first six months of 2022. Subordinated debentures, issued in December 2020 by the Corporation, averaged $30,787,000 for the first six months of 2023 and $30,706,000 for the first six months of 2022.

Table 5-Average Balances and Interest Rates (tax equivalent basis)

	Six months ended June 30,					
	2023			2022		
(dollars in thousands)	Average Balance	Interest	Yield/ Rate	Average Balance	Interest	Yield/ Rate
Assets						
Interest bearing deposits with banks	$ 51,598	$ 1,229	4.80 %	$ 407,024	$ 876	0.43 %
Investment securities:						
Taxable	369,754	5,017	2.74	288,164	3,031	2.12
Tax-exempt	23,057	246	2.15	25,075	256	2.06
Total investment securities	392,811	5,263	2.70	313,239	3,287	2.12
Loans:						
Taxable (1)	1,629,051	47,490	5.88	1,537,122	32,241	4.23
Tax-exempt	22,443	431	3.87	13,378	287	4.33
Total loans	1,651,494	47,921	5.85	1,550,500	32,528	4.23
Total earning assets	2,095,903	54,413	5.24	2,270,763	36,691	3.26
Other assets (2)	72,031			87,410		
Total assets	$ 2,167,934			$ 2,358,173		
Liabilities and Shareholders' Equity						
Deposits:						
Interest bearing demand	$ 901,186	$ 8,073	1.81 %	$ 989,158	$ 761	0.16 %
Savings	155,578	24	0.03	160,639	24	0.03
Time	402,569	4,117	2.06	437,138	1,287	0.59
Total interest bearing deposits	1,459,333	12,214	1.69	1,586,935	2,072	0.26
Short-term borrowings	28,603	475	3.35	11,029	22	0.40
Long-term debt	14,605	402	5.55	22,591	308	2.75
Subordinated debentures	30,787	738	4.83	30,706	738	4.85
Total interest bearing liabilities	1,533,328	13,829	1.82	1,651,261	3,140	0.38
Noninterest bearing deposits	431,394			507,162		
Other liabilities	19,391			12,649		
Shareholders' equity	183,821			187,101		
Total liabilities and shareholders' equity	$ 2,167,934			$ 2,358,173		
Net interest income (tax equivalent basis)		$ 40,584			$ 33,551	
Net interest margin (3)			3.90 %			2.98 %
Tax equivalent adjustment		(130)			(111)	
Net interest income		$ 40,454			$ 33,440	

(1)Average balance includes average nonaccrual loans of $8,475,000 for 2023 and $31,514,000 for 2022.
Interest includes net loan fees of $1,509,000 for 2023 and $2,647,000 for 2022.
(2)Average balance includes average bank owned life insurance and foreclosed real estate.
(3)Net interest income (tax equivalent basis) annualized as a percentage of average interest earning assets.

Table 6-Rate/Volume Analysis of Changes in Net Interest Income (tax equivalent basis)

	Six months ended June 30, 2023 vs. 2022		
	Increase (decrease) due to change in*		
(dollars in thousands)	Volume	Rate	Net
Interest Income			
Interest bearing deposits with banks	$ (765)	$ 1,118	$ 353
Investment securities:			
Taxable	846	1,140	1,986
Tax-exempt	(21)	11	(10)
Loans:			
Taxable	1,105	14,144	15,249
Tax-exempt	195	(51)	144
Total interest income	1,360	16,362	17,722
Interest Expense			
Deposits:			
Interest bearing demand	(64)	7,376	7,312
Savings	1	(1)	0
Time	(102)	2,932	2,830
Short-term borrowings	2	451	453
Long-term debt	(123)	217	94
Subordinated debentures	2	(2)	0
Total interest expense	(284)	10,973	10,689
Net interest income (tax equivalent basis)	$ 1,644	$ 5,389	$ 7,033

*Changes which are due to both volume and rate are allocated in proportion to their relationship to the amount of change attributed directly to volume or rate.

Provision for Credit Losses

The provision for credit losses is an expense charged to earnings to cover the estimated losses attributable to uncollected loans. The provision reflects management’s judgment of an appropriate level for the allowance for credit losses. Total provision for credit losses, including off-balance sheet exposures, for the first six months of 2023 was $661,000. The allowance as a percentage of total loans was 1.23 percent at June 30, 2023, as compared to 1.27 percent at December 31, 2022 and 1.44 percent at June 30, 2022.

More information about the allowance for loan losses can be found in this report under the caption Allowance for Loan Losses on page 56.

Noninterest Income

The following table presents the components of total noninterest income for the first six months of 2023, compared to the first six months of 2022.

Table 7 - Noninterest income

	Six months ended June 30,		Change Increase (Decrease)	
(dollars in thousands)	2023	2022	$	%
Trust and investment services fees	$ 2,477	$ 2,299	$ 178	8 %
Income from mutual fund, annuity and insurance sales	692	675	17	3
Service charges on deposit accounts	3,026	2,650	376	14
Income from bank owned life insurance	651	619	32	5
Other income	1,449	951	498	52
Gain on sales of loans held for sale	6	579	(573)	(99)
Gain on sales of assets held for sale	118	0	118	100
Loss on sales of securities	(388)	0	(388)	100
Total noninterest income	$ 8,031	$ 7,773	$ 258	3 %

The discussion that follows addresses changes in selected categories of noninterest income.

Other income—The $498,000 or 52 percent increase in other income is attributable to fees associated with interest rate swaps recognized in the current period.

Gain on sales of loans held for sale—The $573,000 or 99 percent decrease in gain on sales of loans is due to the sale of a smaller volume of mortgage loans to the secondary market during the current period.

Gain on sales of assets held for sale—The $118,000 or 100 percent increase in gain on sales of assets is due to the sale of the Gardenville branch real estate during the current period.

Loss on sales of securities—There was a $388,000 loss on sales of securities in the current period compared to no sales of securities in the prior period.

Noninterest Expense

The following table presents the components of total noninterest expense for the first six months of 2023, compared to the first six months of 2022.

Table 8 - Noninterest expense

	Six months ended June 30,		Change Increase (Decrease)	
(dollars in thousands)	**2023**	**2022**	**$**	**%**
Personnel	$ 18,531	$ 16,881	$ 1,650	10 %
Occupancy of premises, net	1,858	1,901	(43)	(2)
Furniture and equipment	1,716	1,699	17	1
Professional and legal	846	1,914	(1,068)	(56)
Marketing	663	833	(170)	(20)
FDIC insurance	494	427	67	16
Debit card processing	910	767	143	19
Charitable donations	931	915	16	2
External data processing	2,053	1,839	214	12
(Recovery of) impaired loan carrying costs	(336)	295	(631)	(214)
Other	2,621	3,428	(807)	(24)
Total noninterest expense	$ 30,287	$ 30,899	$ (612)	(2)%

The discussion that follows addresses changes in selected categories of noninterest expense.

Personnel—The $1,650,000 or 10 percent increase in personnel expense is attributed to higher variable compensation accruals in the current period.

Professional and legal—The $1,068,000 or 56 percent decrease in professional and legal expense is primarily due to corporate matters in the prior period.

Marketing—The $170,000 or 20 percent decrease in marketing expense is due to activity with branding and marketing campaigns in the prior period.

FDIC insurance—The $67,000 or 16 percent increase in FDIC insurance expense is attributed to higher assessment rates in the current period.

Debit card processing—The $143,000 or 19 percent increase in debit card processing expense is attributed to higher reliance by our clients on electronic access to their accounts in the current period.

(Recovery of) impaired loan carrying costs—The $631,000 or 214 percent decrease in impaired loan carrying costs is attributed to the recovery of costs associated with impaired loans during the current period.

Other—The $807,000 or 24 percent decrease in other expense is primarily related to corporate matters in the prior period.

Provision for Income Taxes

The provision for income taxes for the six months ended June 30, 2023 was $3,934,000 an increase of $2,627,000 or 201 percent as compared to the six months ended June 30, 2022. The increase was attributed to higher pre-tax net income for the six months ended June 30, 2023 compared to the six months ended June 30, 2022. The effective tax rate for the six months ended June 30, 2023 and June 30, 2022 was 22.4 percent and 20.7 percent, respectively. The effective tax rate differs from the statutory tax rate primarily due to the impact of certain elements with specific tax benefits, including tax-exempt income, such as income from tax-exempt investments, tax-exempt loans, and bank-owned life insurance

BALANCE SHEET REVIEW

Interest Bearing Deposits with Banks

On June 30, 2023, interest bearing deposits with banks totaled $68,946,000, a decrease of $30,831,000 or 31 percent, compared to the level at year-end 2022. The decrease is primarily the result of an increase in commercial loans.

Investment Securities (Available-for-Sale)

The Corporation's entire investment securities portfolio is classified available-for-sale, and is comprised of interest-earning debt securities. The overall composition of the Corporation's investment securities portfolio is provided in Note 2—Securities. On June 30, 2023, the fair value of investment securities available-for-sale totaled $342,691,000, which represented a decrease of $2,766,000 as compared to the fair value of investment securities at year-end 2022. Purchases of securities did not exceed the cash flows from principal reductions and maturities during the first six months of 2023.

Restricted Investments in Bank Stock, at Cost

On June 30, 2023, restricted investments in bank stock, at cost, was $3,917,000, which was $2,962,000 or 310 percent higher than the level at year-end 2022. This was attributable to short-term borrowings of $70,000,000 with FHLBP, which requires a corresponding membership stock purchase.

Loans Held For Sale

On June 30, 2023, loans held for sale totaled $428,000, which was $274,000 or 178 percent higher than the level at year-end 2022. This was primarily attributable to SBA loans held for sale at the end of the period.

Loans Held For Investment

On June 30, 2023, total loans, net of deferred fees, were $1.66 billion, which was $48,886,000 or 3 percent higher than the level at year-end 2022. The composition of the Corporation's loan portfolio is provided in Note 4—Loans and Allowance for Credit Losses.

Deposits

Deposits are the Corporation's principal source of funding for earning assets. On June 30, 2023, deposits totaled $1.88 billion, which reflected a $60,546,000 or 3 percent decrease compared to the level at year-end 2022. Of the decrease in total deposits, $5,563,000 is attributable to noninterest bearing deposits and $4,983,000 is related to interest bearing deposits, primarily money market accounts, offset by an increase in time deposits. The composition of the Corporation's total deposit portfolio is provided in Note 5—Deposits.

Short-term Borrowings

Short-term borrowings, which consist of securities sold under agreements to repurchase (repurchase agreements), federal funds purchased, and other short-term borrowings, totaled $83,320,000 at June 30, 2023, which reflected a $71,715,000 or 618 percent increase compared to the level at year-end 2022. At June 30, 2023, the balance of other short-term borrowings was $70,000,000 compared to $0 at December 31, 2022, which consisted of FHLBP Open Repo line of credit advances.

Long-term Debt and Subordinated Debentures

The Corporation uses long-term borrowings as a secondary funding source for asset growth and to manage interest rate risk. On June 30, 2023, long-term debt, including subordinated debentures totaled $42,339,000 compared to $42,314,000 at year-end 2022. A listing of outstanding long-term debt obligations is provided in Note 6—Short-Term Borrowings and Long-Term Debt.

Shareholders’ Equity and Capital Adequacy

Shareholders’ equity, or capital, enables Codorus Valley to maintain asset growth and absorb losses. Capital adequacy can be affected by a multitude of factors, including profitability, new stock issuances, corporate expansion and acquisitions, dividend policy and distributions, and regulatory mandates. The Corporation’s total shareholders’ equity was approximately $185,869,000 on June 30, 2023, an increase of $8,569,000 or 5 percent compared to the level at year-end 2022. The increase was primarily attributable to net income of $13,600,000, partially offset by dividends paid of $3,100,000 for the six months ended June 30, 2023 and the adoption of ASC Topic 326 (CECL) of $2,100,000.

Cash Dividends on Stock

The Corporation has historically paid cash dividends on its stock on a quarterly basis. The Board of Directors determines the dividend rate after considering the Corporation's capital requirements, current and projected net income, and other relevant factors. As recently announced, the Board of Directors declared a quarterly cash dividend of $0.17 per share on July 11, 2023, payable on August 8, 2023, to shareholders of record at the close of business on July 25, 2023. The cash dividend follows a quarterly cash dividend of $0.16 per share distributed in February 2023 and May 2023.

Capital Adequacy

The Corporation and PeoplesBank are subject to various regulatory capital requirements administered by banking regulators that involve quantitative guidelines and qualitative judgments. The regulatory capital measures for the Corporation and PeoplesBank as of June 30, 2023 and the minimum capital ratios established by regulators are set forth in Note 8—Regulatory Matters to the financial statements. We believe that PeoplesBank is well capitalized on June 30, 2023 and had no regulatory dividend restrictions (see Note 8—Regulatory Matters to the financial statements).

RISK MANAGEMENT

Credit Risk Management

Credit risk represents the possibility that a loan client, counterparty or issuer may not perform in accordance with contractual terms, posing one of the most significant risks of loss to the Corporation. Accordingly, the Corporation emphasizes the management of credit risk, and has established a lending policy which management believes is sound given the nature and scope of our operations. The Credit Risk Management section included in Item 7 of the Corporation’s previously filed Annual Report on Form 10-K for the year ended December 31, 2022, provides a more detailed overview of the Corporation’s credit risk management process.

Management regularly analyzes the commercial real estate portfolio, which includes the review of occupancy, cash flows, expenses and expiring leases, as well as the location of the real estate. At June 30, 2023, the Corporation has $142,000,000 total potential exposure in loans related to office space. Management believes that the office space portfolio is well-diversified and includes only limited exposure to properties located in major metro markets.

Nonperforming Assets

Nonperforming assets, as shown in the table below, are asset categories that pose the greatest risk of loss. The level of nonperforming assets at June 30, 2023 was $11,765,000, which increased by $316,000 or 3 percent when compared to year-end 2022, of which $1,213,000 relates to troubled debt restructured loans reported under previously applicable GAAP. The increase was primarily attributed one commercial construction loan that was more than 90 days past due but still accuring at June 30, 2023, offset by a reduction of nonaccrual loans.

The Corporation regularly monitors large and criticized assets in its commercial loan portfolio recognizing that prolonged low economic growth, or a weakening economy, could have negative effects on these commercial borrowers. Nonperforming assets are monitored and managed for collection of these accounts. Collection efforts, including modification of contractual terms for individual accounts based on prevailing market conditions and liquidation of collateral assets, are employed to maximize recovery. A special assets committee meets regularly, at a minimum quarterly, to review nonperforming assets. We generally rely on appraisals performed by independent licensed appraisers to determine the value of real estate collateral for collateral-dependent loans. Generally, an appraisal is performed when: an account reaches 90 days past due, unless a certified appraisal was completed within the past twelve months; market values have changed significantly; the condition of the property has changed significantly; or the existing appraisal is outdated based upon regulatory or policy requirements. In instances where the value of the collateral, net of costs to sell, is less than the net carrying amount for individually evaluated commercial related loans, a specific loss allowance is established for the difference. Further provisions for credit losses may be required for nonaccrual loans as additional information becomes available or conditions change. When it is probable that some portion or an entire loan balance will not be collected, that amount is charged off as loss against the allowance.

The paragraphs and table below address significant changes in the nonperforming asset categories as of June 30, 2023 compared to December 31, 2022.

Table 9 – Nonperforming assets

(dollars in thousands)		**June 30, 2023**
Nonaccrual loans:		
Commercial loans	$	6,081
Commercial real estate:		
Construction		42
Owner occupied		2,124
Non-owner occupied		54
Residential real estate:		
Revolving		484
Other		845
Total nonaccrual loans	$	9,630
Accruing loans that are contractually past due 90 days or more as to principal and interest:		
Commercial real estate:		
Construction	$	1,693
Other Real Estate Owned	$	442
Total Nonperforming assets	$	11,765
Individually evaluated loans without a valuation allowance	$	7,903
Individually evaluated loans with a valuation allowance		1,727
Total individually evaluated loans	$	9,630
Valuation allowance related to individually evaluated loans	$	1,172
Nonperforming loans as a % of total loans		0.67 %
Nonperforming assets to total loans and foreclosed real estate		0.70 %
Nonperforming assets as a % of total period-end assets		0.53 %
ACL as a % of nonperforming loans		182.65 %
ACL as a % of nonperforming assets		175.78 %
ACL as a % of total loans		1.23 %
Nonaccrual loans as a % of applicable portfolio:		
Commercial loans		3.59 %
Commercial real estate:		
Construction		0.02 %
Owner occupied		0.62 %
Non-owner occupied		0.01 %
Residential real estate:		
Revolving		0.47 %
Other		0.32 %

(dollars in thousands)		**December 31, 2022**
Nonaccrual loans:		
Builder & developer	$	1,773
Commercial real estate investor		222
Residential real estate investor		856
Manufacturing		2,965
Agriculture		912
Commercial other		3,436
Residential mortgages		349
Home equity		457
Total nonaccrual loans	$	10,970
Troubled debt restructurings (TDRs):		
Performing	$	1,213
Total TDR loans	$	1,213
Other Real Estate Owned:	$	479
Total Nonperforming assets	$	11,449
Impaired loans without a valuation allowance	$	9,400
Impaired loans with a valuation allowance		2,783
Total impaired loans	$	12,183
Valuation allowance related to impaired loans	$	2,484
Nonaccrual loans as a % of total loans		0.67 %
Nonperforming loans as a % of total loans		0.67 %
Nonperforming assets as a % of total period-end assets		0.52 %
ALL as a % of nonaccrual loans		189.02 %
ALL as a % of nonperforming assets		181.12 %
ALL as a % of total loans		1.27 %
Nonaccrual loans as a % of applicable portfolio:		
Builder & developer		1.38 %
Commercial real estate investor		0.06 %
Residential real estate investor		0.33 %
Manufacturing		3.42 %
Agriculture		1.00 %
Commercial other		1.64 %
Residential mortgages		0.26 %
Home equity		0.47 %

Nonperforming loans

Nonperforming loans consist of nonaccrual loans and accruing loans 90 days or more past due. We generally place a loan on nonaccrual status and cease accruing interest income (i.e., recognize interest income on a cash basis, as long as the loan is sufficiently collateralized) when loan payment performance is unsatisfactory and the loan is past due 90 days or more. A loan is returned to interest accruing status when we determine that circumstances have improved to the extent that all of the principal and interest amounts contractually due are current for at least six consecutive payments and future payments are reasonably assured. Loans past due 90 days or more and still accruing interest represent loans that are contractually past due, but are well collateralized and in the process of collection. As of June 30, 2023, the nonperforming loan portfolio balance totaled $11,323,000, compared to $10,970,000 at year-end 2022. For both periods, the nonperforming portfolio balance was comprised primarily of collateralized commercial loans.

Foreclosed Real Estate

Foreclosed real estate represents real estate acquired to satisfy debts owed to PeoplesBank and is included in the Other Assets category on the Corporation's balance sheet. Foreclosed real estate was $442,000 as of June 30, 2023 and $479,000 as of December 31, 2022. A write-down of $37,000 was recorded during the second quarter of 2023.

Allowance for Credit Losses (ACL)

The ACL is a reserve accumulated on the Consolidated Balance Sheets through the recognition of the provision for credit losses. The Corporation records a provision for credit losses in the Consolidated Statements of Income to maintain the ACL at a level considered sufficient to absorb expected credit losses.

The ACL on loans was $20,681,000 as of June 30, 2023 and $20,736,000 as of December 31, 2022. As a percentage of period-end loans, the ACL was 1.23 percent as of June 30, 2023 and 1.27 percent as of December 31, 2022. As detailed in Note 1–Summary of Significant Accounting Policies, the ACL increased $927,000 at the adoption of CECL.

The ACL as a percentage of nonperforming loans was 182.65 percent as of June 30, 2023 and 189.02 percent as of December 31, 2022. The ACL as a percentage of nonperforming assets was 175.78 percent as of June 30, 2023 and 181.12 percent as of December 31, 2022.

The ACL on unfunded commitments was $2,089,000 as of June 30, 2023 and $0 as of December 31, 2022. The Corporation recorded $200,000 of provision for credit losses on unfunded commitments for the six months ended June 30, 2023, compared to none in the prior year. Similar to the increase in ACL on loans, the increase in ACL and provision expense on unfunded commitments was related to the adoption of CECL.

Liquidity Risk Management

Maintaining adequate liquidity provides the Corporation with the ability to meet financial obligations to depositors, loan clients, employees, and shareholders on a timely and cost effective basis in the normal course of business. Additionally, adequate liquidity provides funds for growth and business opportunities as they arise. Liquidity is generated from transactions relating to both the Corporation's assets and liabilities. The primary sources of asset liquidity are funds received from client loan payments, investment maturities and cash inflows from mortgage-backed securities, and the net proceeds of asset sales. The primary sources of liability liquidity are deposit growth, and funds obtained from short-term borrowings and long-term debt. The Consolidated Statements of Cash Flows, included in this report, present the changes in cash from operating, investing and financing activities. At June 30, 2023, we believe that liquidity was adequate based upon the availability of unpledged available-for-sale securities with a fair value totaling approximately $156,914,000. With an unrealized loss of $19,470,000, liquidation options would need to be considered, however there would be options for pledging of these securities to other borrowing sources. Although the Corporation has not utilized the Federal Reserve's Bank Term Funding Facility as of June 30, 2023, the program has attractive features, such as being able to borrow based on the par values (rather than market values) of a bank's investment securities that are pledged as collateral. For this reason, the program would be considered among the Corporation's other wholesale borrowing options if additional liquidity was needed. Available credit from the Federal Home Loan Bank of Pittsburgh totals approximately $696,200,000. The Corporation's loan-to-deposit ratio was 89.3 percent as of June 30, 2023, 84.0 percent as of December 31, 2022 and 72.9 percent as of March 31, 2022.

Off-Balance Sheet Arrangements

The Corporation's financial statements do not reflect various commitments that are made in the normal course of business, which may involve some liquidity risk. These commitments consist primarily of commitments to grant new loans, unfunded commitments under existing loan facilities, and letters of credit issued under the same standards as on-balance sheet instruments. Unused commitments at June 30, 2023, totaled $715,878,000 and consisted of $650,785,000 in unfunded commitments under existing loan facilities, $46,992,000 to grant new loans and $18,101,000 in letters of credit. Generally these commitments have fixed expiration dates or termination clauses and are for specific purposes. Accordingly, many of the commitments are expected to expire without being drawn upon and, therefore, generally do not present significant liquidity risk to the Corporation or PeoplesBank.

Critical Accounting Estimates

Disclosure of the Corporation's significant accounting policies is included in Note 1 in the notes to the consolidated financial statements its December 31, 2022 Form 10-K. Some of these policies require management to make significant judgments, estimates and assumptions that have a material impact on the carrying value of certain assets and liabilities. Management makes significant estimates in determining the allowance for credit loans. Subsequent to the adoption of ASC 326 in the first quarter of 2023, the Corporation's accounting policy for ACL – loans is now as follows:

<u>Allowance for credit losses – loans</u>
The allowance for credit losses ("ACL") is a valuation account that is deducted from the loans' amortized cost basis to present the net amount expected to be collected on the loans. Loans are charged off against the allowance when management believes the uncollectibility of a loan balance is confirmed. Expected recoveries do not exceed the aggregate of amounts previously charged-off and expected to be charged-off.

Management estimates the allowance balance using relevant available information from both internal and external sources, relating to past events, current conditions and reasonable and supportable forecasts. Historical credit loss experience provides the basis for the estimation of expected credit losses. Adjustments to historical loss information are made for differences in current loan-specific risk characteristics such as differences in underwriting standards, portfolio mix, delinquency level, or term as well as changes in environmental conditions, such as changes in unemployment rates, property values, or other relevant factors. These adjustments are commonly known as the Qualitative Framework.

In addition to the estimated quantitative credit loss for loans evaluated collectively, qualitative factors that may not be fully captured in the quantitative results are also evaluated. These include changes in lending policy, the nature and volume of the portfolio, overall business conditions in the economy, credit concentrations, competition, model imprecision, and legal and regulatory requirements. Qualitative adjustments are judgmental and are based on management's knowledge of the portfolio and the markets in which the Corporation operates. Qualitative adjustments are evaluated and approved on a quarterly basis. Additionally, the ACL includes other allowance categories that are not directly incorporated in the quantitative results including loans in process.

The allowance for credit losses is measured on a collective (pool) basis when similar risk characteristics exist. Loans evaluated collectively for expected credit losses include loans on accrual status and loans initially evaluated individually but determined to not to have enhanced credit risk characteristics. The Corporation has identified the following portfolio segments:

- Commercial loans
- Commercial real estate – construction
- Commercial real estate – owner occupied
- Commercial real estate – non-owner occupied
- Residential real estate – construction
- Residential real estate – revolving
- Residential real estate – multi family
- Residential real estate – other
- Consumer loans

The Corporation measures the allowance for credit losses using the following methods.

- Loans are aggregated into pools based on similar risk characteristics.
- The Probability of Default (PD) and Loss Given Default (LGD) CECL model components are determined based on loss estimates driven by historical experience at the input level.
- The PD model component uses "through the economic cycle transition" matrices based on the Corporation's and peer group historical loan and transaction data across each pool of loans.
- The LGD model component calculates a lifetime estimate across each pool of loans utilizing a nonparametric loss curve modeling approach.
- Reasonable and supportable forecasts are incorporated into the PD model component that are based on different economic forecasts and scenarios sourced from an external party. A future loss forecast over the reasonable and supportable forecast period is based on the projected performance of specific economic variables that statistically correlate with the PD and LGD pools. After the reasonable and supportable forecast period, loss estimates naturally revert to input-level reversion.
- Cash flow assumptions are established for each loan using maturity date, amortization schedule and interest rate.
- A constant prepayment rate is calculated for each loan pool in the CECL model.

Loans that do not share risk characteristics are evaluated on an individual basis. Loans evaluated individually are not also included in the collective evaluation. When management determines that foreclosure is probable or when the borrower is experiencing financial difficulty at the reporting date and repayment is expected to be provided substantially through the operation or sale of the collateral expected credit losses are based on the fair value of the collateral at the reporting date, adjusted for selling costs as appropriate.

Loans are modified if the Corporation grants borrowers experiencing financial difficulties concessions that it would not otherwise consider. Concessions granted under a modification may involve a reduction of the interest rate, forgiveness of principal, extension of the term of the loan, and/or other-than-insignificant payment delays.

Expected credit losses are estimated over the contractual terms of the loans, adjusted for expected prepayments when appropriate.

To the extent actual outcomes differ from management's estimates, additional provision for credit losses may be required that would impact the Corporation's operating results.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

The most significant market risk to which the Corporation is exposed is interest rate risk. The primary business of the Corporation and the composition of its balance sheet consist of investments in interest earning assets (primarily loans and securities), which are funded by interest bearing liabilities (deposits and borrowings), all of which have varying levels of sensitivity to changes in market interest rates. Changes in rates also have an impact on the Corporation's liquidity position and could affect its ability to meet obligations and continue to grow.

The Corporation employs various management techniques to minimize its exposure to interest rate risk. An Asset Liability Management Committee, consisting of key financial and senior management personnel, meets on a regular basis. The Committee is responsible for reviewing the interest rate sensitivity and liquidity positions of the Corporation, reviewing projected sources and uses of funds, approving asset and liability management policies, monitoring economic conditions, and overseeing the formulation and implementation of strategies regarding balance sheet positions.

Simulation of net interest income is performed for the next twelve-month period. A variety of interest rate scenarios are used to measure the effects of sudden and gradual movements upward and downward in the yield curve. These results are compared to the results obtained in a flat or unchanged interest rate scenario. Simulation of net interest income is used primarily to measure the Corporation's short-term earnings exposure to rate movements. A "shock" is an immediate upward or downward movement of interest rates. The shocks do not take into account changes in client behavior that could result in changes to mix and/or volumes in the balance sheet, nor do they account for competitive pricing over the forward 12-month period. The Corporation applies these interest rate "shocks" to its financial instruments up and down 100, 200, 300, and 400 basis points. A 400 basis point decrease in interest rates is not simulated at this time.

The following table summarizes the expected impact of interest rate shocks on net interest income as well as the Corporation's policy limits at each level. All scenarios were within policy limits at June 30, 2023.

Change in Interest Rates (basis points)	**Annual Change in Net Interest Income (in thousands)**	**% Change in Net Interest Income**	**% Change Policy Limit**
+100	$ 920	1.13 %	(7.50) %
(100)	$ (79)	(0.10) %	(7.50) %
+200	$ 2,044	2.52 %	(15.00) %
(200)	$ (797)	(0.98) %	(15.00) %
+300	$ 3,186	3.92 %	(25.00) %
(300)	$ (2,458)	(3.03) %	(25.00) %
+400	$ 4,343	5.35 %	(35.00) %

Item 4. Controls and Procedures

The Corporation carried out an evaluation, under the supervision and with the participation of the Corporation's management, including the Corporation's Chief Executive Officer and Treasurer, of the effectiveness of its disclosure controls and procedures, as defined in Exchange Act Rules 13a-15(e) and 15d-15(e). Based upon the evaluation, the Corporation's Chief Executive Officer and Treasurer concluded that, as of June 30, 2023, the Corporation's disclosure controls and procedures were effective. The Corporation's disclosure controls and procedures are designed to provide reasonable, not absolute, assurance that information required to be disclosed in the Corporation's reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms. A control system, no matter how well conceived and operated, must reflect the fact that there are resource constraints and that the benefits of controls must be considered relative to their costs, and no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within a company have been detected.

Effective January 1, 2023, the Corporation adopted ASC 326. The Corporation designed new controls and modified existing controls in conjunction with its adoption. These additional controls over financial reporting included controls over model creation and design, model governance and model assumptions, among others. There were no changes in the Corporation's internal control over financial reporting that occurred during the period covered by this report that have materially affected, or are reasonably likely to materially affect, the Corporation's internal control over financial reporting.

Part II—OTHER INFORMATION

Item 1. Legal Proceedings

The Corporation is involved in pending and threatened claims and other legal proceedings from time to time in the ordinary course of its business activities. Management evaluates the possible impact of these matters taking into consideration the most recent information available. A loss reserve is established for any matter for which it is believed that a loss is both probable and reasonably estimable. Once established, the reserve is adjusted as appropriate to reflect any subsequent developments. Actual losses with respect to any such matter may be more or less than the amount estimated. For any matter for which a loss is not probable, or the amount of the loss cannot reasonably be estimated, no loss reserve is established.

In addition, the Corporation may be involved in legal proceedings in the form of investigations of regulatory or governmental inquiries covering a range of possible issues. These could be specific to the Corporation, or part of more wide-spread inquires by regulatory authorities. These inquiries or investigations could lead to administrative, civil or criminal proceedings involving the Corporation and could result in fines, penalties, restitution, or other types of sanctions, or the need for the Corporation to undertake remedial actions, or to alter its business, financial or accounting practices.

Management believes that any liabilities, individually or in the aggregate, that may result from the final outcomes of pending or threatened legal proceedings will not have a material adverse effect on the financial condition of the Corporation or upon its results of operations.

Item 1A. Risk Factors

Other than the risk factors set for below, there have been no material changes to the risk factors as previously disclosed in Item 1A – Risk Factors – in the Corporation's 2022 10K.

Risks Related to Recent Banking Industry Turmoil

The Corporation is exposed to the risk that when a bank or other financial institution experiences financial difficulties, there could be an adverse "contagion" impact on other banking institutions. The failures of Silicon Valley Bank in California, Signature Bank in New York and First Republic Bank in California during the first and second quarters of 2023 caused an element of panic and uncertainty in the investor community and among bank customers generally, including, specifically, deposit customers. While the Corporation does not believe that the circumstances of these three failures are necessarily indicators of broader issues for concern with all other banks or with the banking system itself, the failures are likely to reduce customer confidence, affect sources of funding and liquidity, increase regulatory requirements and costs, adversely affect financial markets and/or have negative reputational ramifications for institutions in the banking industry, including, possibly, the Corporation and its PeoplesBank subsidiary. The Corporation will continue to closely monitor the ongoing events and volatility in the financial services industry, together with any responsive measures taken by the banking regulators to mitigate or manage the concerns of bank customers regarding FDIC deposit insurance coverage and the safety and soundness of community banks.

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

The Corporation relies on its subsidiary PeoplesBank, A Codorus Valley Company, for dividend distributions, which are subject to restrictions as reported in Note 9—Regulatory Matters of the Corporation's Annual Report on Form 10-K for the year ended December 31, 2022.

The Corporation's Board of Directors approved a new Share Repurchase Program in January 2023. Under the newly approved Program, the Corporation is authorized to repurchase up to $5 million of the Corporation's issued and outstanding common stock. All shares of common stock repurchased pursuant to the Program are required to be held as treasury shares and be available for use and reissuance for purposes as and when determined by the Board of Directors including, without limitation, pursuant to the Corporation's Dividend Reinvestment and Stock Purchase Plan and its equity compensation program. There was no activity under the new Program during the three and six months ended June 30, 2023.

Item 3. Defaults Upon Senior Securities

None

Item 4. Mine Safety Disclosures

This Item 4 is not applicable to the Corporation.

Item 5. Other Information

None

Item 6. Exhibits

Exhibit Number	Description of Exhibit
3.1	Amended Articles of Incorporation (Incorporated by reference to Exhibit 3.1 to the Quarterly Report on Form 10-Q for June 30, 2018, filed with the Commission on August 6, 2018)
3.2	Amended and Restated By-laws (Incorporated by reference to Exhibit 3.1 of the Registrant's Current Report on Form 8-K filed with the Commission on December 20, 2021)
4.1	Form of 4.50% Fixed-to-Floating Rate Subordinated Notes due 2030 of Codorus Valley Bancorp, Inc. (Incorporated by reference to Exhibit 4.1 to the Current Report on Form 8-K filed with the Commission on December 10, 2020)
14	Code of Ethics, dated May 16, 2023 – filed herewith
31.1	Certification of Principal Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 – filed herewith.
31.2	Certification of Principal Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 – filed herewith.
32	Certification of Principal Executive Officer and Principal Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 – filed herewith.
101	Financial statements from the Quarterly Report on Form 10-Q of Codorus Valley Bancorp, Inc. for the quarter ended June 30, 2023, formatted in XBRL: (i) the Consolidated Balance Sheets, (ii) the Consolidated Statements of Income (iii) the Consolidated Statements of Comprehensive Income (iv) the Consolidated Statements of Cash Flows, (v) the Consolidated Statements of Changes in Shareholder's Equity, and (vi) the Notes to Consolidated Financial Statements – filed herewith.
104	Cover page interactive data file (formatted as inline XBRL and contained in 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.

Codorus Valley Bancorp, Inc.
(Registrant)

August 7, 2023 Date	/s/ Craig L. Kauffman Craig L. Kauffman, President and Chief Executive Officer (Principal Executive Officer)
August 7, 2023 Date	/s/ Larry D. Pickett Larry D. Pickett Treasurer (Principal Financial and Accounting Officer)

CODORUS VALLEY BANCORP, INC.
Code of Business Conduct and Ethics
Approved: May 16, 2023

I. PURPOSE AND APPLICATION

The purpose of this Code of Business Conduct and Ethics (this "Code") is to promote honest and ethical conduct, to focus the Board of Directors and employees of Codorus Valley Bancorp, Inc., and its subsidiaries and affiliates, (the "Company") on areas of ethical risk, to provide guidance to directors, and employees to help them recognize and deal with ethical issues, to provide mechanisms to report unethical conduct and to help to preserve a culture of honesty and accountability at the Company.

This Code applies to all directors and employees of the Company (each a "Person") In addition, certain provisions of this Code apply specifically to the directors and officers of the Company, including, but not limited to the Company's President and Chief Executive Officer, Chief Financial Officer, Executive Vice Presidents, Senior Vice Presidents, General Counsel, and all persons performing similar functions (each a "Principal Person").

II. ADMINISTRATION

This Code will be administered and interpreted by the Company's General Counsel. The General Counsel is authorized to formulate and implement rules, procedures, and educational programs designed to promote the effectiveness of this Code and to respond to questions concerning this Code and its application to specific situations. The Company's General Counsel will report as necessary to the Audit Committee of the Board of Directors regarding compliance with this Code, but in any event no less frequently than annually. If questions arise with respect to this Code, they should be referred to the Company's General Counsel at the earliest possible time.

III. ETHICAL PRINCIPLES

A. Fair Dealing

1. Each Person shall act at all times in good faith, responsibly, with honesty and integrity, and with due care, competence, and diligence, without misrepresenting material facts and without allowing such Person's independent judgment to be unduly influenced.

2. No Person shall take unfair advantage of anyone through manipulation, concealment, abuse of privileged information, misrepresentation of facts, or any other unfair dealing.

3. Each Person shall at all times proactively promote ethical behavior among peers in the Person's work environment, and shall not tolerate

any form of harassment, whether based on race, color, religion, gender, national origin, age, disability, veteran status, pregnancy, or sexual orientation.

B. Conflicts of Interest

1. Each Person shall avoid at all times actual or apparentconflicts between private and Company interests. A conflict of interest occurs when an individual's private interest is different from the interests of the Company. Conflicts of interest include:

    - When a Person, or a member of his or herimmediate family, will benefit personally from something the Person does or fails to do that is not in the best interest of the Company;

    - When a Person takes actions or has interests that may make it difficult to perform his or her work for the Company objectively and effectively; and

    - When a Person, or a member of his or herimmediate family, receives personal benefits from someone other than the Company as a result of his or her position in the Company.

2. No Person nor any member of his immediate family shall at any time enter into employment positions or consulting arrangements, acquire any ownership interests, or engage in any other activity that may create an actual or apparent conflict of interest between his personal interests and either (a) the interests of the Company, or (b) his ability to perform his duties and responsibilities for the Company.

3. No Person nor any member of his or her immediate family shall solicit or accept any personal benefit from any outside concern from which the Company secures goods or services, which is a customer of the Company, or which is a competitor of the Company, or which is a regulatory agency having jurisdiction over the Company, except only (a) loans from financial institutions on the same terms generally available to its other customers, and (b) entertainment appropriate to the business relationship, extended in the ordinary course of business, in accordance with the Company's Conflicts of Interest Policy and not intended to influence the actions of the Person or the Company.

4. Each Person shall comply at all times withthe Company's Conflicts of Interest Policy adopted by the Company from time to time

5. Each Principal Person shall immediately disclose to the Chairman of the Audit Committee any material transaction or relationship that

reasonably could be expected to give rise to any conflict of interest, whether real or perceived.

6. For purposes of this Code, the term "immediate family" includes a Person's spouse, parents, children, stepchildren, siblings, mothers and fathers-in-law, sons and daughters-in-law, brothers and sisters-in-law, and other members of their household.

C. Company Information and Confidentiality

1. Any information disclosed by each Person in the performance of his or her duties for the Company shall be full, fair, complete, accurate, objective, relevant, timely, understandable, and not misleading. Each Person shall share at all times important and relevant knowledge (a) with persons to whom such Person reports, and (b) as is appropriate with persons reporting to such Person.

2. Each Person shall maintain at all times the confidentiality of information acquired in the course of his work except when authorized by the Company or otherwise legally obligated to disclose such information. No confidential information acquired in the course of work shall be used by any Person for any personal advantage, whether real or perceived. All Persons shall comply with all confidentiality provisions in agreements to which they or the Company are parties.

3. The term "confidential information" includes, but is not limited to:

   - the Company's business information, records, activities and plans;
   - the identity of, or information relating to, merger and acquisition candidates;
   - the identity, business information, records, activities and plans of clients and prospective clients;
   - the Company's computer programs, system documentation, and software and technology developments;
   - manuals, formulae, processes, methods, ideas, improvements, inventions and compositions;
   - security information such as passwords, personal identification numbers, electronic keys and vault combinations,
   - reports written to and by regulatory agencies; and
   - any additional confidential information described in the Company's Insider Trading Policy.

4. Each Person shall document and report all of the Company's business and financial transactions in accordance with the Company's internal control procedures. No Person shall create misleading records or falsify or improperly destroy company documents.

D. Compliance with Laws, Rules and Regulations (including Insider Trading Laws)

1. Each Person shall comply at all times with all rules and regulations of federal, state, and local governments, and other appropriate private and public regulatory agencies, including but not limited to regulations promulgated by the U.S. Securities and Exchange Commission ("SEC") and any other governmental agencies ("Laws"). In the event that a Person is ever unsure of any such Laws, the Person shall consult with the General Counsel prior to taking any action.

2. No Person nor any member of his or her immediate familyshall at any time buy or sell any security while aware of any material, non-public information relating to the Company or the security. Each Principal Person and all members of his or her immediate family shall refrain from any trading in any Company securities during blackout periods and shall comply with the Company's Insider Trading Policy and SEC requirements during non blackout periods.

3. All Persons shall cooperate fully with the people responsible for preparing reports filed with the SEC and all other materials that are made available to the investing public to make sure those people are aware in a timely manner of all information that might have to be disclosed in those reports or other materials or that might affect the way in which information is disclosed in them.

E. Corporate Opportunities

1. All Persons owe a duty to the Company to advance its legitimate interests when the opportunity to do so arises. No Person shall:

   - take for himself or herself personally any opportunity of which he or she becomes aware, or to which he or she obtains access, through the use of Company property, information or position;
   - make it possible for someone other than the Company to take advantage of an opportunity in any of the Company's areas of business of which the Person becomes aware in the course of his or her activities on behalf of the Company, unless the company has expressly decided not to take advantage of the opportunity;
   - otherwise use Company property, information, or position for personal gain; or

- compete with the Company generally or with regard to specific transactions or opportunities.

F. Improper Use of Corporate Funds or Assets

1. Each Person shall maintain at all times responsible use of and control over all Company assets and resources employed or entrusted to such Person.

2. Each Person shall safeguard against theft, loss, or misuse of any and all property of the Company in the custody or possession of such Person.

3. The following uses of corporate funds or assets are prohibited:

   - Direct or indirect payments, gifts, contributions or offers, or promises of anything of value in the nature of bribes, gratuities, payoffs or kickbacks to domestic or foreign governments, government agencies, business organizations or individuals, or any other effort to obtain favors, including but not limited to inducements to procure orders for the sales of the Company's goods or services. Granting lawful customer discounts and allowances in the ordinary course of business is not prohibited by this Code of Ethics provided such discounts and allowances are properly approved and documented.
   - Excessive gifts or gratuities per individual recipient are prohibited without the express consent of a Person's immediate supervisor (or in the case of the CEO or a Director, the approval of a majority of the Board of Directors). All gifts and gratuities shall be made in the ordinary course of business and in accordance with the guidelines set forth in the Company's Conflicts of Interest Policy.
   - Commissions, fees, or similar payments which are not reasonably related in value to the services rendered; or commissions, fees, or similar payments made in exchange for services that are illegal, improper, or violations of this Code in any manner.
   - Direct or indirect contributions of money, property, or resources to the campaign of a candidate for office in the federal government or in any U.S. political party, other than as permitted by law. Because the laws of various states and foreign countries vary as to the legality of corporate political contributions, all requests for such contributions shall be referred to the Company's General Counsel. It is legal and appropriate for individual Persons to make political contributions with their personal funds and on their own behalf; however, such contributions shall not be reimbursed directly or indirectly by the Company.
   - Use of assets, funds, or resources of the Company by Persons or members of their family, which is personal, or not in the furtherance

of the business of the Company, or payment by the Company of personal expenses of Persons or members of their family, without the express consent of one's immediate supervisor (or in the case of the CEO or a Director, the approval of a majority of the Board of Directors).

4. The use of brokers, consultants, distributors, and agents to assist or counsel in the procurement of contracts and the payment of reasonable fees for their services are within the bounds of ordinary business practice and are not contrary to this Code of Ethics. However, such brokers, consultants, distributors, and agents must perform a bona fide function and actually render bona fide services for the Company. Such individuals are not to be directly or indirectly related to or subject to the control of a customer, prospective customer, or its managing agents or employees.

G. Compliance and Enforcement

1. Each Person shall be held accountable for full compliance with this Code of Ethics. In the event that any Person is determined to have violated this Code of Ethics, such violation shall be reported to the Chief Executive Officer and, if the Person is a Principal Person, the Board of Directors of the Company, and that Person shall be subject to all disciplinary action available, including but not limited to immediate termination of employment by the Company, for cause and possible legal prosecution.

2. Any Person, upon receipt of any information of the possible violation of this Code of Ethics, shall immediately report the same. Possible violations may be reported verbally or in writing and may be reported anonymously. Failure to report a violation can lead to disciplinary action against the Person who failed to report the violation, which may be as severe as the disciplinary action against the Person who committed the violation.

3. Normally, a possible violation of this Code by an employee other than a Principal Person should be reported to the supervisor of the employee who commits the violation. That supervisor shall inform the General Counsel and the CEO of such report. However, any employee may report any possible violation to the General Counsel. All reports of a possible violation of this Code by a Principal Person should be reported directly to the General Counsel. If a Person believes that in a particular situation it would not be appropriate to report a possible violation to his or supervisor or the General Counsel, the Person may report the possible violation to the CEO, to the Chairman of the Audit Committee of the Board of Directors, or to any other officer or director to whom the Person believes it would be appropriate to report the possible violation. The

Person may also report the possible violation as provided by the Whistleblower Policy, which is accessed in the Investor Relations section of the Company's website at www.peoplesbanknet.com.

4. The identity of the Person who reports a possible violation of this Code by another Person will be kept confidential, except to the extent that the reporting Person consents to be identified or that the identification of that reporting Person is required by law.

5. The Company shall not allow retaliation for reports of possible violations of this Code made in good faith.

6. If doubt exists as to the scope or applicability of this Code of Ethics in any particular future instance, the matter shall be reviewed in advance with the manager or supervisor who has the overall responsibility for the operation in which the question arises, or if the request comes from a Principal Person, the matter shall be reviewed in advance with the General Counsel. Any manager or supervisor receiving such a request shall refer the matter in writing to an immediate supervisor or to the General Counsel of the Company. The person making the request shall be advised what action, if any, is appropriate under the circumstances.

7. Each Principal Person shall execute this Code of Ethics annually prior to the annual meeting of shareholders of the Company.

H. Change in or Waiver of the Code of Ethics

1. Any waiver of any provision of this Code of Ethics must be approved:

   - With regard to any Principal Person, by the Board of Directors, or if a significant number of its members will be personally affected by the waiver, by a committee of the Board of Directors consisting entirely of directors who will not be personally affected by the waiver;
   - With regard to any employee who is not a Principal Person, by the CEO of the Company or any other person designated by the CEO to waive such provisions, with a report thereof provided to the Board of Directors at their next regularly scheduled meeting.

2. No waiver of any provision of this Code of Ethics with respect to a Principal Person will be effective until that waiver has been reported to the person responsible for the preparation and filing of the Company's reports on Form 8-K (or any successor to that form) in sufficient detail to enable that person to prepare a report on Form 8-K containing any required disclosure with regard to the waiver. The company will promptly disclose on Form 8-K, by means of the filing of such form, any change in or waiver of this Code of Ethics.

3. Any change in or waiver of provisions of this Code of Ethics will be reported in filings with the SEC and otherwise reported to the Company's shareholders to the full extent required by the rules of the SEC and by any applicable rules of any securities exchange or securities quotation system on which the Company's securities are listed or quoted.

I. Execution of Certificate by Persons

In my role as a Person of the Company, I certify to the Company, and to the Audit Committee of the Board of Directors of the Company, that I adhere to and advocate the above principles and responsibilities governing my professional and ethical conduct.

Date: ____

Name: ______________________________________

Signature:____________________________________

Approving Body	Date
Board of Directors	March 8, 2022
Corporate Governance & Nominating Committee	April 11, 2023
Board of Directors	May 16, 2023

EXHIBIT 31.1
Certification of Principal Executive Officer
Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, Craig L. Kauffman, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Codorus Valley Bancorp, Inc.;
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 the 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.

Date: August 7, 2023

/s/ Craig L. Kauffman
Craig L. Kauffman,
President and Chief Executive Officer
(Principal Executive Officer)

EXHIBIT 31.2
Certification of Principal Financial Officer
Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, Larry D. Pickett, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Codorus Valley Bancorp, Inc.;
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 the 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.

Date: August 7, 2023

/s/ Larry D. Pickett
Larry D. Pickett
Treasurer
(Principal Financial and Accounting Officer)

EXHIBIT 32

Certification of Principal Executive Officer and Principal Financial Officer
Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

The certification set forth below is being submitted in connection with the Quarterly Report of Codorus Valley Bancorp, Inc. (the "Company") on Form 10-Q for the period ended June 30, 2023, as filed with the Securities and Exchange Commission (the "Report"), for the purpose of complying with Rule 13a-14(b) or Rule 15d-14(b) of the Securities Exchange Act of 1934 (the “Exchange Act”) and Section 1350 of Chapter 63 of Title 18 of the United States Code.

Craig L. Kauffman, the Chief Executive Officer, and Larry D. Pickett, the Principal Financial Officer, of the Company, each certifies that, to the best of his knowledge:

1. the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act; and

2. the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: August 7, 2023

/s/ Craig L. Kauffman
Craig L. Kauffman,
President and Chief Executive Officer
(Principal Executive Officer)

/s/ Larry D. Pickett
Larry D. Pickett
Treasurer
(Principal Financial and Accounting Officer)