
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 quarterly period ended September 30, 2023

TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE EXCHANGE ACT

For the transition period from _____ to _____
Commission file number 0-14237

First United Corporation

(Exact name of registrant as specified in its charter)

Maryland	52-1380770
(State or other jurisdiction of incorporation or organization)	(I. R. S. Employer Identification No.)
19 South Second Street, Oakland, Maryland	21550-0009
(Address of principal executive offices)	(Zip Code)

(800) 470-4356
(Registrant's telephone number, including area code)

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

Title of each class	Trading Symbols	Name of each exchange on which registered
Common Stock	FUNC	Nasdaq Stock 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 periods 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 non-accelerated filer, a smaller reporting company, or an emerging growth company. See definition of "large accelerated filer", "accelerated filer", "smaller reporting company", and "emerging growth company" in Rule 12b-2 of the Exchange Act. (Check one):

Large Accelerated filer
Non-Accelerated filer
Emerging Growth Company

Accelerated Filer
Smaller Reporting 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 standard provided pursuant to Section 13(a) of the Exchange Act.

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: 6,686,222 shares of common stock, par value \$0.01 per share, as of October 31, 2023 .

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FIRST UNITED CORPORATION**

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PART I. FINANCIAL INFORMATION
Item 1. Financial Statements

First United Corporation and Subsidiaries
 Consolidated Statements of Financial Condition
 (In thousands, except share data - Unaudited)

	September 30, 2023	December 31, 2022
Assets		
Cash and due from banks	\$ 78,939	\$ 72,720
Interest bearing deposits in banks	1,713	1,595
Cash and cash equivalents	80,652	74,315
Investment securities – available for sale (at fair value)	114,370	125,889
Investment securities – held to maturity, net of allowance for credit losses of \$45 and \$0, respectively (fair value \$176,781 at September 30, 2023 and \$203,080 at December 31, 2022)	215,683	235,659
Restricted investment in bank stock, at cost	5,251	1,027
Loans held for sale	208	—
Loans	1,380,019	1,279,494
Unearned fees	(371)	(174)
Allowance for credit/loan losses	(17,146)	(14,636)
Net loans	1,362,502	1,264,684
Premises and equipment, net	32,766	34,948
Goodwill and other intangibles	12,185	12,433
Bank owned life insurance	47,282	46,346
Deferred tax assets	13,020	10,605
Other real estate owned, net	4,878	4,733
Right of use assets	1,905	1,898
Pension asset	7,476	8,001
Accrued interest receivable	6,689	6,051
Other assets	23,334	21,580
Total Assets	\$ 1,928,201	\$ 1,848,169
Liabilities and Shareholders' Equity		
Liabilities:		
Non-interest bearing deposits	\$ 429,691	\$ 506,613
Interest bearing deposits	1,145,378	1,064,120
Total deposits	1,575,069	1,570,733
Short-term borrowings	53,330	64,565
Long-term borrowings	110,929	30,929
Operating lease liability	2,347	2,373
SERP deferred compensation	7,294	7,194
Allowance for credit losses on off-balance sheet credit exposures	985	133
Accrued interest payable	578	151
Other liabilities	21,335	19,099
Dividends payable	1,344	1,199
Total Liabilities	1,773,211	1,696,376
Shareholders' Equity:		
Common Stock – par value \$0.01 per share; Authorized 25,000,000 shares; issued and outstanding 6,715,170 shares at September 30, 2023 and 6,666,428 at December 31, 2022	67	67
Surplus	25,029	24,409
Retained earnings	173,467	166,343
Accumulated other comprehensive loss	(43,573)	(39,026)
Total Shareholders' Equity	154,990	151,793
Total Liabilities and Shareholders' Equity	\$ 1,928,201	\$ 1,848,169

See accompanying notes to the consolidated financial statements

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First United Corporation and Subsidiaries
 Consolidated Statements of Operations
 (In thousands, except per share data)

	Nine Months Ended September 30,	
	2023	2022
	(Unaudited)	
Interest income		
Interest and fees on loans	\$ 50,279	\$ 39,351
Interest on investment securities		
Taxable	5,339	4,533
Exempt from federal income tax	661	834
Total investment income	6,000	5,367
Other	2,686	345
Total interest income	58,965	45,063
Interest expense		
Interest on deposits:		
Savings	189	70
Interest-bearing transaction accounts	8,912	716
Time deposits	3,599	711
Total interest on Deposits	12,700	1,497
Interest on short-term borrowings	93	86
Interest on long-term borrowings	3,496	1,027
Total Interest Expense	16,289	2,610
Net Interest income		
Credit loss expense - loans	42,676	42,453
Credit loss expense - debt securities held to maturity	1,170	97
Credit loss expense - off-balance sheet credit exposures	45	—
Total credit loss expense	(14)	12
Net interest income after provision for credit losses	1,201	109
	41,475	42,344
Other operating income		
Net gains on investments, available for sale	—	3
Net gains on investments, held to maturity	—	93
Net gains on sales of residential mortgage loans	322	31
Net gains on disposal of fixed assets	—	34
Net gains	322	161
Other Income		
Service charges on deposit accounts	1,631	1,451
Other service charges	706	686
Trust department	6,134	6,238
Debit card income	2,981	2,922
Bank owned life insurance	936	891
Brokerage commissions	800	805
Other	350	406
Total other income	13,538	13,399
Total other operating income	13,860	13,560
Other operating expenses		
Salaries and employee benefits	21,112	17,891
FDIC premiums	724	479
Equipment expense	3,168	3,110
Occupancy expense of premises	2,274	2,172
Data processing expense	2,926	2,516
Marketing expense	474	409
Professional services	1,530	873
Contract labor	471	482
Telephone	341	365
Total OREO expenses, net	281	375
Investor relations	272	258
Contributions	217	184
Other	4,144	2,425
Total other operating expenses	37,934	31,539
Income before income tax expense	17,401	24,365
Provision for income tax expense	4,099	6,286
Net Income	\$ 13,302	\$ 18,079
Basic net income per share	\$ 1.99	\$ 2.72
Diluted net income per share	\$ 1.98	\$ 2.72
Weighted average number of basic shares outstanding	6,698	6,645
Weighted average number of diluted shares outstanding	6,714	6,655
Dividends declared per common share	\$ 0.60	\$ 0.45

See accompanying notes to the consolidated financial statements

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First United Corporation and Subsidiaries
 Consolidated Statements of Operations
 (In thousands, except per share data)

	Three Months Ended	
	September 30,	
	2023	2022
	(Unaudited)	
Interest income		
Interest and fees on loans	\$ 18,055	\$ 14,058
Interest on investment securities		
Taxable	1,792	1,587
Exempt from federal income tax	123	273
Total investment income	1,915	1,860
Other	1,194	267
Total interest income	21,164	16,185
Interest expense		
Interest on deposits:		
Savings	54	34
Interest-bearing transaction accounts	3,784	397
Time deposits	1,834	190
Total interest on Deposits	5,672	621
Interest on short-term borrowings	33	47
Interest on long-term borrowings	1,475	376
Total Interest Expense	7,180	1,044
Net Interest income	13,984	15,141
Credit loss expense/(credit) - loans	322	(108)
Credit loss expense - debt securities held to maturity	45	—
Credit loss (credit)/expense - off-balance sheet credit exposures	(104)	7
Total credit loss expense/(credit)	263	(101)
Net interest income after provision for credit losses	13,721	15,242
Other operating income		
Net gains on investments, available for sale	—	—
Net gains on investments, held to maturity	—	93
Gains on sales of residential mortgage loans	182	3
Gains on disposal of fixed assets	—	—
Net gains	182	96
Other Income		
Service charges on deposit accounts	569	523
Other service charges	230	241
Trust department	2,139	2,005
Debit card income	995	1,053
Bank owned life insurance	320	302
Brokerage commissions	245	272
Other	218	208
Total other income	4,716	4,604
Total other operating income	4,898	4,700
Other operating expenses		
Salaries and employee benefits	6,957	6,130
FDIC premiums	254	150
Equipment	1,029	1,037
Occupancy	747	734
Data processing	1,011	890
Marketing	220	152
Professional services	490	(211)
Contract labor	173	159
Telephone	—	—
Telephone	115	112
Total other real estate owned expenses, net	139	128
Investor relations	83	39
Contributions	74	121
Settlement expense	—	—
FHLB prepayment penalty	—	—
Other	1,493	888
Total other operating expenses	12,785	10,329
Income before income tax expense	5,834	9,613
Provision for income tax expense	1,321	2,677
Net Income	\$ 4,513	\$ 6,936
Basic net income per common share	\$ 0.67	\$ 1.04
Diluted net income per common share	\$ 0.67	\$ 1.04
Weighted average number of basic shares outstanding	6,714	6,658
Weighted average number of diluted shares outstanding	6,728	6,669
Dividends declared per common share	\$ 0.20	\$ 0.15

First United Corporation and Subsidiaries
 Consolidated Statements of Comprehensive Income/(Loss)
 (In thousands)

	Nine Months Ended September 30,	
	2023 (Unaudited)	2022
Comprehensive Income/(Loss)		
Net Income	\$ 13,302	\$ 18,079
Other comprehensive loss, net of tax and reclassification adjustments:		
Available for sale securities:		
Unrealized holding losses on investments with credit related impairment	\$ (777)	\$ (853)
Reclassification adjustment for accretable yield realized in income	152	152
Other comprehensive loss on investments with credit related impairment	<u>(929)</u>	<u>(1,005)</u>
Unrealized holding losses on all other AFS investments	\$ (5,065)	\$ (22,971)
Unrealized holding losses on securities transferred from available for sale to held to maturity	—	8,328
Reclassification adjustment for gains realized in income	—	3
Other comprehensive loss on all other AFS investments	<u>(5,065)</u>	<u>(14,646)</u>
Held to Maturity Securities		
Unrealized holding losses on securities transferred to held to maturity	\$ —	\$ (8,328)
Unrealized holding losses on HTM investments	—	—
Reclassification adjustment for gains/(losses) realized in income	—	93
Reclassification adjustment for amortization realized in income	<u>(513)</u>	<u>(644)</u>
Other comprehensive income/(loss) on HTM investments	513	<u>(7,777)</u>
Cash flow hedges:		
Unrealized holding gains on cash flow hedges	\$ 30	\$ 1,622
Other comprehensive income on cash flow hedges	<u>30</u>	<u>1,622</u>
Pension plan liability:		
Unrealized holding gains/(losses) on pension plan liability	\$ (1,250)	\$ (14,079)
Reclassification adjustment for amortization of unrecognized loss realized in income	<u>(750)</u>	<u>(837)</u>
Other comprehensive loss on pension plan liability	<u>(500)</u>	<u>(13,242)</u>
SERP liability:		
Unrealized holding losses on SERP liability	\$ —	\$ —
Reclassification adjustment for amortization of unrealized loss realized in income	6	<u>(203)</u>
Other comprehensive (loss)/income on SERP liability	<u>(6)</u>	203
Other comprehensive losses before income tax	<u>(5,957)</u>	<u>(34,845)</u>
Income tax benefit related to other comprehensive income	1,410	9,325
Other comprehensive loss, net of tax	<u>(4,547)</u>	<u>(25,520)</u>
Comprehensive income/(loss)	<u>\$ 8,755</u>	<u>\$ (7,441)</u>

See accompanying notes to the consolidated financial statements

First United Corporation and Subsidiaries
Consolidated Statements of Comprehensive Income
(In thousands)

	Three Months Ended September 30,	
	2023 (Unaudited)	2022
Comprehensive Income/(Loss)		
Net Income	\$ 4,513	\$ 6,936
Other comprehensive loss, net of tax and reclassification adjustments:		
Available for sale securities:		
Unrealized holding gains/(losses) on investments with credit related impairment	\$ 633	\$ (199)
Reclassification adjustment for accretable yield realized in income	51	51
Other comprehensive income/(loss) on investments with credit related impairment	582	(250)
Unrealized holding loss on all other AFS investments	\$ (4,183)	\$ (6,768)
Other comprehensive loss on all other AFS investments	(4,183)	(6,768)
Held to Maturity Securities		
Unrealized holding losses on HTM investments	\$ —	\$ —
Reclassification adjustment for gains realized in income	—	93
Reclassification adjustment for amortization realized in income	(167)	(320)
Other comprehensive income on HTM investments	167	227
Cash flow hedges:		
Unrealized holding gains on cash flow hedges	\$ 14	\$ 534
Other comprehensive income on cash flow hedges	14	534
Pension plan liability:		
Unrealized holding losses on pension plan liability	\$ (1,352)	\$ (3,537)
Reclassification adjustment for amortization of unrecognized loss realized in income	(251)	(279)
Other comprehensive losses on pension plan liability	(1,101)	(3,258)
SERP liability:		
Unrealized holding losses on SERP liability	\$ —	\$ —
Reclassification adjustment for amortization of unrealized loss realized in income	2	(68)
Other comprehensive (loss)/income on SERP liability	(2)	68
Other comprehensive losses before income tax	(4,523)	(9,447)
Income tax benefit related to other comprehensive income	1,060	2,529
Other comprehensive loss, net of tax	(3,463)	(6,918)
Comprehensive income	<u>\$ 1,050</u>	<u>\$ 18</u>

First United Corporation and Subsidiaries
Consolidated Statements of Changes in Shareholders' Equity
(In thousands, except per share data)

	Common Stock	Surplus	Retained Earnings	Accumulated Other Comprehensive Loss	Total Shareholders' Equity
Balance at January 1, 2023	\$ 67	\$ 24,409	\$ 166,343	\$ (39,026)	\$ 151,793
Adoption of ASC 326- Financial Instruments- Credit Losses			(2,155)		(2,155)
Net income			4,375		4,375
Other comprehensive income				69	69
Stock based compensation		56			56
Common stock issued - 22,282 shares		64			64
Common stock dividend declared - \$0.20 per share			(1,334)		(1,334)
Balance at March 31, 2023	\$ 67	\$ 24,529	\$ 167,229	\$ (38,957)	\$ 152,868
Net income			4,414		4,414
Other comprehensive loss			(1,153)		(1,153)
Stock based compensation		298			298
Common stock issued - 18,416 shares		74			74
Common stock dividend declared - \$0.20 per share			(1,345)		(1,345)
Balance at June 30, 2023	\$ 67	\$ 24,901	\$ 170,298	\$ (40,110)	\$ 155,156
Net income			4,513		4,513
Other comprehensive loss			(3,463)		(3,463)
Stock based compensation		69			69
Common stock issued - 5,046 shares		80			80
Common stock repurchased - 1,298 share		(21)			(21)
Common stock dividend declared - \$0.20 per share			(1,344)		(1,344)
Balance at September 30, 2023	\$ 67	\$ 25,029	\$ 173,467	\$ (43,573)	\$ 154,990

First United Corporation and Subsidiaries
Consolidated Statements of Changes in Shareholders' Equity
(In thousands, except per share data)

	Common Stock	Surplus	Retained Earnings	Accumulated Other Comprehensive Loss	Total Shareholders' Equity
Balance at January 1, 2022	\$ 66	\$ 23,661	\$ 145,487	\$ (27,314)	\$ 141,900
Net income			5,715		5,715
Other comprehensive loss				(9,593)	(9,593)
Stock based compensation			(4)		(4)
Common stock issued - 15,456 shares			55		55
Common stock dividend declared - \$0.15 per share				(995)	(995)
Balance at March 31, 2022	\$ 66	\$ 23,712	\$ 150,207	\$ (36,907)	\$ 137,078
Net income			5,428		5,428
Other comprehensive loss				(9,009)	(9,009)
Stock based compensation	1	339			340
Common stock issued - 18,416 shares			54		54
Common stock dividend declared - \$0.15 per share				(999)	(999)
Balance at June 30, 2022	\$ 67	\$ 24,105	\$ 154,636	\$ (45,916)	\$ 132,892
Net income			6,936		6,936
Other comprehensive loss				(6,918)	(6,918)
Stock based compensation		80			80
Common stock issued - 4,563 shares			53		53
Common stock dividend declared- \$0.15 per share				(999)	(999)
Balance at September 30, 2022	\$ 67	\$ 24,238	\$ 160,573	\$ (52,834)	\$ 132,044

See accompanying notes to the consolidated financial statement

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First United Corporation and Subsidiaries
Consolidated Statements of Cash Flows
(In thousands)

	Nine Months Ended September 30,	
	2023	2022
	(Unaudited)	
Operating activities		
Net income	\$ 13,302	\$ 18,079
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for credit losses	1,201	109
Depreciation	2,528	2,475
Stock based compensation	423	415
Gain on sales of other real estate owned	(36)	—
Recoveries of other real estate owned, net	(55)	—
Originations of loans held for sale	(3,627)	(1,156)
Proceeds from sales of loans held for sale	3,741	1,254
Gains from sales of loans held for sale	(322)	(31)
Gains on disposal of fixed assets	—	(34)
Net (accretion)/ amortization of investment securities discounts and premiums- AFS	(32)	100
Net accretion of investment securities discounts and premiums- HTM	(618)	(625)
Amortization of intangible assets	248	157
Gains on sales/calls of investment securities – AFS	—	(3)
Gains on calls of investment securities – HTM	—	(93)
Earnings on bank owned life insurance	(936)	(891)
Amortization of deferred loan costs/(fees), net	40	(123)
Amortization of operating lease right of use asset	249	260
Increase in accrued interest receivable and other assets	(1,754)	(651)
Deferred tax expense/(benefit)	(97)	(9,322)
Operating lease liability	(282)	(289)
Increase in accrued interest payable and other liabilities	2,793	9,094
Net cash provided by operating activities	<u>16,766</u>	<u>18,725</u>
Investing activities		
Proceeds from maturities/calls of investment securities - AFS	5,320	12,153
Proceeds from maturities/calls of investment securities - HTM	24,537	13,254
Proceeds from sales of investment securities - AFS	—	1,023
Purchases of investment securities - AFS	—	(17,652)
Purchases of investment securities - HTM	(3,988)	(55,686)
Proceeds from sales of other real estate owned	172	—
Proceeds from disposal of fixed assets	—	37
Net (increase)/decrease in restricted stock	(4,224)	2
Net increase in loans	(101,320)	(124,963)
Purchases of premises and equipment	(346)	(2,803)
Net cash used in by investing activities	<u>(79,849)</u>	<u>(174,635)</u>
Financing activities		
Net increase in deposits	4,336	41,744
Issuance of common stock	218	162
Cash dividends paid on common stock	(3,878)	(2,987)
Net (decrease)/increase in short-term borrowings	(11,235)	32,027
Stock repurchase	(21)	—
Proceeds from long-term borrowings	80,000	—
Net cash provided by financing activities	<u>69,420</u>	<u>70,946</u>
Increase/(decrease) in cash and cash equivalents	6,337	(84,964)
Cash and cash equivalents at beginning of the year	74,315	115,720
Cash and cash equivalents at end of period	<u>\$ 80,652</u>	<u>\$ 30,756</u>
Supplemental information		
Interest paid	\$ 16,406	\$ 2,655
Taxes paid	\$ 4,821	\$ 5,248
Non-cash investing activities:		
Transfers from loans to other real estate owned	\$ 226	\$ 256
Transfers from securities available for sale to held to maturity	\$ —	\$ 139,036

FIRST UNITED CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

Note 1 – Basis of Presentation

The financial information is presented in accordance with generally accepted accounting principles and general practice for financial institutions in the United States of America ("GAAP"). First United Corporation has prepared these unaudited condensed consolidated financial statements in accordance with GAAP for interim financial information, rules of the Securities and Exchange Commission that permit reduced disclosure for interim periods, and Article 8 of Regulation S-X. Certain reclassifications have been made to prior year amounts to conform with current year classifications. These reclassifications did not have a material impact on the Corporation's consolidated financial condition or results of operations. Operating results for the three- and nine-month periods ended September 30, 2023, are not necessarily indicative of the results that may be expected for the full year or for any future interim period. These consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto included in First United Corporation's Annual Report on Form 10-K for the year ended December 31, 2022.

In preparing financial statements, management is required to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosure of contingent assets and liabilities as of the date of financial statements. In addition, these estimates and assumptions affect revenues and expenses in the financial statements and as such, actual results could differ from those estimates.

In the opinion of management, all adjustments (all of which are of a normal recurring nature) that are necessary for a fair statement are reflected in the unaudited condensed consolidated financial statements.

Principles of Consolidation

The consolidated financial statements include the accounts of First United Corporation, First United Bank & Trust (the "Bank"), First United Statutory Trust I, First United Statutory Trust II, OakFirst Loan Center, LLC, OakFirst Loan Center, Inc., First OREO Trust and FUBT OREO I, LLC. All significant inter-company accounts and transactions have been eliminated.

As used in these notes, the terms "the Corporation" "we", "us", and "our" refer to First United Corporation and, unless the context clearly requires otherwise, its consolidated subsidiaries.

The Corporation has evaluated events and transactions occurring subsequent to the statement of financial condition date of September 30, 2023 and through the date these consolidated financial statements were issued, for items of potential recognition or disclosure.

Newly Adopted Pronouncements in 2023

In June 2016, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2016-13, *Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*, universally referred to as CECL. The amendments in ASU, 2016-13 among other things, requires the measurement of all expected credit losses for financial assets held at the reporting date based on historical experience, current conditions, and reasonable and supportable forecasts. Financial institutions and other organizations will now use forward-looking information to better inform their credit loss estimates. Many of the loss estimation techniques applied previously are still permitted, although the inputs to those techniques changed to reflect the full amount of expected credit losses. In addition, ASU 2016-13 amends the accounting for credit losses on purchased financial assets with credit deterioration. For periodic report filers that are smaller reporting companies, such as the Corporation, ASU 2016-13 was effective as of January 1, 2023.

As part of its process of adopting the CECL accounting method, management implemented a third party software solution and determined the appropriate loan segments, methodologies, model assumptions and qualitative components. Our CECL model includes portfolio loan segmentation based upon similar risk characteristics and both a quantitative and qualitative component of the calculation which incorporates a forecasting component of certain economic variables. Our implementation plan also includes the assessment and documentation of appropriate processes, policies and internal controls. Management had a third party independent consultant review and validate our CECL model.

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In addition, ASU 2016-13 amends the accounting for credit losses on certain debt securities. The Corporation did not record any allowance for credit losses ("ACL") on its debt securities as a result of adopting this ASU.

The ultimate impact of adopting ASU 2016-13, and at each subsequent reporting period, is highly dependent on credit quality, macroeconomic forecasts and conditions, compensation of our loan portfolio, and other management judgments. The Corporation adopted ASU 2016-13 using the modified retrospective method. Results beginning after January 1, 2023 are presented under ASU 2016-13, while prior period amounts continue to be reported in accordance with previously applicable GAAP. We made the accounting policy election to not measure an ACL for accrued interest receivables for loans and securities. Accrued interest deemed uncollectible will be written off through interest income.

The following table illustrates the day-one impact of adopting ASU 2016-13.

(Dollars in thousands)	January 1, 2023		
	As Reported Under ASU 2016-13	Pre ASU 2016-13	Impact of ASU 2016- 13 Adoption
Assets			
Allowance for credit losses on loans			
Commercial real estate	\$ 5,202	\$ 6,345	\$ (1,143)
Acquisition and development	964	979	(15)
Commercial and industrial	4,179	2,845	1,334
Residential mortgage	5,272	3,160	2,112
Consumer	1,085	877	208
Unallocated	-	430	(430)
Allowance for Credit Losses on Loans	\$ 16,702	\$ 14,636	\$ 2,066
Assets:			
Investment securities- available for sale (at fair value)	\$ 125,889	\$ 125,889	\$ -
Investment securities- held to maturity	245,659	245,659	-
Total loans held for investments, net	1,262,792	1,264,858	(2,066)
Net deferred tax asset	11,381	10,605	776
Liabilities:			
Life-of-loss reserve on unfunded loan commitments	\$ 998	\$ 133	\$ 865
Equity:			
Retained earnings	\$ 149,638	\$ 151,793	\$ (2,155)

In connection with our adoption of ASU 2016-13, we made changes to our loan portfolio segments to align with the methodology of CECL. Refer to Note 5, Loans and Related Allowance for Credit Losses, for further discussion of these portfolio segments. The adoption of ASU 2016-13 resulted in a Day 1 adjustment of \$2.9 million to our ACL, including an increase of \$ 2.0 million to the ACL for loans and \$0.9 million to the ACL for unfunded commitments. The Corporation did not record any ACL on its available-for-sale or held-to-maturity investments upon adoption of ASC 326. The Corporation recorded a net decrease to retained earnings of \$2.2 million as of January 1, 2023 for the cumulative effect of adopting ASU 2016-13.

In March 2022, FASB issued ASU No. 2022-02, *Financial Instruments – Credit Losses (Topic 326): Troubled Debt Restructurings and Vintage Disclosures*. ASU 2022-02, which eliminates the troubled debt restructuring ("TDR") accounting model for creditors that have adopted ASU 2016-13. Due to the removal of the TDR accounting model, all loan modifications were evaluated to determine if they resulted in a new loan or a continuation of the existing loan. The amendments in ASU 2022-02 also required that entities disclose current-period gross charge-offs by year of origination for loans and leases. The amendments in ASU 2022-02 were effective January 1, 2023. This change did not have a material effect on our consolidated financial statements. Refer to Note 5, Loans and Related Allowance for Credit Losses for disclosures for debtors experiencing financial difficulty and for vintage disclosures related to gross charge-offs by loan segment by year of origination.

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Allowance for Credit Losses Policy

The ACL represents an amount that, in management's judgment, is adequate to absorb expected losses on outstanding loans at the balance sheet date based on the evaluation of the size and current risk characteristics of the loan portfolio, past events, current conditions, reasonable and supportable forecasts of future economic conditions and prepayment experience. The ACL is measured and recorded upon the initial recognition of a financial asset. The ACL is reduced by charge-offs, net of recoveries of previous losses, and is increased or decreased by a provision for credit losses, which is recorded as a current period operating expense.

Determination of an appropriate ACL is inherently complex and requires the use of significant and highly subjective estimates. The reasonableness is reviewed quarterly by management.

Management believes it uses relevant information available to make determinations about the ACL and that it has established the existing allowance in accordance with GAAP. However, the determination of the ACL requires significant judgment, and estimates of expected losses in the loan portfolio can vary significantly from the amounts actually observed. While management uses available information to recognize losses, future additions to the ACL may be necessary based on changes in the loans comprising the portfolio, changes in the current and forecasted economic conditions, changes to the interest rate environment which may directly impact prepayment and curtailment rate assumptions, and changes in the financial condition of borrowers.

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

The Corporation's note 5 for discussion related to the Corporation's methodology for estimating the ACL includes:

Loan Commitments and Allowance for Credit Loss on Off-Balance Sheet Credit Exposures

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

The Corporation records a reserve for unfunded commitments ("RUC") on off-balance sheet credit exposures through a charge to provision for credit loss expense in the Corporation's Consolidated Statement of Income. The RUC on off-balance sheet credit exposures is estimated by loan segment at each balance sheet date under the CECL model using the same methodologies as portfolio loans, taking into consideration the likelihood that funding will occur, and is included in the RUC on the Corporation's Consolidated Balance Sheet.

Loan Restructurings

In situations where, for economic or legal reasons related to a borrower's financial condition, management may grant a concession to the borrower that it would not otherwise consider, the related loan is classified as a restructured loan. Management strives to identify borrowers in financial difficulty early and work with them to modify the loan to more affordable terms before their loan reaches nonaccrual status. The Corporation modifies loans to borrowers in financial distress by providing principal forgiveness, term extension, an other-than-insignificant payment delay, or interest rate reductions. When principal forgiveness is provided, the amount of forgiveness is charged-off against the allowance for credit losses. These concessions are intended to minimize the economic loss and to avoid foreclosure or repossession of the collateral. See Note 5 for more detail related to the accounting of restructured loans.

Allowance for Credit Losses – Available-for-Sale and Held-to-Maturity Securities

The Corporation adopted Accounting Standards Codification ("ASC ") 326 using the prospective transition approach for debt securities for which other than temporary impairment ("OTTI") had been recognized prior to January 1, 2023, such as available-for-sale ("AFS") collateralized debt obligations. As a result, the amortized cost basis for such debt securities remained the same before and after the effective date of ASC 326. The effective interest rate on these debt securities was not changed. Amounts

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previously written off are recognized in other comprehensive income ("OCI") as of January 1, 2023 relating to improvements in cash flows expected to be collected are accreted into income over the remaining life of the asset. Recoveries of amounts previously written off relating to improvements in cash flows after January 1, 2023 are recorded in earnings when received.

See Note 5 for additional information related to investment securities and the related allowance for credit losses on the AFS and held-to-maturity ("HTM") portfolio.

Note 2 – Accounting Statements Issued but Not Yet Adopted

In March 2020, FASB issued ASU No. 2020-04, *"Reference Rate Reform (Topic 848): Facilitation of Reference Rate Reform on Financial Reporting."* The amendments in ASU 2020-04 provide optional guidance for a limited period of time to ease the potential burden in accounting for or recognizing the effects of reference rate reform on financial reporting. The amendments provide optional expedients and exceptions for applying GAAP to loan and lease agreements, derivative contracts, and other transactions affected by the anticipated transition away from the London Interbank Offered Rate ("LIBOR") toward new interest rate benchmarks. Modified contracts that meet certain scope guidance are eligible for relief from these modification accounting requirements in GAAP. The optional guidance generally allows for the modified contract to be accounted for as a continuation of the existing contract and does not require contract remeasurement at the modification date or reassessment of a previous accounting determination. The amendments in ASU 2020-04 are effective for all entities between March 12, 2020 and December 31, 2022. In December 2022, FASB issued ASU No. 2022-06: *"Reference Rate Reform (Topic 848): Deferral of the Sunset Date of Topic 848."* The amendments in ASU 2020-06 defer the sunset date for applying the reference rate reform relief by two years to December 31, 2024, after which entities will no longer be permitted to apply the relief in Topic 848.

An internal team of the Corporation was formed to transition loans held for investment away from LIBOR. As of September 30, 2023, there are no loans in our loan portfolio whose variable rate is tied to the LIBOR. The Corporation no longer offers LIBOR for any new contract as part of this transition.

The Corporation has identified all known LIBOR exposures, created a plan to address the exposures, and continues to communicate with all stakeholders to transition to alternative reference rates. The Corporation does not anticipate that the adoption of ASU 2020-04 will have a material impact on the Corporation's consolidated financial statements.

Note 3 – Earnings Per Common Share

Basic earnings per common share is derived by dividing net income available to common shareholders by the weighted-average number of common shares outstanding during the period and does not include the effect of any potentially dilutive common stock equivalents. Diluted earnings per share is derived by dividing net income available to common shareholders by the weighted-average number of shares outstanding, adjusted for the dilutive effect of outstanding common stock equivalents, such as restricted stock units ("RSUs"). There were no anti-dilutive shares outstanding at September 30, 2023 or 2022.

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The following table sets forth the calculation of basic and diluted earnings per common share for the nine- and three-month periods ended September 30, 2023 and 2022:

(in thousands, except for per share amount)	Nine months ended September 30,					
	2023			2022		
	Income	Average Shares	Per Share Amount	Income	Average Shares	Per Share Amount
Basic Earnings Per Share:						
Net income	\$ 13,302	6,698	\$ 1.99	\$ 18,079	6,645	\$ 2.72
Diluted Earnings Per Share:						
Restricted stock units		16			10	
Net income	\$ 13,302	6,714	\$ 1.98	\$ 18,079	6,655	\$ 2.72
Three months ended September 30,						
(in thousands, except for per share amount)	2023			2022		
	Income	Average Shares	Per Share Amount	Income	Average Shares	Per Share Amount
	\$ 4,513	6,714	\$ 0.67	\$ 6,936	6,658	\$ 1.04
Basic Earnings Per Share:						
Net income	\$ 4,513	6,728	\$ 0.67	\$ 6,936	6,669	\$ 1.04
Diluted Earnings Per Share:						
Restricted stock units		14			11	
Net income	\$ 4,513	6,728	\$ 0.67	\$ 6,936	6,669	\$ 1.04

Note 4 – Investments

The following tables show a comparison of amortized cost and fair values of investment securities at September 30, 2023 and December 31, 2022:

(in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Allowance for Credit Losses	Estimated Fair Value
September 30, 2023					
Available for Sale:					
U.S. government agencies	\$ 11,020	\$ —	\$ 1,660	\$ —	\$ 9,360
Residential mortgage-backed agencies	42,073	—	8,704	—	33,369
Commercial mortgage-backed agencies	36,722	—	9,667	—	27,055
Collateralized mortgage obligations	24,223	—	5,236	—	18,987
Obligations of states and political subdivisions	10,832	—	766	—	10,066
Corporate bonds	1,000	—	251	—	749
Collateralized debt obligations	18,670	—	3,886	—	14,784
Total available for sale	\$ 144,540	\$ —	\$ 30,170	\$ —	\$ 114,370

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(in thousands)	Amortized Cost	Gross Unrecognized Gains	Gross Unrecognized Losses	Estimated Fair Value	Allowance for Credit Losses
September 30, 2023					
Held to Maturity:					
U.S. treasuries	\$ 37,397	\$ —	\$ 670	\$ 36,727	\$ —
U.S. government agencies	67,944	—	14,411	53,533	—
Residential mortgage-backed agencies	30,336	—	4,495	25,841	—
Commercial mortgage-backed agencies	21,454	—	6,494	14,960	—
Collateralized mortgage obligations	53,994	—	12,114	41,880	—
Obligations of states and political subdivisions	4,603	126	844	3,885	45
Total held to maturity	\$ 215,728	\$ 126	\$ 39,028	\$ 176,826	\$ 45

(in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	OTTI in AOCL
December 31, 2022					
Available for Sale:					
U.S. government agencies	\$ 11,044	\$ —	\$ 1,582	\$ 9,462	\$ —
Residential mortgage-backed agencies	45,052	—	7,651	37,401	—
Commercial mortgage-backed agencies	37,393	—	6,661	30,732	—
Collateralized mortgage obligations	25,828	—	4,784	21,044	—
Obligations of states and political subdivisions	10,848	4	360	10,492	—
Corporate Bonds	1,000	—	113	887	—
Collateralized debt obligations	18,664	—	2,793	15,871	(1,695)
Total available for sale	\$ 149,829	\$ 4	\$ 23,944	\$ 125,889	\$ (1,695)

(in thousands)	Amortized Cost	Gross Unrecognized Gains	Gross Unrecognized Losses	Fair Value	OTTI in AOCL
December 31, 2022					
Held to Maturity:					
U.S. treasuries	\$ 37,204	\$ —	\$ 1,593	\$ 35,611	\$ —
U.S. government agencies	67,734	—	13,261	54,473	—
Residential mortgage-backed agencies	28,624	1	3,503	25,122	—
Commercial mortgage-backed agencies	22,389	—	4,568	17,821	—
Collateralized mortgage obligations	57,085	—	10,001	47,084	—
Obligations of states and political subdivisions	22,623	946	600	22,969	—
Total held to maturity	\$ 235,659	\$ 947	\$ 33,526	\$ 203,080	\$ —

The Corporation reassessed the classification of certain investments and, effective February 1, 2022, transferred \$ 139.0 million of callable agencies, obligations of state and political subdivisions, and collateralized mortgage obligations from available for sale to held to maturity securities. The transfer occurred at fair value. The related unrealized loss of \$8.4 million included in other comprehensive loss remained in other comprehensive loss, to be amortized out of other comprehensive loss with an offsetting entry to interest income as a yield adjustment over the remaining term of the securities. No gain or loss was recorded at the time of transfer.

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The following table shows the Corporation's investment securities with gross unrealized and unrecognized losses and fair values at September 30, 2023 and December 31, 2022, aggregated by investment category and the length of time that individual securities have been in a continuous unrealized loss position:

(in thousands)	Less than 12 months			12 months or more		
	Fair Value	Unrealized Losses	Number of Investments	Fair Value	Unrealized Losses	Number of Investments
September 30, 2023						
Available for Sale:						
U.S. government agencies	\$ —	\$ —	—	\$ 9,360	\$ 1,660	3
Residential mortgage-backed agencies	—	—	—	33,369	8,704	5
Commercial mortgage-backed agencies	—	—	—	27,055	9,667	8
Collateralized mortgage obligations	—	—	—	18,987	5,236	10
Obligations of states and political subdivisions	3,357	294	6	6,369	472	3
Corporate Bonds	—	—	—	749	251	1
Collateralized debt obligations	—	—	—	14,784	3,886	9
Total available for sale	<u><u>\$ 3,357</u></u>	<u><u>\$ 294</u></u>	<u><u>6</u></u>	<u><u>\$ 110,673</u></u>	<u><u>\$ 29,876</u></u>	<u><u>39</u></u>
(in thousands)	Less than 12 months			12 months or more		
	Fair Value	Unrecognized Losses	Number of Investments	Fair Value	Unrecognized Losses	Number of Investments
September 30, 2023						
Held to Maturity:						
U.S. treasuries	\$ —	\$ —	—	\$ 36,727	\$ 670	4
U.S. government agencies	—	—	—	53,533	14,411	9
Residential mortgage-backed agencies	3,977	98	3	21,864	4,397	35
Commercial mortgage-backed agencies	—	—	—	14,960	6,494	2
Collateralized mortgage obligations	—	—	—	41,880	12,114	8
Obligations of states and political subdivisions	—	—	—	2,030	844	1
Total held to maturity	<u><u>\$ 3,977</u></u>	<u><u>\$ 98</u></u>	<u><u>3</u></u>	<u><u>\$ 170,994</u></u>	<u><u>\$ 38,930</u></u>	<u><u>59</u></u>

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(in thousands)	Less than 12 months			12 months or more		
	Fair Value	Unrealized Losses	Number of Investments	Fair Value	Unrealized Losses	Number of Investments
December 31, 2022						
Available for Sale:						
U.S. government agencies	\$ 4,598	\$ 402	1	\$ 4,865	\$ 1,180	2
Residential mortgage-backed agencies	—	—	—	37,401	7,651	5
Commercial mortgage-backed agencies	4,044	455	3	26,688	6,206	6
Collateralized mortgage obligations	1,600	210	5	19,444	4,574	5
Obligations of states and political subdivisions	8,906	360	7	—	—	—
Corporate Bonds	887	113	1	—	—	—
Collateralized debt obligations	—	—	—	15,871	2,793	9
Total available for sale	\$ 20,035	\$ 1,540	17	\$ 104,269	\$ 22,404	27

(in thousands)	Less than 12 months			12 months or more		
	Fair Value	Unrecognized Losses	Number of Investments	Fair Value	Unrecognized Losses	Number of Investments
December 31, 2022						
Held to Maturity:						
U.S. treasuries	\$ —	\$ —	—	\$ 35,611	\$ 1,593	4
U.S. government agencies	38,883	9,617	7	15,591	3,644	2
Residential mortgage-backed agencies	16,893	1,425	29	8,138	2,078	7
Commercial mortgage-backed agencies	17,821	4,568	3	—	—	—
Collateralized mortgage obligations	47,083	10,001	8	—	—	—
Obligations of states and political subdivisions	2,269	600	1	—	—	—
Total held to maturity	\$ 122,949	\$ 26,211	48	\$ 59,340	\$ 7,315	13

The Corporation utilizes ASC 326 to evaluate its AFS and HTM debt security portfolio for expected credit losses. For AFS 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 criteria is met, the security's amortized cost basis is written down to fair value through income. For AFS debt securities 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 is 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 ACL is recorded for the credit loss, limited by the amount that the fair value is less than the amortized cost basis. Any impairment that has not been recorded through an ACL is recognized in other comprehensive income, as a non-credit-related impairment.

Changes in the allowance for credit losses are recorded as a provision for (or reversal of) credit losses. Losses are charged against the allowance when management believes the uncollectibility of an AFS security is confirmed or when either of the criteria regarding intent or requirement to sell is met. Any impairment not recorded through an allowance for credit loss is recognized in other comprehensive income as a non-credit-related impairment.

The Corporation has made the policy election to exclude accrued interest from the amortized cost basis of available-for-sale debt securities and report accrued interest separately in other assets in the Consolidated Balance Sheets. Available-for-sale debt

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securities are placed on nonaccrual status when we no longer expect to receive all contractual amounts due, which is generally at 90 days past due. Accrued interest receivable is reversed against interest income when a security is placed on nonaccrual status. Accordingly, we do not recognize an allowance for credit loss against accrued interest receivable.

The Corporation separately evaluates its HTM investment securities for any credit losses. The Corporation pools like securities and calculates expected credit losses through an estimate based on a security's credit rating, which is recognized as part of the allowance for credit losses for held-to-maturity securities and is included in the balance of investment securities held to maturity on the Consolidated Balance Sheets. If the Corporation determines that a security indicates evidence of deteriorated credit quality, the security is individually evaluated and a discounted cash flow analysis is performed and compared to the amortized cost basis.

As of September 30, 2023, the Corporation recorded ACL of approximately \$ 45,000 related to one bond in the HTM security portfolio. There was no ACL related to its AFS or HTM security portfolio at December 31, 2022.

The following table presents a cumulative roll-forward of the amount of non-cash credit-related impairment charges related to credit losses that have been previously recognized in earnings for the trust preferred securities held in the collateralized debt obligation ("CDO") portfolio during the nine- and three- month periods ended September 30, 2023 and 2022 that the Corporation does not intend to sell:

(in thousands)	Nine Months Ended September 30,	
	2023	2022
Balance of credit-related impairment at January 1	\$ 1,841	\$ 2,043
Reduction for increases in cash flows expected to be collected	(152)	(152)
Balance of credit-related impairment at September 30	\$ 1,689	\$ 1,891

(in thousands)	Three Months Ended September 30,	
	2023	2022
Balance of credit-related impairment at July 1	\$ 1,740	\$ 1,942
Reduction for increases in cash flows expected to be collected	(51)	(51)
Balance of credit-related impairment at September 30	\$ 1,689	\$ 1,891

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The amortized cost and estimated fair value of securities by contractual maturity at September 30, 2023 are shown in the following table. Actual maturities may differ from contractual maturities because the issuers of the securities may have the right to call or prepay obligations with or without call or prepayment penalties.

	September 30, 2023	
(in thousands)	Amortized Cost	Fair Value
Available for Sale:		
Due in one year or less		
Due in one year or less	\$ 3,010	\$ 2,953
Due after one year through five years	9,270	8,391
Due after five years through ten years	1,895	1,560
Due after ten years	27,347	22,055
	41,522	34,959
Residential mortgage-backed agencies	42,073	33,369
Commercial mortgage-backed agencies	36,722	27,055
Collateralized mortgage obligations	24,223	18,987
Total available for sale	\$ 144,540	\$ 114,370
Held to Maturity:		
Due in one year or less		
Due in one year or less	\$ 37,397	\$ 36,727
Due after one year through five years	12,500	11,306
Due after five years through ten years	38,681	30,544
Due after ten years	21,366	15,568
	109,944	94,145
Residential mortgage-backed agencies	30,336	25,841
Commercial mortgage-backed agencies	21,454	14,960
Collateralized mortgage obligations	53,994	41,880
Total held to maturity	\$ 215,728	\$ 176,826

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Note 5 – Loans and Related Allowance for Credit Losses

The following table summarizes the primary segments of the loan portfolio at September 30, 2023 and December 31, 2022:

(in thousands)	Commercial Real Estate	Acquisition and Development	Commercial and Industrial	Residential Mortgage	Consumer	Total
September 30, 2023						
Individually evaluated for impairment	\$ —	\$ —	\$ —	\$ 2,314	\$ —	\$ 2,314
Collectively evaluated for impairment	<u>491,284</u>	<u>79,796</u>	<u>254,650</u>	<u>489,372</u>	<u>62,603</u>	<u>1,377,705</u>
Total loans	<u>\$ 491,284</u>	<u>\$ 79,796</u>	<u>\$ 254,650</u>	<u>\$ 491,686</u>	<u>\$ 62,603</u>	<u>\$ 1,380,019</u>
December 31, 2022						
Individually evaluated for impairment	\$ 2,262	\$ 356	\$ —	\$ 3,880	\$ —	\$ 6,498
Collectively evaluated for impairment	<u>456,569</u>	<u>70,240</u>	<u>245,396</u>	<u>440,531</u>	<u>60,260</u>	<u>1,272,996</u>
Total loans	<u>\$ 458,831</u>	<u>\$ 70,596</u>	<u>\$ 245,396</u>	<u>\$ 444,411</u>	<u>\$ 60,260</u>	<u>\$ 1,279,494</u>

The following table presents the classes of the loan portfolio summarized by the aging categories of performing loans and non-accrual loans at September 30, 2023 and December 31, 2022:

(in thousands)	Current	30-59 Days Past Due	60-89 Days Past Due	90 Days+ Past Due	Total Past Due and Accruing	Non-Accrual	Total Loans
September 30, 2023							
Commercial real estate:							
Non-owner-occupied	\$ 293,932	\$ —	\$ 229	\$ —	\$ 229	\$ —	\$ 294,161
All other CRE	<u>196,524</u>	<u>599</u>	<u>—</u>	<u>—</u>	<u>599</u>	<u>—</u>	<u>197,123</u>
Acquisition and development:							
1-4 family residential construction	17,527	—	—	—	—	—	17,527
All other A&D	62,149	—	—	—	—	120	62,269
Commercial and industrial	254,193	75	382	—	457	—	254,650
Residential mortgage:							
Residential mortgage - term	425,383	214	1,109	—	1,323	3,011	429,717
Residential mortgage - home equity	61,299	288	22	86	396	274	61,969
Consumer	61,786	541	143	59	743	74	62,603
Total	<u>\$ 1,372,793</u>	<u>\$ 1,717</u>	<u>\$ 1,885</u>	<u>\$ 145</u>	<u>\$ 3,747</u>	<u>\$ 3,479</u>	<u>\$ 1,380,019</u>
December 31, 2022							
Commercial real estate:							
Non-owner-occupied	\$ 269,971	\$ —	\$ —	\$ —	\$ —	87	\$ 270,058
All other CRE	<u>188,715</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>58</u>	<u>188,773</u>
Acquisition and development:							
1-4 family residential construction	19,637	—	—	—	—	—	19,637
All other A&D	50,813	—	—	—	—	146	50,959
Commercial and industrial	245,342	54	—	—	54	—	245,396
Residential mortgage:							
Residential mortgage - term	380,502	31	722	239	992	2,893	384,387
Residential mortgage - home equity	59,223	399	48	43	490	311	60,024
Consumer	59,789	363	83	25	471	—	60,260
Total	<u>\$ 1,273,992</u>	<u>\$ 847</u>	<u>\$ 853</u>	<u>\$ 307</u>	<u>\$ 2,007</u>	<u>\$ 3,495</u>	<u>\$ 1,279,494</u>

Non-accrual loans that have been subject to partial charge-offs totaled \$ 0.1 million at September 30, 2023 and \$ 0.1 million at December 31, 2022. Loans secured by 1-4 family residential real estate properties in the process of foreclosure totaled \$1.8

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million at September 30, 2023. There were no loans in the process of foreclosure at December 31, 2022. As a percentage of the loan portfolio, accruing loans past due 30 days or more was 0.27% at September 30, 2023 compared to 0.16% at December 31, 2022.

Effective January 1, 2023, the Corporation adopted the accounting guidance in ASU 2022-02, which eliminated the recognition and measurement of TDRs. Due to the removal of the TDR designation, the Corporation evaluates all loan restructurings according to the accounting guidance for loan modifications to determine if the restructuring results in a new loan or a continuation of the existing loan. Loan modifications to borrowers experiencing financial difficulty that result in a direct change in the timing or amount of contractual cash flows include situations where there is principal forgiveness, interest rate reductions, other-than-insignificant payment delays, term extensions, and combinations of the above. Therefore, the disclosures related to loan restructurings are only for modifications that directly affect cash flows.

A loan that is considered a non-accrual or restructured loan may be subject to the individually evaluated loan analysis if the commitment is \$0.1 million or greater; otherwise, the restructured loan remains in the appropriate segment in the ACL model and associated reserves are adjusted based on changes in the discounted cash flows resulting from the modification of the restructured loan. For a discussion with respect to reserve calculations regarding individually evaluated loans, refer to the "Nonrecurring Loans" section in Note 6, Fair Value Measurements. There were no loan modifications made to borrowers facing financial difficulties in the three- or nine-month period ending September 30, 2023.

The Corporation maintains an ACL at a level determined to be adequate to absorb expected credit losses associated with the Corporation's financial instruments over the life of those instruments as of the balance sheet date. The Corporation develops and documents a systematic ACL methodology based on the following portfolio segments: (i) commercial real estate, (ii) acquisition and development, (iii) commercial and industrial, (iv) residential mortgage, and (v) consumer. The Corporation's loan portfolio is segmented by homogeneous loan types that behave similarly to economic cycles. The segmentation in the CECL model is different from the segmentation in the Incurred Loss model. The following is a discussion of the key risks by portfolio segment that management assesses in preparing the ACL.

Commercial Real Estate- loans are secured by commercial purpose real estate, including both owner occupied properties and properties obtained for investment purposes, such as hotels, strip malls and apartments. Operations of the individual projects as well as global cash flows of the debtors are the primary source of repayment of these loans. The condition of the local economy is an important indicator of risk, but there are more specific risks depending on the collateral type as well as the business.

Acquisition and Development- loans include both commercial and consumer. Commercial loans are made to finance construction of buildings or other structures, as well as to finance the acquisition and development of raw land for various purposes. While the risk of these loans is generally confined to the construction period, if there are problems, the project may not be completed, and as such, may not provide sufficient cash flow on its own to service the debt or have sufficient value in a liquidation to cover the outstanding principal. The condition of the local economy is an important indicator of risk, but there are also more specific risks depending on the type of project and the experience and resources of the developer. Consumer loans are made for the construction of residential homes for which a binding sales contract exists and generally are for a period of time sufficient to complete construction. Residential construction loans to individuals generally provide for the payment of interest only during the construction phase. Credit risk for residential real estate construction loans can arise from construction delays, cost overruns, failure of the contractor to complete the project to specifications and economic conditions that could impact demand for supply of the property being constructed.

Commercial and Industrial- loans are made to operating companies or manufacturers for the purpose of production, operating capacity, accounts receivable, inventory or equipment financing. Cash flow from the operations of the borrower is the primary source of repayment for these loans. The condition of the local economy is an important indicator of risk, but there are also more specific risks depending on the industry of the borrower. Collateral for these types of loans often do not have sufficient value in a distressed or liquidation scenario to satisfy the outstanding debt. These loans are also made to local municipalities for various purposes including refinancing existing obligations, infrastructure up-fit and expansion, or to purchase new equipment. The primary repayment source for local municipalities include the tax base of the municipality, specific revenue streams related to the infrastructure financed, and other business operations of the municipal authority. The health and stability of state and local economies directly impacts each municipality's tax basis and are important indicators of risk for this segment. The ability of each

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municipality to increase taxes and fees to offset service requirements give this type of loan a very low risk profile in the continuum of the Corporation's loan portfolio.

Residential mortgage- loans are secured by first and second liens such as home equity lines of credit and 1-4 family residential mortgages. The primary source of repayment for these loans is the income of the borrower. The condition of the local economy, in particular the unemployment rate, is an important indicator of risk for this segment. The state of the local housing market can also have a significant impact on this segment because low demand and/or declining home values can limit the ability of borrowers to sell a property and satisfy debt.

Consumer- loans are made to individuals and may be either secured by assets other than 1-4 family residences or unsecured. This segment includes automobile loans and unsecured loans and lines of credit. The primary source of repayment for these loans is the income and assets of the borrower. The condition of the local economy, in particular the unemployment rate, is an important indicator of risk for this segment. The value of the collateral, if there is any, is less likely to be a source of repayment due to less certain collateral values.

The following table summarizes the primary segments of the ACL at September 30, 2023 and allowance for loan loss ("ALL") at December 31, 2022, segregated by the amount required for loans individually evaluated for impairment and the amount required for loans collectively evaluated for impairment:

(in thousands)	Commercial Real Estate	Acquisition and Development	Commercial and Industrial	Residential Mortgage	Consumer	Unallocated	Total
September 30, 2023							
Individually evaluated for impairment	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —
Collectively evaluated for impairment	5,038	1,065	3,477	6,642	924	—	17,146
Total ACL	\$ 5,038	\$ 1,065	\$ 3,477	\$ 6,642	\$ 924	\$ —	\$ 17,146
December 31, 2022							
Individually evaluated for impairment	\$ —	\$ —	\$ —	\$ 26	\$ —	\$ —	\$ 26
Collectively evaluated for impairment	6,345	979	2,845	3,134	877	430	14,610
Total ALL	\$ 6,345	\$ 979	\$ 2,845	\$ 3,160	\$ 877	\$ 430	\$ 14,636

Changes in the fair value of the types of collateral for individually evaluated loans are reported as provision for credit loss in the period of change. The evaluation of the need and amount of a specific allocation of the ACL and whether a loan can be removed from impairment status is made on a quarterly basis.

The following table presents the amortized cost basis of collateral-dependent individually evaluated loans as of September 30, 2023.

(dollars in thousands)	September 30, 2023	
	Real Estate	Non-Accrual Loans with No Allowance
Residential mortgage	\$ 2,314	\$ 2,314
Total Loans	\$ 2,314	\$ 2,314

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The following table presents impaired loans by class, segregated by those for which a specific allowance was required and those for which a specific allowance was not required at September 30, 2023 and December 31, 2022:

(in thousands)	Impaired Loans with Specific Allowance		Impaired Loans with No Specific Allowance	Total Impaired Loans	
	Recorded Investment	Related Allowances	Recorded Investment	Recorded Investment (1)	Unpaid Principal Balance
September 30, 2023					
Commercial real estate					
Non-owner-occupied	\$ —	\$ —	\$ —	\$ —	\$ —
All other CRE	—	—	—	—	—
Acquisition and development					
1-4 family residential construction	—	—	—	—	—
All other A&D	—	—	—	—	—
Commercial and industrial	—	—	—	—	—
Residential mortgage					
Residential mortgage – term	—	—	2,314	2,314	—
Residential mortgage – home equity	—	—	—	—	—
Consumer	—	—	—	—	—
Total impaired loans	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 2,314</u>	<u>\$ 2,314</u>	<u>\$ —</u>
December 31, 2022					
Commercial real estate					
Non-owner-occupied	\$ —	\$ —	\$ 187	\$ 187	\$ —
All other CRE	—	—	2,075	2,075	—
Acquisition and development					
1-4 family residential construction	—	—	210	210	—
All other A&D	—	—	146	146	109
Commercial and industrial	—	—	—	—	—
Residential mortgage					
Residential mortgage – term	345	26	3,225	3,570	41
Residential mortgage – home equity	—	—	310	310	—
Consumer	—	—	—	—	—
Total impaired loans	<u>\$ 345</u>	<u>\$ 26</u>	<u>\$ 6,153</u>	<u>\$ 6,498</u>	<u>\$ 150</u>

(1) Recorded investment consists of unpaid principal balance, net of charge-offs, interest payments received applied to principal and unamortized deferred loan origination fees and cost.

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The following tables present the activity in the ACL and ALL for the nine- and three-month periods ended September 30, 2023 and 2022:

Nine months ended (in thousands)	Commercial Real Estate	Acquisition and Development	Commercial and Industrial	Residential Mortgage	Consumer	Unallocated	Total
Beginning balance at January 1, 2023 prior to adoption of ASC 326	\$ 6,345	\$ 979	\$ 2,845	\$ 3,160	\$ 877	\$ 430	\$ 14,636
Impact of adopting ASC 326	(1,143)	(15)	1,334	2,112	208	(430)	2,066
Loan charge-offs	(87)	—	(301)	(55)	(681)	—	(1,124)
Recoveries collected	5	8	176	56	153	—	398
Credit loss (credit)/expense	(82)	93	(577)	1,369	367	—	1,170
ACL balance at September 30, 2023	\$ 5,038	\$ 1,065	\$ 3,477	\$ 6,642	\$ 924	\$ —	\$ 17,146
ALL balance at January 1, 2022	\$ 6,032	\$ 2,615	\$ 2,460	\$ 3,484	\$ 934	\$ 430	\$ 15,955
Loan Charge-offs	—	(20)	(134)	(34)	(726)	—	(914)
Recoveries collected	1	21	92	172	117	—	403
Loan loss expense/(credit)	323	(1,117)	984	(645)	552	—	97
ALL balance at September 30, 2022	\$ 6,356	\$ 1,499	\$ 3,402	\$ 2,977	\$ 877	\$ 430	\$ 15,541

Three months ended (in thousands)	Commercial Real Estate	Acquisition and Development	Commercial and Industrial	Residential Mortgage	Consumer	Unallocated	Total
ACL balance at July 1, 2023	\$ 4,946	\$ 1,134	\$ 3,549	\$ 6,417	\$ 859	\$ —	\$ 16,905
Loan charge-offs	—	—	(135)	(31)	(163)	—	(329)
Recoveries collected	—	1	167	20	60	—	248
Credit loss expense/(credit)	92	(70)	(104)	236	168	—	322
ACL balance at September 30, 2023	\$ 5,038	\$ 1,065	\$ 3,477	\$ 6,642	\$ 924	\$ —	\$ 17,146
ALL balance at July 1, 2022	\$ 6,220	\$ 2,172	\$ 2,830	\$ 3,112	\$ 973	\$ 430	\$ 15,737
Charge-offs	—	(20)	(82)	(1)	(181)	—	(284)
Recoveries	—	1	83	71	41	—	196
Loan loss expense/(credit)	136	(654)	571	(205)	44	—	(108)
ALL balance at September 30, 2022	\$ 6,356	\$ 1,499	\$ 3,402	\$ 2,977	\$ 877	\$ 430	\$ 15,541

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The Corporation's methodology for estimating the ACL includes:

Segmentation. The Corporation's loan portfolio is segmented by homogeneous loan types that behave similarly to economic cycles.

Specific Analysis. A specific reserve analysis is applied to certain individually evaluated loans. These loans are evaluated quarterly generally based on collateral value, observable market value or the present value of expected future cash flows. A specific reserve is established if the fair value is less than the loan balance. A charge-off is recognized when the loss is quantifiable. Individually evaluated loans not specifically analyzed reside in the Quantitative Analysis.

Quantitative Analysis. The Corporation elected to use discounted cash flows. Economic forecasts include but are not limited to unemployment, the Consumer Price Index, the Housing Affordability Index, and Gross State Product. These forecasts are assumed to revert to the long term average and are utilized in the model to estimate the probability of default and the loss given default is the estimated loss rate, which varies over time. The estimated loss rate is applied within the appropriate periods in the cash flow model to determine the net present value. Net present value is also impacted by assumption related to the duration between default and recovery. The reserve is based on the difference between the summation of the principal balances taking amortized costs into consideration and the summation of the net present values.

Qualitative Analysis. Based on management's review and analysis of internal, external and model risks, management may adjust the model output. Management reviews the peaks and troughs of the model's calibrations, taking into account economic forecasts to develop guardrails that serve as the basis for determining the reasonableness of the model's output and makes adjustments as necessary. This process challenges unexpected variability resulting from outputs beyond the model's calibrations that appear to be unreasonable. Management also enhances the calculation through the use of Moody's economic forecast data in its calculation. Additionally, management may adjust the economic forecast if it is incompatible with known market conditions based on management's experience and perspective.

The ACL is based on estimates, and actual losses may vary from current estimates. Management believes that the granularity of the homogeneous pools and the related historical loss ratios and other qualitative factors, as well as the consistency in the application of assumptions, result in an ACL that is representative of the risk found in the components of the portfolio at any given date.

Credit Quality Indicators:

The Corporation's portfolio grading analysis estimates the capability of the borrower to repay the contractual obligations of the loan agreements as scheduled or at all. The Corporation's internal credit risk grading system is based on debt service coverage, collateral values and other subjective factors. Mortgage and consumer loans are defaulted to pass grade until a loan migrates to past due status.

The Corporation has a loan review policy and annual scope report that details the level of loan review for loans in a given year. The annual loan review provides the Credit Risk Committee with an independent analysis of the following: (i) credit quality of the loan portfolio, (ii) compliance with loan policy, (iii) adequacy of documentation in credit files and (iv) validity of risk ratings.

The Corporation's internally assigned grades are as follows:

Pass- The Corporation uses six grades of pass, including its watch rating. Generally, a pass rating indicates that the loan is currently performing and is of high quality.

Special Mention- Assets with potential weaknesses that warrant management's close attention and if left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the asset or in the institution's credit position at some future date.

Substandard- Assets that are inadequately protected by the current sound worth and paying capacity of the obligor or by the collateral pledged, if any. Assets so classified have a well-defined weakness, or weaknesses that jeopardize the liquidation of

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the debt. Such assets are characterized by the distinct possibility that the institution will sustain some loss if the deficiencies are not corrected.

Doubtful- Assets with all weaknesses inherent in one classified substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently known facts, conditions, and values, highly questionable and improbable.

Loss- Assets considered of such little value that its continuance on the books is not warranted. This classification does not mean that the asset has absolutely no recovery or salvage value, but rather it is not practical to defer writing off this basically worthless asset even though partial recovery may be affected in the future.

The ability of borrowers to repay commercial loans is dependent upon the success of their business and general economic conditions. Due to the greater potential for loss within our commercial portfolio, we monitor the commercial loan portfolio through an internal risk rating system. Loan risk ratings are assigned based upon the creditworthiness of the borrower and are reviewed on an ongoing basis according to our internal policies. Loans rated special mention or substandard have potential or well-defined weaknesses not generally found in high quality, performing loans, and require attention from management to limit loss.

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The following table presents loan balances by year of origination and internally assigned risk rating for our portfolio segments as of dates presented:

(in thousands)	2023	2022	2021	2020	2019	2018 and Prior	Revolving	Total Portfolio Loans
September 30, 2023								
Commercial real estate:								
Non-owner-occupied								
Pass	\$ 20,580	\$ 66,381	\$ 30,726	\$ 54,643	\$ 39,758	\$ 63,496	\$ 1,111	\$ 276,695
Special Mention	—	—	—	—	—	6,098	—	6,098
Substandard	—	—	—	—	—	11,368	—	11,368
Total non-owner occupied	20,580	66,381	30,726	54,643	39,758	80,962	1,111	294,161
Current period gross charge-offs	—	—	—	—	—	87	—	87
All other CRE								
Pass	21,848	27,791	25,848	22,666	24,603	65,306	4,057	192,119
Special Mention	—	—	—	—	—	—	1,095	1,095
Substandard	—	—	—	—	1,871	1,438	600	3,909
Total all other CRE	21,848	27,791	25,848	22,666	26,474	66,744	5,752	197,123
Current period gross charge-offs	—	—	—	—	—	—	—	—
Acquisition and development:								
1-4 family residential construction								
Pass	7,716	9,311	—	—	—	—	500	17,527
Special Mention	—	—	—	—	—	—	—	—
Substandard	—	—	—	—	—	—	—	—
Total acquisition and development	7,716	9,311	—	—	—	—	500	17,527
Current period gross charge-offs	—	—	—	—	—	—	—	—
All other A&D								
Pass	14,592	23,197	3,994	3,101	2,512	10,631	4,122	62,149
Special Mention	—	—	—	—	—	—	—	—
Substandard	—	—	—	—	—	120	—	120
Total all other A&D	14,592	23,197	3,994	3,101	2,512	10,751	4,122	62,269
Current period gross charge-offs	—	—	—	—	—	—	—	—
Commercial and industrial:								
Pass	28,861	71,185	25,176	12,868	9,915	12,253	71,371	231,629
Special Mention	—	—	—	—	—	329	562	891
Substandard	—	8,923	2,022	6,885	117	842	3,341	22,130
Total commercial and industrial	28,861	80,108	27,198	19,753	10,032	13,424	75,274	254,650
Current period gross charge-offs	100	—	35	166	—	—	—	301
Residential mortgage:								
Residential mortgage - term								
Pass	43,211	87,386	91,415	40,083	25,855	132,866	1,723	422,539
Special Mention	—	—	—	—	—	—	—	—
Substandard	—	—	—	—	—	7,120	58	7,178
Total residential mortgage - term	43,211	87,386	91,415	40,083	25,855	139,986	1,781	429,717
Current period gross charge-offs	—	—	—	—	—	13	—	13
Residential mortgage - home equity								
Pass	1,194	5,131	887	490	296	523	52,821	61,342
Special Mention	—	—	—	—	—	—	—	—
Substandard	—	—	—	40	—	17	570	627
Total residential mortgage - home equity	1,194	5,131	887	530	296	540	53,391	61,969
Current period gross charge-offs	—	—	—	—	—	42	—	42
Consumer:								
Pass	15,997	11,773	7,254	2,503	718	21,278	2,807	62,330
Special Mention	—	—	—	—	—	—	—	—
Substandard	48	35	139	25	7	7	12	273
Total consumer	16,045	11,808	7,393	2,528	725	21,285	2,819	62,603
Current period gross charge-offs	158	184	55	3	—	281	—	681
Total Portfolio Loans								
Pass	153,999	302,155	185,300	136,354	103,657	306,353	138,512	1,326,330
Special Mention	—	—	—	—	—	6,427	1,657	8,084
Substandard	48	8,958	2,161	6,950	1,995	20,912	4,581	45,605
Total Portfolio Loans	\$ 154,047	\$ 311,113	\$ 187,461	\$ 143,304	\$ 105,652	\$ 333,692	\$ 144,750	\$ 1,380,019
Current YTD Period:								
Current period gross charge-offs	\$ 258	\$ 184	\$ 90	\$ 169	\$ —	\$ 423	\$ —	\$ 1,124

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(in thousands)	2022	2021	2020	2019	2018	2017 and Prior	Revolving	Total Portfolio Loans
December 31, 2022								
Commercial real estate:								
Non-owner-occupied								
Pass	\$ 67,429	\$ 31,710	\$ 48,421	\$ 41,221	\$ 19,414	\$ 42,069	\$ 1,570	\$ 251,834
Special Mention	—	—	—	—	—	6,289	—	6,289
Substandard	—	—	—	—	—	11,935	—	11,935
Total non-owner occupied	67,429	31,710	48,421	41,221	19,414	60,293	1,570	270,058
Current period gross charge-offs	—	—	—	—	—	—	—	—
All other CRE								
Pass	24,655	26,947	22,906	27,213	8,873	67,691	4,790	183,075
Special Mention	—	1,111	—	—	—	—	—	1,111
Substandard	—	—	—	3,006	—	357	1,224	4,587
Total all other CRE	24,655	28,058	22,906	30,219	8,873	68,048	6,014	188,773
Current period gross charge-offs	—	—	—	—	—	—	—	—
Acquisition and development:								
1-4 family residential construction								
Pass	15,629	1,453	151	—	—	210	2,194	19,637
Special Mention	—	—	—	—	—	—	—	—
Substandard	—	—	—	—	—	—	—	—
Total acquisition and development	15,629	1,453	151	—	—	210	2,194	19,637
Current period gross charge-offs	—	—	—	—	—	20	—	20
All other A&D								
Pass	18,733	4,979	9,755	1,408	558	12,961	2,419	50,813
Special Mention	—	—	—	—	—	—	—	—
Substandard	—	—	—	—	—	146	—	146
Total all other A&D	18,733	4,979	9,755	1,408	558	13,107	2,419	50,959
Commercial and industrial:								
Pass	83,608	30,451	15,982	12,707	5,013	9,528	63,668	220,957
Special Mention	—	2,555	—	—	—	338	2,134	5,027
Substandard	8,923	—	7,167	173	634	311	2,204	19,412
Total commercial and industrial	92,531	33,006	23,149	12,880	5,647	10,177	68,006	245,396
Current period gross charge-offs	—	—	—	—	—	—	—	134
Residential mortgage:								
Residential mortgage - term								
Pass	64,930	93,665	42,784	27,120	14,132	133,397	2,306	378,334
Special Mention	—	—	—	—	—	—	—	—
Substandard	—	—	16	237	143	5,634	23	6,053
Total residential mortgage - term	64,930	93,665	42,800	27,357	14,275	139,031	2,329	384,387
Current period gross charge-offs	—	—	—	—	—	28	—	28
Residential mortgage - home equity								
Pass	5,739	957	538	328	97	478	51,232	59,369
Special Mention	—	—	—	—	—	—	—	—
Substandard	—	—	44	—	21	40	550	655
Total residential mortgage - home equity	5,739	957	582	328	118	518	51,782	60,024
Current period gross charge-offs	—	—	—	—	12	6	—	18
Consumer:								
Pass	16,748	10,495	3,845	1,596	687	24,096	2,654	60,121
Special Mention	—	—	—	—	—	—	—	—
Substandard	—	92	27	9	7	—	4	139
Total consumer	16,748	10,587	3,872	1,605	694	24,096	2,658	60,260
Current period gross charge-offs	36	494	18	37	11	40	—	636
Total Portfolio Loans								
Pass	297,471	200,657	144,382	111,593	48,774	290,430	130,833	1,224,140
Special Mention	—	3,666	—	—	—	6,627	2,134	12,427
Substandard	8,923	92	7,254	3,425	805	18,423	4,005	42,927
Total Portfolio Loans	\$ 306,394	\$ 204,415	\$ 151,636	\$ 115,018	\$ 49,579	\$ 315,480	\$ 136,972	\$ 1,279,494
Current YTD Period:								
Current period gross charge-offs	\$ 36	\$ 591	\$ 52	\$ 40	\$ 23	\$ 94	\$ —	\$ 836

Management further monitors the performance and credit quality of the loan portfolio by analyzing the age of the portfolio as determined by the length of time a recorded payment is past.

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The following tables present loan balances by year of origination segregated by performing and non-performing loans for the periods presented:

(in thousands)	2023	2022	2021	2020	2019	2018 and Prior	Revolving	Total Portfolio Loans
September 30, 2023								
Commercial real estate:								
Non-owner-occupied								
Performing	\$ 20,580	\$ 66,381	\$ 30,726	\$ 54,643	\$ 39,758	\$ 80,962	\$ 1,111	\$ 294,161
Nonperforming	—	—	—	—	—	—	—	—
Total non-owner occupied	20,580	66,381	30,726	54,643	39,758	80,962	1,111	294,161
All other CRE								
Performing	21,848	27,791	25,848	22,666	26,474	66,744	5,752	197,123
Nonperforming	—	—	—	—	—	—	—	—
Total all other CRE	21,848	27,791	25,848	22,666	26,474	66,744	5,752	197,123
Acquisition and development:								
1-4 family residential construction								
Performing	7,716	9,311	—	—	—	—	500	17,527
Nonperforming	—	—	—	—	—	—	—	—
Total acquisition and development	7,716	9,311	—	—	—	—	500	17,527
All other A&D								
Performing	14,592	23,197	3,994	3,101	2,512	10,631	4,122	62,149
Nonperforming	—	—	—	—	—	120	—	120
Total all other A&D	14,592	23,197	3,994	3,101	2,512	10,751	4,122	62,269
Commercial and industrial:								
Performing	28,861	80,108	27,198	19,753	10,032	13,424	75,274	254,650
Nonperforming	—	—	—	—	—	—	—	—
Total commercial and industrial	28,861	80,108	27,198	19,753	10,032	13,424	75,274	254,650
Residential mortgage:								
Residential mortgage - term								
Performing	43,211	87,386	91,415	40,083	25,755	137,107	1,749	426,706
Nonperforming	—	—	—	—	100	2,879	32	3,011
Total residential mortgage - term	43,211	87,386	91,415	40,083	25,855	139,986	1,781	429,717
Residential mortgage - home equity								
Performing	1,194	5,131	887	490	296	524	53,087	61,609
Nonperforming	—	—	—	40	—	16	304	360
Total residential mortgage - home equity	1,194	5,131	887	530	296	540	53,391	61,969
Consumer:								
Performing	16,045	11,793	7,384	2,504	725	21,200	2,819	62,470
Nonperforming	—	15	9	24	—	85	—	133
Total consumer	16,045	11,808	7,393	2,528	725	21,285	2,819	62,603
Total Portfolio Loans								
Performing	154,047	311,098	187,452	143,240	105,552	330,592	144,414	1,376,395
Nonperforming	—	15	9	64	100	3,100	336	3,624
Total Portfolio Loans	\$ 154,047	\$ 311,113	\$ 187,461	\$ 143,304	\$ 105,652	\$ 333,692	\$ 144,750	\$ 1,380,019

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(in thousands)	2022	2021	2020	2019	2018	2017 and Prior	Revolving	Total Portfolio Loans
December 31, 2022								
Commercial real estate:								
Non-owner-occupied								
Performing	\$ 67,429	\$ 31,710	\$ 48,421	\$ 41,221	\$ 19,414	\$ 60,206	\$ 1,570	\$ 269,971
Nonperforming	—	—	—	—	—	87	—	87
Total non-owner occupied	67,429	31,710	48,421	41,221	19,414	60,293	1,570	270,058
All other CRE								
Performing	24,655	28,058	22,906	30,219	8,873	67,990	6,014	188,715
Nonperforming	—	—	—	—	—	58	—	58
Total all other CRE	24,655	28,058	22,906	30,219	8,873	68,048	6,014	188,773
Acquisition and development:								
1-4 family residential construction								
Performing	15,629	1,453	151	—	—	210	2,194	19,637
Nonperforming	—	—	—	—	—	—	—	—
Total acquisition and development	15,629	1,453	151	—	—	210	2,194	19,637
All other A&D								
Performing	18,733	4,979	9,755	1,408	558	12,962	2,419	50,814
Nonperforming	—	—	—	—	—	145	—	145
Total all other A&D	18,733	4,979	9,755	1,408	558	13,107	2,419	50,959
Commercial and industrial:								
Performing								
Performing	92,531	33,006	23,149	12,880	5,647	10,177	68,006	245,396
Nonperforming	—	—	—	—	—	—	—	—
Total commercial and industrial	92,531	33,006	23,149	12,880	5,647	10,177	68,006	245,396
Residential mortgage:								
Residential mortgage - term								
Performing	64,930	93,665	42,800	27,120	14,198	136,228	2,313	381,254
Nonperforming	—	—	—	237	77	2,803	16	3,133
Total residential mortgage - term	64,930	93,665	42,800	27,357	14,275	139,031	2,329	384,387
Residential mortgage - home equity								
Performing	5,739	957	538	328	115	478	51,515	59,670
Nonperforming	—	—	44	—	3	40	267	354
Total residential mortgage - home equity	5,739	957	582	328	118	518	51,782	60,024
Consumer:								
Performing								
Performing	16,748	10,581	3,872	1,605	694	24,077	2,658	60,235
Nonperforming	—	6	—	—	—	19	—	25
Total consumer	16,748	10,587	3,872	1,605	694	24,096	2,658	60,260
Total Portfolio Loans								
Performing	306,394	204,409	151,592	114,781	49,499	312,328	136,689	1,275,692
Nonperforming	—	6	44	237	80	3,152	283	3,802
Total Portfolio Loans	\$ 306,394	\$ 204,415	\$ 151,636	\$ 115,018	\$ 49,579	\$ 315,480	\$ 136,972	\$ 1,279,494

Note 6 – Fair Value of Financial Instruments

The Corporation complies with the guidance of ASC Topic 820, *Fair Value Measurements and Disclosures*, which defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements required under other accounting pronouncements. The Corporation also follows the guidance on matters relating to all financial instruments found in ASC Subtopic 825-10, *Financial Instruments – Overall*.

Fair value is defined as the price to sell an asset or to transfer a liability in an orderly transaction between willing market participants as of the measurement date. Fair value is best determined by values quoted through active trading markets. Active trading markets are characterized by numerous transactions of similar financial instruments between willing buyers and willing sellers. Because no active trading market exists for various types of financial instruments, many of the fair values disclosed were derived using present value discounted cash flows or other valuation techniques described below. As a result, the Corporation's ability to actually realize these derived values cannot be assumed.

The Corporation measures fair values based on the fair value hierarchy established in ASC Paragraph 820-10-35-37. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of inputs that may be used to measure fair value under the hierarchy are as follows:

Level 1: Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets and liabilities. This level is the most reliable source of valuation.

Level 2: Quoted prices that are not active, or inputs that are observable either directly or indirectly, for substantially the full term of the asset or liability. Level 2 inputs include inputs other than quoted prices that are observable for the asset or liability (for example, interest rates and yield curves at commonly quoted intervals, volatilities, prepayment speeds, loss severities, credit risks, and default rates). It also includes inputs that are derived principally from or corroborated by observable market data by correlation or other means (market-corroborated inputs). Several sources are utilized for valuing these assets, including a contracted valuation service, Standard & Poor's ("S&P") evaluations and pricing services, and other valuation matrices.

Level 3: Prices or valuation techniques that require inputs that are both significant to the valuation assumptions and not readily observable in the market (i.e. supported with little or no market activity). Level 3 instruments are valued based on the best available data, some of which is internally developed, and consider risk premiums that a market participant would require.

The level established within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement. Transfers in and out of Level 1, 2 or 3 are recorded at fair value at the beginning of the reporting period.

Investments – The investment portfolio is classified and accounted for based on the guidance of ASC Topic 320, *Investments – Debt and Equity Securities*.

The fair value of investments is determined using a market approach. As of September 30, 2023, the U.S. Government agencies and treasuries, residential and commercial mortgage-backed securities, collateralized mortgage obligations, and state and political subdivisions bonds, excluding tax increment financing ("TIF") bonds, were classified as Level 2 within the valuation hierarchy. Their fair values were determined based upon market-corroborated inputs and valuation matrices, which were obtained through third party data service providers or securities brokers through which the Corporation has historically transacted both purchases and sales of investment securities. The TIF bonds and CDO portfolio, which consists of pooled trust preferred securities issued by banks, thrifts, and insurance companies, are classified as Level 3 within the valuation hierarchy. The CDO fair values are determined by a third party using a discounted cash flow model.

Derivative financial instruments (Cash flow hedge) – The Corporation's open derivative positions are interest rate swap agreements. Those classified as Level 2 open derivative positions are valued using externally developed pricing models based on observable market inputs provided by a third party and validated by management. The Corporation has considered counterparty credit risk in the valuation of its interest rate swap assets.

Nonrecurring Basis –

Individually Evaluated Loans- Individual loans with borrowers experiencing financial difficulty and with a remaining principal balance of \$0.1 million or more are evaluated for potential specific reserves and adjusted, if a shortfall exists, to fair value less costs to sell. Fair value is measured based on the value of the value of the underlying collateral securing the loan if repayment is expected solely from the sale of operation of the collateral or present value of estimated future cash flows discounted at the loan's contractual interest rate if the loan is not determined to be collateral dependent.

Fair value for individually evaluated loans is determined using several methods. Generally, the fair value of real estate is determined based on appraisals by qualified licensed appraisals. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Adjustments are routinely made in the appraisal process by the appraisers to adjust for differences between the comparable sales and income data available. These routine adjustments are made to adjust the value of a specific property relative to comparable properties for variations in qualities such as location, size, and income production capacity relative to the subject property of the appraisal.

Subsequent to the initial impairment date, existing individually evaluated loans are reevaluated quarterly for additional impairment and adjustments to fair value less costs to sell are made, where appropriate. For individually evaluated loans, the first state of our impairment analysis involves inspection of the property in question to affirm the condition has not deteriorated since the previous impairment analysis date. Management also engages in conversations with local real estate professionals and market participants to determine the likely marketing time and value range for the property. The second state involves an assessment of current trends in the regional market. After thorough consideration of these factors, management will order a new appraisal.

For non-individually evaluated loans, the fair value is determined by updating the present value of estimated future cash flows using the loan's existing rate to reflect the payment schedule for the remaining life of the loan.

Equity Investment- Equity investments included in the table below are considered impaired with losses recognized on the income statement in net gains. Fair value of the equity investment was based on an independent third party valuation report where the value was determined based on the revenue multiples of like kind information technology businesses. These assets are included as Level 3 fair values based upon the lowest level of input that is significant to the fair value measurements.

Other real estate owned – Other real estate owned included in the table below are considered impaired with specific write-downs. Fair value of other real estate owned was based on independent third party appraisals of the properties. These values were determined based on the sales prices of similar properties in the approximate geographic area. These assets are included as Level 3 fair values based upon the lowest level of input that is significant to the fair value measurements.

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For assets measured at fair value on a recurring and non-recurring basis, the fair value measurements by level within the fair value hierarchy used at September 30, 2023 and December 31, 2022 were as follows:

(in thousands)	Fair Value Measurements at September 30, 2023 Using			
	Assets Measured at Fair Value 09/30/23	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Recurring:				
Investment securities available-for-sale:				
U.S. government agencies	\$ 9,360		\$ 9,360	
Residential mortgage-backed agencies	\$ 33,369		\$ 33,369	
Commercial mortgage-backed agencies	\$ 27,055		\$ 27,055	
Collateralized mortgage obligations	\$ 18,987		\$ 18,987	
Obligations of states and political subdivisions	\$ 10,066		\$ 10,066	
Corporate bonds	\$ 749		\$ 749	
Collateralized debt obligations	\$ 14,784			\$ 14,784
Financial derivatives	\$ 1,099		\$ 1,099	
Non-recurring:				
Equity Investment	\$ 2,862			\$ 2,862
Other real estate owned	\$ —			\$ —
(in thousands)	Fair Value Measurements at December 31, 2022 Using			
	Assets/(liabilities) Measured at Fair Value 12/31/22	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Recurring:				
Investment securities available-for-sale:				
U.S. government agencies	\$ 9,462		\$ 9,462	
Residential mortgage-backed agencies	\$ 37,401		\$ 37,401	
Commercial mortgage-backed agencies	\$ 30,732		\$ 30,732	
Collateralized mortgage obligations	\$ 21,044		\$ 21,044	
Obligations of states and political subdivisions	\$ 10,492		\$ 10,492	
Corporate bonds	\$ 887		887	
Collateralized debt obligations	\$ 15,871			\$ 15,871
Financial derivatives	\$ 1,068		\$ 1,068	
Non-recurring:				
Impaired loans, net	\$ 211			\$ 211
Equity investment	\$ 1,796			\$ 1,796
Other real estate owned	\$ —			\$ —

At September 30, 2023, individually evaluated loans had a net carrying amount of \$ 2.3 million with no valuation allowance.

At December 31, 2022, the fair value of impaired loans with a valuation allowance or charge-off was \$ 1.0 million, net of valuation allowances of \$64,700 and charge-offs of \$1.3 million. During the year ended December 31, 2022, changes to the valuation allowance or additional charge off activity was recorded on loans with a net balance of approximately \$0.4 million.

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There were no transfers of assets between any of the fair value hierarchy for the nine-month periods ended September 30, 2023 or 2022.

For Level 3 assets and liabilities measured at fair value on a recurring and non-recurring basis as of September 30, 2023 and December 31, 2022, the significant unobservable inputs used in the fair value measurements were as follows:

(in thousands)	Fair Value at September 30, 2023	Valuation Technique	Significant Unobservable Inputs	Significant Unobservable Input Value
Recurring:				
Investment Securities – available for sale -CDO	\$ 14,784	Discounted Cash Flow	Discount Margin	Range of mid 500 to low 600
Non-recurring:				
Individually Evaluated Loans, net	\$ -	Market Comparable Properties	Marketability Discount	N/A
Equity Investment	\$ 2,862	Market Method	Revenue Multiples	2.8x

(in thousands)	Fair Value at December 31, 2022	Valuation Technique	Significant Unobservable Inputs	Significant Unobservable Input Value
Recurring:				
Investment Securities – available for sale -CDO	\$ 15,871	Discounted Cash Flow	Discount Rate	Range of low to mid 300 and low to high 400
Non-recurring:				
Impaired Loans, net	\$ 211	Market Comparable Properties	Marketability Discount	10.0% - 15.0%
Equity Investment	\$ 1,796	Market Method	Revenue Multiples	2.8x

(1) Range would include discounts taken since appraisal and estimated values

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The following tables show a reconciliation of the beginning and ending balances for fair valued assets measured on a recurring basis using Level 3 significant unobservable inputs for the nine- and three- month periods ended September 30, 2023 and 2022:

		Fair Value Measurements Using Significant Unobservable Inputs (Level 3) Investment Securities Available for Sale
(in thousands)		
Beginning balance January 1, 2023		\$ 15,871
Total losses realized/unrealized:		
Included in other comprehensive loss		(1,087)
Ending balance September 30, 2023		<u>14,784</u>

		Fair Value Measurements Using Significant Unobservable Inputs (Level 3) Investment Securities Available for Sale
(in thousands)		
Beginning balance January 1, 2022		\$ 17,192
Total losses realized/unrealized:		
Included in other comprehensive loss		(1,310)
Ending balance September 30, 2022		<u>15,882</u>

		Fair Value Measurements Using Significant Unobservable Inputs (Level 3) Investment Securities Available for Sale
(in thousands)		
Beginning balance July 1, 2023		\$ 14,105
Total gains realized/unrealized:		
Included in other comprehensive income		679
Ending balance September 30, 2023		<u>14,784</u>

		Fair Value Measurements Using Significant Unobservable Inputs (Level 3) Investment Securities Available for Sale
(in thousands)		
Beginning balance July 1, 2022		\$ 16,258
Total losses realized/unrealized:		
Included in other comprehensive income		(376)
Ending balance September 30, 2022		<u>15,882</u>

There were no gains or losses included in earnings attributable to the change in realized/unrealized gains or losses related to the assets for the nine- or three-month periods ended September 30, 2023 or 2022.

The disclosed fair values may vary significantly between institutions based on the estimates and assumptions used in the various valuation methodologies. The derived fair values are subjective in nature and involve uncertainties and significant judgment.

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Therefore, they cannot be determined with precision. Changes in the assumptions could significantly impact the derived estimates of fair value. Disclosure of non-financial assets such as buildings, as well as certain financial instruments such as leases is not required. Accordingly, the aggregate fair values presented do not represent the underlying value of the Corporation.

The following tables present fair value information about financial instruments, whether or not recognized in the Consolidated Statement of Financial Condition, for which it is practicable to estimate that value. The actual carrying amounts and estimated fair values of the Corporation's financial instruments that are included in the Consolidated Statement of Financial Condition are as follows:

(in thousands)	September 30, 2023		Fair Value Measurements		
	Carrying Amount	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Financial Assets:					
Cash and due from banks	\$ 78,939	\$ 78,939	\$ 78,939		
Interest bearing deposits in banks	1,713	1,713	1,713		
Investment securities - AFS	114,370	114,370		\$ 99,586	\$ 14,784
Investment securities - HTM	215,683	176,826		174,971	1,855
Restricted bank stock	5,251	N/A			
Loans held for sale	208	208			208
Loans, net	1,362,502	1,265,829			1,265,829
Financial derivatives	1,099	1,099		1,099	
Accrued interest receivable	6,689	6,689		874	5,815
Financial Liabilities:					
Deposits - non-maturity	1,354,015	1,354,015		1,354,015	
Deposits - time deposits	221,054	217,610		217,610	
Short-term borrowed funds	53,330	53,330		53,330	
Long-term borrowed funds	110,929	110,514		110,514	
Accrued interest payable	578	578		578	
December 31, 2022		Fair Value Measurements			
		Carrying Amount	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)
					Significant Unobservable Inputs (Level 3)
Financial Assets:					
Cash and due from banks	\$ 72,720	\$ 72,720	\$ 72,720		
Interest bearing deposits in banks	1,595	1,595	1,595		
Investment securities - AFS	125,889	125,889		\$ 110,018	\$ 15,871
Investment securities - HTM	235,659	203,080		182,380	20,700
Restricted bank stock	1,027	N/A			
Loans held for sale	—	—			
Loans, net	1,264,684	1,177,702			1,177,702
Financial derivative	1,068	1,068		1,068	
Accrued interest receivable	6,051	6,051		933	5,118
Financial Liabilities:					
Deposits - non-maturity	1,450,210	1,450,210		1,450,210	
Deposits - time deposits	120,523	120,083		120,083	
Financial derivatives	—	—			—
Short-term borrowed funds	64,565	64,565		64,565	
Long-term borrowed funds	30,929	30,909		30,909	
Accrued interest payable	151	151		151	

Note 7 – Accumulated Other Comprehensive Loss

The following table presents the changes in each component of accumulated other comprehensive loss for the 12 months ended December 31, 2022 and the three-month periods ended March 31, 2023, June 30, 2023, and September 30, 2023:

(in thousands)	Investment securities- with credit related impairment AFS	Investment securities- all other AFS	Investment securities- HTM	Cash Flow Hedge	Pension Plan	SERP	Total
Accumulated OCL, net:							
Balance - January 1, 2022	\$ (949)	\$ (5,749)	\$ (134)	\$ (319)	\$ (18,108)	\$ (2,055)	\$ (27,314)
Other comprehensive (loss)/income before reclassifications	(614)	(10,629)	(6,120)	1,116	684	2,430	(13,133)
Amounts reclassified from accumulated other comprehensive loss	(148)	(2)	551	—	821	199	1,421
Balance - December 31, 2022	<u>\$ (1,711)</u>	<u>\$ (16,380)</u>	<u>\$ (5,703)</u>	<u>\$ 797</u>	<u>\$ (16,603)</u>	<u>\$ 574</u>	<u>\$ (39,026)</u>
Other comprehensive (loss)/income before reclassifications	(1,180)	985	—	(138)	123	—	(210)
Amounts reclassified from accumulated other comprehensive income	(37)	—	133	—	184	(1)	279
Balance - March 31, 2023	<u>\$ (2,928)</u>	<u>\$ (15,395)</u>	<u>\$ (5,570)</u>	<u>\$ 659</u>	<u>\$ (16,296)</u>	<u>\$ 573</u>	<u>\$ (38,957)</u>
Other comprehensive income/(loss) before reclassifications	111	(1,654)	—	150	(42)	—	(1,435)
Amounts reclassified from accumulated other comprehensive loss	(40)	—	129	—	195	(2)	282
Balance - June 30, 2023	<u>\$ (2,857)</u>	<u>\$ (17,049)</u>	<u>\$ (5,441)</u>	<u>\$ 809</u>	<u>\$ (16,143)</u>	<u>\$ 571</u>	<u>\$ (40,110)</u>
Other comprehensive income/(loss) before reclassifications	475	(3,201)	—	11	(1,033)	—	(3,748)
Amounts reclassified from accumulated other comprehensive loss	(38)	—	130	—	194	(1)	285
Balance - September 30, 2023	<u>\$ (2,420)</u>	<u>\$ (20,250)</u>	<u>\$ (5,311)</u>	<u>\$ 820</u>	<u>\$ (16,982)</u>	<u>\$ 570</u>	<u>\$ (43,573)</u>

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The following tables present the components of other comprehensive loss for the nine- and three- month periods ended September 30, 2023 and 2022:

Components of Other Comprehensive Loss (in thousands)	Before Tax Amount	Tax (Expense) Benefit	Net
For the nine months ended September 30, 2023			
Available for sale (AFS) securities with credit related impairment:			
Unrealized holding losses	\$ (777)	\$ 183	\$ (594)
Less: accretable yield recognized in income	152	(37)	115
Net unrealized losses on investments with credit related impairment	(929)	220	(709)
Available for sale securities – all other:			
Unrealized holding losses	(5,065)	1,195	(3,870)
Held to maturity securities:			
Unrealized holding losses on securities transferred to held to maturity	—	—	—
Less: amortization recognized in income	(513)	121	(392)
Net unrealized gains on HTM securities	513	(121)	392
Cash flow hedges:			
Unrealized holding gains	30	(7)	23
Pension Plan:			
Unrealized net actuarial gain	(1,250)	298	(952)
Less: amortization of unrecognized loss	(750)	177	(573)
Net pension plan liability adjustment	(500)	121	(379)
SERP:			
Unrealized net actuarial loss	—	—	—
Less: amortization of unrecognized loss	6	(2)	4
Net SERP liability adjustment	(6)	2	(4)
Other comprehensive loss	\$ (5,957)	\$ 1,410	\$ (4,547)

Components of Other Comprehensive Loss (in thousands)	Before Tax Amount	Tax (Expense) Benefit	Net
For the nine months ended September 30, 2022			
Available for sale (AFS) securities with credit related impairment:			
Unrealized holding gains	\$ (853)	\$ 228	\$ (625)
Less: accretable yield recognized in income	152	(41)	111
Net unrealized losses on investments with credit related impairment	(1,005)	269	(736)
Available for sale securities – all other:			
Unrealized holding losses	(22,971)	6,147	(16,824)
Unrealized holding losses on securities transferred from available for sale to held to maturity	8,328	(2,228)	6,100
Less: gains recognized in income	3	(1)	2
Net unrealized losses on all other AFS securities	(14,646)	3,920	(10,726)
Held to maturity securities:			
Unrealized holding losses on securities transferred to held to maturity	(8,328)	2,228	(6,100)
Less: gains recognized in income	93	(25)	68
Less: amortization recognized in income	(644)	172	(472)
Net unrealized losses on HTM securities	(7,777)	2,081	(5,696)
Cash flow hedges:			
Unrealized holding gains	1,622	(434)	1,188
Pension Plan:			
Unrealized net actuarial loss	(14,079)	3,767	(10,312)
Less: amortization of unrecognized loss	(837)	224	(613)
Net pension plan liability adjustment	(13,242)	3,543	(9,699)
SERP:			
Unrealized net actuarial loss	—	—	—
Less: amortization of unrecognized loss	(203)	54	(149)
Less: amortization of prior service costs	—	—	—
Net SERP liability adjustment	203	(54)	149
Other comprehensive loss	\$ (34,845)	\$ 9,325	\$ (25,520)

Components of Other Comprehensive Loss (in thousands)	Before Tax Amount	Tax (Expense) Benefit	Net
For the three months ended September 30, 2023			
Available for sale (AFS) securities with credit related impairment:			
Unrealized holding gains	\$ 633	\$ (158)	\$ 475
Less: accretable yield recognized in income	51	(13)	38
Net unrealized gains on investments with credit related impairment	<u>582</u>	<u>(145)</u>	<u>437</u>
Available for sale securities – all other:			
Net unrealized losses on all other AFS securities	(4,183)	982	(3,201)
Held to maturity securities:			
Unrealized holding gains	—	—	—
Less: amortization recognized in income	(167)	37	(130)
Net unrealized gains on HTM securities	<u>167</u>	<u>(37)</u>	<u>130</u>
Cash flow hedges:			
Unrealized holding gains	14	(3)	11
Pension Plan:			
Unrealized net actuarial loss	(1,352)	319	(1,033)
Less: amortization of unrecognized loss	(251)	57	(194)
Net pension plan liability adjustment	<u>(1,101)</u>	<u>262</u>	<u>(839)</u>
SERP:			
Unrealized net actuarial loss	—	—	—
Less: amortization of unrecognized loss	2	(1)	1
Net SERP liability adjustment	<u>(2)</u>	<u>1</u>	<u>(1)</u>
Other comprehensive loss	<u><u>\$ (4,523)</u></u>	<u><u>\$ 1,060</u></u>	<u><u>\$ (3,463)</u></u>

Components of Other Comprehensive Loss (in thousands)	Before Tax Amount	Tax (Expense) Benefit	Net
For the three months ended September 30, 2022			
Available for sale (AFS) securities with credit related impairment:			
Unrealized holding gains	\$ (199)	\$ 53	\$ (146)
Less: accretable yield recognized in income	51	(14)	37
Net unrealized losses on investments with credit related impairment	(250)	67	(183)
Available for sale securities – all other:			
Unrealized holding losses	(6,768)	1,811	(4,957)
Less: gains recognized in income	—	—	—
Net unrealized losses on all other AFS securities	(6,768)	1,811	(4,957)
Held to maturity securities:			
Unrealized holding gains	—	—	—
Less: gains recognized in income	93	(25)	68
Less: amortization recognized in income	(320)	85	(235)
Net unrealized gains on HTM securities	227	(60)	167
Cash flow hedges:			
Unrealized holding gains	534	(142)	392
Pension Plan:			
Unrealized net actuarial loss	(3,537)	945	(2,592)
Less: amortization of unrecognized loss	(279)	74	(205)
Less: amortization of prior service costs	—	—	—
Net pension plan liability adjustment	(3,258)	871	(2,387)
SERP:			
Unrealized net actuarial loss	—	—	—
Less: amortization of unrecognized loss	(68)	18	(50)
Less: amortization of prior service costs	—	—	—
Net SERP liability adjustment	68	(18)	50
Other comprehensive loss	\$ (9,447)	\$ 2,529	\$ (6,918)

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The following table presents the details of amounts reclassified from accumulated other comprehensive loss for the nine- and three- month periods ended September 30, 2023 and 2022:

Amounts Reclassified from Accumulated Other Comprehensive Loss (in thousands)	Nine Months Ended September 30, 2023 2022		Affected Line Item in the Statement Where Net Income is Presented
	2023	2022	
Net unrealized gains on available for sale investment securities with OTTI:			
Accretable yield	\$ 152	\$ 152	Interest income on taxable investment securities
Taxes	(37)	(41)	Credit for income tax expense
	<u>\$ 115</u>	<u>\$ 111</u>	Net of tax
Net unrealized gains on available for sale investment securities - all others:			
Gains recognized	\$ —	\$ 3	Net gains
Taxes	—	(1)	Provision for income tax expense
	<u>\$ —</u>	<u>\$ 2</u>	Net of tax
Net unrealized losses on held to maturity securities:			
Amortization	\$ (513)	\$ (644)	Interest income on taxable investment securities
Gains/(losses) recognized	—	93	Net gains/(losses)
Taxes	<u>121</u>	<u>147</u>	Provision for income tax expense
	<u><u>\$ (392)</u></u>	<u><u>\$ (404)</u></u>	Net of tax
Net pension plan liability adjustment:			
Amortization of unrecognized loss	\$ (750)	\$ (837)	Other Expense
Taxes	177	224	Provision for income tax expense
	<u><u>\$ (573)</u></u>	<u><u>\$ (613)</u></u>	Net of tax
Net SERP liability adjustment:			
Amortization of unrecognized gain/(loss)	\$ 6	\$ (203)	Other Expense
Taxes	(2)	54	(Credit)/provision for income tax expense
	<u><u>\$ 4</u></u>	<u><u>\$ (149)</u></u>	Net of tax
Total reclassifications for the period	<u><u>\$ (846)</u></u>	<u><u>\$ (1,053)</u></u>	Net of tax

Amounts Reclassified from Accumulated Other Comprehensive Loss (in thousands)	Three Months Ended September 30, Affected Line Item in the Statement		
	2023	2022	Where Net Income is Presented
Net unrealized gains on available for sale investment securities with OTTI:			
Accretable Yield	\$ 51	\$ 51	Interest income on taxable investment securities
Taxes	(12)	(14)	Provision for income tax expense
	<u>\$ 39</u>	<u>\$ 37</u>	Net of tax
Net unrealized losses on held to maturity securities:			
Amortization	\$ (167)	\$ (320)	Interest income on taxable investment securities
Gains/(losses) recognized	—	93	Net gains/(losses)
Taxes	38	60	Provision for income tax expense
	<u>\$ (129)</u>	<u>\$ (167)</u>	Net of tax
Net pension plan liability adjustment:			
Amortization of unrecognized loss	\$ (251)	\$ (279)	Other expense
Taxes	57	74	Provision for income tax expense
	<u>\$ (194)</u>	<u>\$ (205)</u>	Net of tax
Net SERP liability adjustment:			
Amortization of unrecognized loss	\$ 2	\$ (68)	Other expense
Taxes	(1)	18	Provision for income tax expense
	<u>\$ 1</u>	<u>\$ (50)</u>	Net of tax
Total reclassifications for the period			
	<u><u>\$ (283)</u></u>	<u><u>\$ (385)</u></u>	Net of tax

Note 8 - Equity Compensation Plan Information

At the 2018 Annual Meeting of Shareholders, First United Corporation's shareholders approved the First United Corporation 2018 Equity Compensation Plan (the "Equity Plan") which authorizes the issuance of up to 325,000 shares of common stock to employees, directors and qualifying consultants pursuant to stock options, stock appreciation rights, stock awards, dividend equivalents, and other stock-based awards.

The Corporation complies with the provisions of ASC Topic 718, *Compensation-Stock Compensation*, in measuring and disclosing stock compensation cost. The measurement objective in ASC Paragraph 718-10-30-6 requires public companies to measure the cost of employee services received in exchange for an award of equity instruments based on the grant date fair value of the award. The cost is recognized in expense over the period in which an employee is required to provide service in exchange for the award (the vesting period).

Pursuant to First United Corporation's director compensation policy, each director receives an annual retainer of 1,000 shares of First United Corporation common stock, plus \$15,000 to be paid, at the director's election, in cash or additional shares of common stock. In May 2023, a total of 16,931 fully vested shares of common stock were issued to directors, which had a grant date fair value of \$13.23 per share. In May 2022, a total of 14,940 fully vested shares of common stock were issued to directors, which had a grant date fair value of \$18.92 per share. In January 2023, a total of 333 fully vested shares of common stock were issued to a new director, which had a grant date fair value of \$19.36 per share. Director stock compensation was \$194,001 for the nine months ended September 30, 2023 and \$196,254 for the nine months ended September 30, 2022. Director stock compensation expense was \$56,000 for the quarter ended September 30, 2023 and \$ 70,666 for the quarter ended September 30, 2022.

During the nine- and three-month periods ended September 30, 2023, employee stock compensation expense was approximately \$12,000 and \$5,000, respectively. Employee stock compensation expense was \$ 0 for both the nine- and three-month periods ended September 30, 2022.

Restricted Stock Units

On March 26, 2020, pursuant to the Corporation's Long Term Incentive Plan (the "LTIP"), which is a sub-plan of the Equity Plan, the Compensation Committee of First United Corporation's Board of Directors (the "Committee") granted RSUs to the Corporation's principal executive officer, its principal financial officer, and certain of its other executive officers. An RSU contemplates the issuance of shares of common stock of First United Corporation if and when the RSU vests.

The RSUs granted to each of the foregoing officers consist of (i) a performance vesting award for a three year performance period and (ii) a time-vesting award that will vest ratably over a three year period. Target performance levels were set based on the annual budget which supports the Corporation's long-term objective of achieving high performance as compared to peers. Threshold performance is the minimum level of acceptable performance as defined by the Committee and maximum performance represented a level potentially achievable under ideal circumstances. Achievement of the threshold performance level would result in each executive participant earning a payout at 50% of his or her respective target award opportunity. Achievement of the target performance level would result in the executive participant earning the target award and achievement at or above the maximum performance level would result in the executive participant earning 150% of the target opportunity. Actual results for any goal that falls between performance levels would be interpolated to calculate a proportionate award. For the performance period ending December 31, 2022, the RSUs performance goals are based on earnings per share for the year ending December 31, 2022 and growth in tangible book value per share during the performance period. For the performance period ending December 31, 2023, the RSUs performance goals are based on earnings per share for the year ending December 31, 2023 and growth in tangible book value per share during the performance period. For the performance period ending December 31, 2024, the RSUs performance goals are based on earnings per share for the year ending December 31, 2024 and growth in tangible book value per share during the performance period.

To receive any shares under an RSU, a grantee must be employed by the Corporation or one of its subsidiaries on the applicable vesting date, except that a grantee whose employment terminates prior to such vesting date due to death, disability or retirement will be entitled to a pro-rated portion of the shares subject to the RSUs, assuming that, in the case of performance-vesting RSUs, the performance goals had been met at their "target" levels.

In the first quarter of 2020, RSUs were granted relating to (i) 9,791 performance-vesting shares (target level) for the performance period ending December 31, 2021 (the "2019 LTIP year") and (ii) 10,143 performance-vesting shares and 5,070 time-vesting shares (target level) for the performance period ending December 31, 2022 (the "2020 LTIP year"). Each RSU had a grant date fair market value of \$12.54 per share of common stock underlying the RSU. The time-vesting RSUs will vest ratably over a three-year period that began on March 26, 2021. On March 9, 2022, 14,688 shares subject to RSUs granted for the 2019 LTIP year were issued at maximum performance level. On March 8, 2023, 15,216 shares subject to RSUs granted for the 2020 LTIP year were issued at maximum performance. On March 26, 2021, 1,690 of the 5,070 time-vesting shares were issued to participants. On March 28, 2022, 1,688 shares of the 3,380 remaining time-vesting shares were issued to participants. On March 26, 2023, 1,692 shares of the remaining time-vesting shares were issued to participants. Net stock compensation expense/(credit) was \$15,896 for the nine months ended September 30, 2023, and (\$ 5,299) for the nine months ended September 30, 2022. Stock compensation expense was \$0 and (\$37,091) for the third quarters of 2023 and 2022, respectively. All compensation expense related to the 2019 LTIP year was recognized as of March 31, 2022. All compensation expense related to the 2020 LTIP plans was recognized as of March 31, 2023.

In May 2021, RSUs relating to 7,389 performance-vesting shares and 3,693 time-vesting shares (target level) for plan year 2021 were granted, which had a grant date fair market value of \$17.93 per share of common stock underlying each RSU. The performance period for the performance-vesting RSUs is the three-year period ending December 31, 2023. The time-vesting RSUs will vest ratably over a three-year period beginning on May 5, 2022. On May 5, 2022, 1,230 shares of the 3,693 time-vesting RSUs were issued to participants. On May 5, 2023, 1,230 shares of the remaining 2,463 time-vesting shares were issued to the participants. Stock compensation expense was \$49,714 for the nine-month periods ended of 2023 and 2022. Stock compensation expense was \$16,571 for both of the three-month periods ended September 30, 2023 and 2022. Unrecognized compensation expense as of September 30, 2023 related to unvested units was \$38,667.

In March 2022, RSUs relating to 8,096 performance-vesting shares and 6,238 time-vesting shares (target level) for plan year 2022 were granted, which had a grant date fair market value of \$21.88 per share of common stock underlying each RSU. The performance period for the performance-vesting RSUs is the three-year period ending December 31, 2024. The time-vesting RSUs will vest ratably over a three year period beginning on March 9, 2023. On March 9, 2023, 2,079 shares of the 6,238 time-vesting

RSUs were issued to participants. Stock compensation expense was \$ 78,436 and \$52,290 for the nine-month periods ended September 30, 2023 and 2022, respectively. Stock compensation expense was \$26,145 for both of the three-month periods ended September 30, 2023 and 2022. Unrecognized compensation expense as of September 30, 2023 related to unvested units was \$156,872.

In March 2023, RSUs relating to 10,214 performance-vesting shares and 7,920 time-vesting shares (target level) for plan year 2023 were granted, which had a grant date fair market value of \$18.25 per share of common stock underlying each RSU. The performance period for the performance-vesting RSUs is the three year period ending December 31, 2025. The time-vesting RSUs will vest ratably over a three-year period beginning on March 15, 2024. Stock compensation expense was \$55,170 and \$27,585 for the nine- and three-month periods ended September 30, 2023. Unrecognized compensation expense as of September 30, 2023 related to unvested units was \$275,859.

Note 9- Derivative Financial Instruments

As a part of managing interest rate risk, the Corporation entered into interest rate swap agreements to modify the re-pricing characteristics of certain interest-bearing liabilities. The Corporation has designated its interest rate swap agreements as cash flow hedges under the guidance of ASC Subtopic 815-30, *Derivatives and Hedging – Cash Flow Hedges*. Cash flow hedges have the effective portion of changes in the fair value of the derivative, net of taxes, recorded in net accumulated other comprehensive income.

In March 2016, the Corporation entered into four interest rate swap contracts totaling \$30.0 million notional amount, hedging future cash flows associated with floating rate trust preferred debt. As of September 30, 2023, \$15.0 million notional amount remains. The interest rate swap creates an effective fixed interest rate of 4.6450% on the \$15.0 million notional amount of the Corporation's junior subordination debt until the interest rate swap's maturity in March 2026. The fair value of the interest rate swap contracts was \$1.1 million at both September 30, 2023 and December 31, 2022.

For the nine months ended September 30, 2023, the Corporation recorded an increase in the value of the derivatives of thousand and the related deferred tax of \$7 thousand in net accumulated other comprehensive loss to reflect the effective portion of cash flow hedges. For the three months ended September 30, 2023, the Corporation recorded an increase in the value of the derivatives of \$14 thousand and the related deferred tax of \$3 thousand in net accumulated other comprehensive income to reflect the effective portion of cash flow hedges. ASC Subtopic 815-30 requires the net accumulated other comprehensive loss to be reclassified to earnings if the hedge becomes ineffective or is terminated. There was no hedge ineffectiveness recorded for the nine- or three-month periods ended September 30, 2023. The Corporation does not expect any material losses relating to these hedges to be reclassified into earnings within the next 12 months.

Interest rate swap agreements are entered into with counterparties that meet established credit standards and the Corporation believes that the credit risk inherent in these contracts is not significant as of September 30, 2023.

The table below discloses the impact of derivative financial instruments on the Corporation's Consolidated Financial Statements for the nine-and three-month periods ended September 30, 2023 and 2022.

Derivative in Cash Flow Hedging Relationships

(in thousands)	Amount of gain or (loss) recognized in OCI on derivative (effective portion), net of tax	Amount of gain or (loss) reclassified from accumulated OCI into income (effective portion) (a)	Amount of gain or (loss) recognized in income or derivative (ineffective portion and amount excluded from effectiveness testing) (b)
Interest rate contracts:			
Nine months ended:			
September 30, 2023	\$ 23	\$ —	\$ —
September 30, 2022	1,188	—	—
Three months ended:			
September 30, 2023	\$ 11	\$ —	\$ —
September 30, 2022	392	—	—

Notes:

- (a) Reported as interest expense
- (b) Reported as other income

Note 10 – Regulatory Capital Requirements

The following table presents our capital ratios as of September 30, 2023 and December 31, 2022.

	September 30, 2023	December 31, 2022	Required for Capital Adequacy Purposes	Required to be Well Capitalized
Total Capital (to risk-weighted assets)	14.12 %	14.37 %	8.00 %	10.00 %
Tier 1 Capital (to risk-weighted assets)	12.88 %	13.29 %	6.00 %	8.00 %
Common Equity Tier 1 Capital (to risk-weighted assets)	12.88 %	13.29 %	4.50 %	6.50 %
Tier 1 Capital (to average assets)	9.81 %	10.01 %	4.00 %	5.00 %

As of September 30, 2023 and December 31, 2022, the Bank was considered "well capitalized" under the regulatory framework for prompt corrective action. We adopted CECL effective January 1, 2023 and elected not to implement the regulatory agencies' capital transition and instead opted to record the impact to our capital ratios immediately upon implementation.

Effective with the implementation of CECL, a \$2.2 million adjustment, net of tax, was made to retained earnings. The adjustment did not have a material impact to our capital ratios.

Note 11 – Deposits

The following table summarizes deposits as of September 30, 2023 and December 31, 2022.

(dollars in thousands)	September 30, 2023		December 31, 2022	
	Balance	Percent	Balance	Percent
Non-Interest-bearing deposits:	\$ 429,691	27%	\$ 506,613	32%
Interest-bearing deposits:				
Demand	381,782	24%	327,685	21%
Money Market	338,153	22%	365,192	23%
Savings deposits	204,389	13%	250,720	16%
Time deposits- retail	160,380	10%	120,523	8%
Time deposits- brokered	60,674	4%	—	0%
Total Deposits	\$ 1,575,069	100%	\$ 1,570,733	100%

Note 12 – Borrowed Funds

The following is a summary of borrowings:

(Dollars in thousands)	Nine Months Ended September 30, 2023	Year Ended December 31, 2022
Short-term Correspondent Bank Advance:		
Securities sold under agreements to repurchase:		
Outstanding at end of period	\$ 53,330	\$ 64,565
Weighted average interest rate at end of period	0.27%	0.12%
Maximum amount outstanding as of any month end	\$ 59,777	\$ 75,912
Average amount outstanding	\$ 51,044	\$ 63,182
Approximate weighted average rate during the period	0.23%	0.12%
FHLB advances, bearing fixed interest at rates ranging from 4.53% to 4.69% at September 30, 2023	\$ 80,000	\$ -
Junior subordinated debt, bearing variable interest rate of 8.42% at September 30, 2023 and 7.49% at December 31, 2022	30,929	30,929
Total borrowings outstanding	\$ 164,259	\$ 95,494

At September 30, 2023, the repurchase agreements were secured by \$ 58.7 million in investment securities issued by government related agencies. A minimum of 102% of fair value is pledged against account balances.

Note 13 – Segment Reporting

Currently, the Corporation conducts business in two operating segments: (i) Community Banking and (ii) Trust and Investment Services. The accounting policies of the segments are the same as those described in the summary of significant accounting policies provided earlier in this report.

Business activity for the operating segments are as follows:

Community Banking: The Community Banking segment is conducted through the Bank and involves delivering a broad range of financial products and services, including various loan and deposit products, to consumer, business, and not-for-profit customers. Parent company income and assets are included in the Community Banking segment, as the majority of parent company functions are related to this segment. Major revenue sources include net interest income, gains on sales of mortgage loans, and service charges on deposit accounts. Expenses include personnel, occupancy, marketing, equipment, and other expenses. Non-cash charges other than depreciation of fixed assets were immaterial for the nine and three months ended September 30, 2023 and 2022.

Trust and Investment Services: The Trust and Investment Services segment is conducted through the Bank and offers corporate trustee services, trust and estate administration, IRA administration and custody services. Revenues for this segment is generated from administration, service and custody fees, as well as management fees that are derived from Assets Under Management. Expenses include personnel, occupancy, marketing, equipment, and other expenses. Non-cash charges associated with amortization of intangibles were approximately \$156,000 for both of the nine-month periods ended September 30, 2023 and 2022 and \$52,000 for both of the three-month periods ended September 30, 2023 and 2022.

Information for the operating segments for the nine- and three-month periods ended September 30, 2023 are presented in the following tables:

	Nine Months Ended September 30, 2023		
	Community Banking	Trust and Investment Services	Total
(in thousands)			
Interest income	\$ 58,965	\$ -	\$ 58,965
Interest expense	16,289	-	16,289
Credit loss expense	1,201	-	1,201
Non-interest income	6,927	6,933	13,860
Non-interest expense	34,070	3,864	37,934
Income before income taxes and intercompany fees	14,332	3,069	17,401
Intercompany management fee income (expense)	9	(9)	-
Income before income taxes	14,341	3,060	17,401
Income tax expense	3,456	643	4,099
Net income	\$ 10,885	\$ 2,417	\$ 13,302

	Nine months ended September 30, 2022		
	Community Banking	Trust and Investment Services	Total
(in thousands)			
Interest income	\$ 45,063	\$ -	\$ 45,063
Interest expense	2,610	-	2,610
Credit loss expense	109	-	109
Non-interest income	6,517	7,043	13,560
Non-interest expense	28,007	3,532	31,539
Income before income taxes and intercompany fees	20,854	3,511	24,365
Intercompany management fee income (expense)	-	-	-
Income before income taxes	20,854	3,511	24,365
Income tax expense	5,549	737	6,286
Net income	\$ 15,305	\$ 2,774	\$ 18,079

	Three Months Ended September 30, 2023		
	Community Banking	Trust and Investment Services	Total
(in thousands)			
Interest income	\$ 21,164	\$ -	\$ 21,164
Interest expense	7,180	-	7,180
Credit loss expense	263	-	263
Non-interest income	2,515	2,383	4,898
Non-interest expense	11,507	1,278	12,785
Income before income taxes and intercompany fees	4,729	1,105	5,834
Intercompany management fee income (expense)	3	(3)	-
Income before income taxes	4,732	1,102	5,834
Income tax expense	1,090	231	1,321
Net income	\$ 3,642	\$ 871	\$ 4,513

	Three Months Ended September 30, 2022		
	Community Banking	Trust and Investment Services	Total
(in thousands)			
Interest income	\$ 16,185	\$ -	\$ 16,185
Interest expense	1,044	-	1,044
Credit loss credit	(101)	-	(101)
Non-interest income	2,423	2,277	4,700
Non-interest expense	9,208	1,121	10,329
Income before income taxes and intercompany fees	8,457	1,156	9,613
Intercompany management fee income (expense)	-	-	-
Income before income taxes	8,457	1,156	9,613
Income tax expense	2,434	243	2,677
Net income	\$ 6,023	\$ 913	\$ 6,936

Total non-fiduciary assets of the trust and investment services segment were \$ 0.8 million (including \$0.7 million in intangible assets) at September 30, 2023 and \$0.9 million (including \$0.8 million in intangible assets) at December 31, 2022.

Note 14 – Goodwill

ASC Topic 350, Intangibles- Goodwill and Other Intangibles provides guidance with respect to goodwill. Under this guidance, goodwill is not amortized but shall be tested at least annually for impairment at a level of accounting referred to as a reporting unit. The Corporation is considered the sole reporting unit. Goodwill of a reporting unit shall be tested for impairment between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount. Impairment of goodwill is the condition that exists when the carrying amount of a reporting unit that includes goodwill exceeds the fair value. A goodwill impairment loss is recognized for the amount that the carrying amount of a reporting unit, including goodwill, exceeds fair value, limited to the total amount of goodwill allocated to that reporting unit.

An entity may assess qualitative factors to determine whether it is more likely than not (that is, a likelihood of more than 50 percent) that the fair value of a reporting unit is less than its carrying amount, including goodwill. If after assessing the totality of events or circumstances qualitatively, an entity determines that it is not more likely than not that the fair value of a reporting unit is less than its carrying amount, then the quantitative goodwill impairment test is unnecessary.

Management notes that the heightened liquidity concerns that caused the failure of three banks in the United States in 2023 has had global impacts on some macroeconomic conditions and has created an unprecedented economic environment in which the Corporation and many other financial institutions are operating. The uncertainty has resulted in a significant decrease in the Corporation's stock price, as well as the banking industry in general. Based on the totality of the circumstances and the impact of the economic conditions on the stock price, an internal analysis as of September 30, 2023, was performed. The results of the internal analysis determined there is no goodwill impairment as of September 30, 2023. Management will continue to monitor the goodwill throughout the remainder of 2023.

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

INTRODUCTION

The following discussion and analysis is intended as a review of material changes in and significant factors affecting the financial condition and results of operations of First United Corporation and its consolidated subsidiaries for the periods indicated. This discussion and analysis should be read in conjunction with the unaudited consolidated financial statements and the notes thereto contained in Item 1 of Part I of this report, as well as the audited consolidated financial statements and related notes included in First United Corporation's Annual Report on Form 10-K for the year ended December 31, 2022.

Unless the context clearly suggests otherwise, references in this report to "us", "we", "our", and "the Corporation" are to First United Corporation and its consolidated subsidiaries.

FORWARD-LOOKING STATEMENTS

This report contains forward-looking statements as defined by the Private Securities Litigation Reform Act of 1995. Forward-looking statements do not represent historical facts, but are statements about management's beliefs, plans and objectives about the future, as well as its assumptions and judgments concerning such beliefs, plans and objectives. These statements are evidenced by terms such as "anticipate," "estimate," "should," "expect," "believe," "intend," and similar expressions. Although these statements reflect management's good faith beliefs and projections, they are not guarantees of future performance and they may not prove true. The beliefs, plans and objectives on which forward-looking statements are based involve risks and uncertainties that could cause actual results to differ materially from those addressed in the forward-looking statements. For a discussion of these risks and uncertainties, see the section of the periodic reports that First United Corporation files with the Securities and Exchange Commission entitled "Risk Factors".

FIRST UNITED CORPORATION

First United Corporation is a Maryland corporation chartered in 1985 and a financial holding company registered with the Board of Governors of the Federal Reserve System (the "FRB") under the Bank Holding Company Act of 1956, as amended, that elected financial holding company status in 2021. The Corporation's primary business is serving as the parent company of First United Bank & Trust, a Maryland trust company (the "Bank"), First United Statutory Trust I ("Trust I") and First United Statutory Trust II ("Trust II" and together with Trust I, "the Trusts"), both Connecticut statutory business trusts. The Trusts were formed for the purpose of selling trust preferred securities that qualified as Tier 1 capital. The Bank has two consumer finance company subsidiaries- OakFirst Loan Center, Inc., a West Virginia corporation, and OakFirst Loan Center, LLC, a Maryland limited liability company – and two subsidiaries that it uses to hold real estate acquired through foreclosure or by deed in lieu of foreclosure – First OREO Trust, a Maryland statutory trust, and FUBT OREO I, LLC, a Maryland limited liability company. In addition, the Bank owns 99.9% of the limited partnership interests in Liberty Mews Limited Partnership, a Maryland limited partnership formed for the purpose of acquiring, developing and operating low-income housing units in Garrett County, Maryland, and a 99.9% non-voting membership interest in MCC FUBT Fund, LLC, an Ohio limited liability company formed for the purpose of acquiring, developing and operating low-income housing units in Allegany County, Maryland.

At September 30, 2023, the Corporation's total assets were \$1.9 billion, net loans were \$1.4 billion, and deposits were \$1.6 billion. Shareholders' equity at September 30, 2023 was \$155.0 million.

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We maintain an Internet site at www.mybank.com on which we make available, free of charge, First United Corporation's Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, and all amendments to the foregoing as soon as reasonably practicable after these reports are electronically filed with, or furnished to, the SEC.

SELECTED FINANCIAL DATA

The following table sets forth certain selected financial data for the nine-month periods ended September 30, 2023 and 2022 and is qualified in its entirety by the detailed information and unaudited financial statements, including the notes thereto, included elsewhere in this quarterly report.

	As of the nine months ended September 30,	
	2023	2022
Per Share Data		
Basic net income per common share	\$ 1.99	\$ 2.72
Diluted net income per common share	\$ 1.98	\$ 2.72
Basic book value per common share	\$ 23.08	\$ 19.83
Diluted book value per common share	\$ 23.03	\$ 19.80
Significant Ratios:		
Return on Average Assets (a)	0.93 %	1.35 %
Return on Average Equity (a)	11.44 %	17.66 %
Average Equity to Average Assets	8.14 %	7.66 %
Capital Ratios:		
Consolidated Total Capital (to risk weighted assets)	15.81 %	15.50 %
Consolidated Tier 1 Capital (to risk weighted assets)	14.60 %	14.40 %
Consolidated Common Equity Tier 1 Capital (to risk weighted assets)	12.60 %	12.36 %
Consolidated Tier 1 Capital (to average assets)	11.25 %	11.23 %

RESULTS OF OPERATIONS

Overview

Consolidated net income was \$4.5 million for the third quarter of 2023, compared to \$6.9 million for the third quarter of 2022 and \$4.4 million for the second quarter of 2023. Basic and diluted net income was \$0.67 per share for the third quarter of 2023, compared to basic and diluted net income of \$1.04 per share for the third quarter of 2022 and \$0.66 per share for the second quarter of 2023.

The decrease in quarterly net income, year-over-year, was primarily driven by a \$1.3 million decrease in net interest income. Interest expense increased by \$6.1 million year-over-year, which was partially offset by an increase in interest income of \$4.9 million. The provision for credit losses was \$0.3 million for the third quarter of 2023, compared to a credit to the provision of \$0.1 million for the third quarter of 2022. Salaries and employee benefits increased by \$0.8 million due to an increase in health insurance costs related to unusually high claims, as well as increased salary expense for new hires, merit increases effective April 1, 2023, a one-time severance pay-out, and decreases in deferred loan costs, partially offset by decreases in incentives and stock compensation. Data processing expenses increased by \$0.1 million, Federal Deposit Insurance Corporation ("FDIC") premiums increased by \$0.1 million and miscellaneous expenses increased by \$0.6 million primarily attributable to increased net periodic pension plan costs of

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\$0.3 million and check fraud related expenses of \$0.3 million. Check fraud has been on the rise throughout 2023 industry-wide. During the third quarter, management implemented additional procedures to help mitigate this increased risk.

Net income for the first nine months of 2023 was \$13.3 million, compared to \$18.1 million for the same period in 2022, a \$4.8 million decrease. The year-over-year decrease was driven by an increase in total operating expenses of \$6.4 million. Salaries and employee benefits increased by \$3.2 due primarily to increased salary expense of \$1.9 million related to new hires, the competitive environment for labor and merit increases effective April 1, 2023, increased health insurance costs of \$1.0 million associated with unusually high claims and decreases of \$0.4 in deferred loan costs. Occupancy and equipment expense increased by \$0.2 million, data processing expense increased by \$0.4 million due to planned implementation of new technology, and FDIC assessments increased by \$0.2 million. Other miscellaneous expenses, such as loan service fees, dues and licenses, check fraud expenses, employee benefit plan expense, and miscellaneous expenses, increased by \$1.7 million and professional fees increased by \$0.7 million due to the one-time \$0.8 million cash receipt related to reimbursement of litigation expenses that was credited to expenses in 2022. Provision for credit losses increased by \$1.1 million when compared to prior year period. These increases were partially offset by increases in net interest income of \$0.2 million, gains on sales of mortgages of \$0.3 million, service charges on deposit accounts of \$0.2 million, and \$0.1 million increase in miscellaneous income. Income taxes were down by \$2.2 million comparing the two periods.

Other operating income, including gains, for the third quarter of 2023 increased by \$0.2 million when compared to the same period of 2022. Increases in service charges, wealth management income, and gains on sales of mortgages were partially offset by a decrease in debit card income.

Other operating income for the nine months ended September 30, 2023 increased by \$0.3 million when compared to the same period of 2022. This increase was primarily due to the increase in gains on sales of mortgages of \$0.3 million, service charges on deposit accounts of \$0.2 million, and debit card income of \$0.1 million, partially offset by a decrease of \$0.1 million in wealth management income attributable to the decline in market values of assets under management.

Operating expenses increased by \$2.5 million when comparing the third quarter of 2023 to the third quarter of 2022. This increase was primarily driven by a \$0.8 million increase in salaries and employee benefits due to an increase in health insurance costs related to unusually high claims, as well as increased salary expense for new hires, merit increases effective April 1, 2023, and reduced loan costs. Legal and professional expenses increased by \$0.7 million attributable to the one-time \$0.8 million cash receipt related to reimbursement of litigation expenses that was credited to expense in 2022. Miscellaneous expenses increased by \$0.6 million due primarily to increases of \$0.3 in check fraud related expenses and net periodic pension plan costs of \$0.3 million. Data processing expenses, FDIC premiums, and marketing expenses each increased by \$0.1 million year over year.

For the nine months ended September 30, 2023, non-interest expenses increased by \$6.4 million when compared to the nine months ended September 30, 2022. Salaries and employee benefits increased by \$3.2 million year-over-year due primarily to increased salary expense of \$1.9 million related to new hires and merit increases effective April 1, 2023 and increased health insurance costs of \$1.0 million associated with unusually high claims. Occupancy and equipment expense increased by \$0.2 million, data processing expense increased by \$0.4 million, and FDIC assessments increased by \$0.2 million. Other miscellaneous expenses, such as loan service fees, dues and licenses, check fraud expenses, employee benefit plan expense, and miscellaneous expenses increased by \$1.7 million.

Net Interest Income

Net interest income is our largest source of operating revenue. Net interest income is the difference between the interest that we earn on our interest-earning assets and the interest expense we incur on our interest-bearing liabilities. For analytical and discussion purposes, net interest income is adjusted to a fully tax equivalent ("FTE") basis to facilitate performance comparisons between taxable and tax-exempt assets by increasing tax-exempt income by an amount equal to the federal income taxes that would have been paid if this income were taxable at the statutorily applicable rate. This is a non-GAAP disclosure and management believes it is not materially different than the corresponding GAAP disclosure.

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The tables below summarize net interest income for the nine- and three-month periods ended September 30, 2023 and 2022.

(dollars in thousands)	Non-GAAP		GAAP	
	Nine Months Ended		Nine Months Ended	
	September 30, 2023	2022	September 30, 2023	2022
Interest income	\$ 59,531	\$ 45,771	\$ 58,965	\$ 45,063
Interest expense	16,289	2,610	16,289	2,610
Net interest income	\$ 43,242	\$ 43,161	\$ 42,676	\$ 42,453
Net interest margin %	3.30 %	3.53 %	3.26 %	3.47 %

(dollars in thousands)	Three Months Ended		Three Months Ended	
	September 30,		September 30,	
	2023	2022	2023	2022
Interest income	\$ 21,276	\$ 16,416	\$ 21,164	\$ 16,185
Interest expense	7,180	1,044	7,180	1,044
Net interest income	\$ 14,096	\$ 15,372	\$ 13,984	\$ 15,141
Net interest margin %	3.12 %	3.66 %	3.09 %	3.61 %

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The following tables set forth the average balances, net interest income and expense, and average yields and rates of our interest-earning assets and interest-bearing liabilities for the nine- and three-month periods ended September 30, 2023 and 2022:

(dollars in thousands)	Nine Months Ended September 30,					
	2023		2022			
	Average Balance	Average Interest	Average Yield/Rate	Average Balance	Average Interest	Average Yield/Rate
Assets						
Loans	\$ 1,320,674	\$ 50,323	5.09 %	\$ 1,203,650	\$ 39,399	4.38 %
Investment Securities:						
Taxable	337,014	5,339	2.12 %	352,446	4,533	1.72 %
Non taxable	21,963	1,183	7.20 %	27,118	1,494	7.37 %
Total	358,977	6,522	2.43 %	379,564	6,027	2.12 %
Federal funds sold	66,708	2,502	5.01 %	47,173	308	0.87 %
Interest-bearing deposits with other banks	2,827	70	3.31 %	3,564	12	0.45 %
Other interest earning assets	3,643	114	4.18 %	1,027	25	3.25 %
Total earning assets	1,752,829	59,531	4.54 %	1,634,978	45,771	3.74 %
Allowance for loan losses	(16,311)			(15,611)		
Non-earning assets	174,411			166,594		
Total Assets	<u>\$ 1,910,929</u>			<u>\$ 1,785,961</u>		
Liabilities and Shareholders' Equity						
Interest-bearing demand deposits	\$ 358,883	\$ 3,375	1.26 %	\$ 296,069	\$ 369	0.17 %
Interest-bearing money markets	324,583	5,537	2.28 %	294,481	347	0.16 %
Savings deposits	227,179	189	0.11 %	249,596	70	0.04 %
Time deposits - Retail	134,732	1,750	1.74 %	143,734	711	0.66 %
Time deposits - Brokered	46,918	1,849	5.27 %	—	—	— %
Short-term borrowings	51,780	93	0.24 %	62,175	86	0.18 %
Long-term borrowings	89,394	3,496	5.23 %	30,929	1,027	4.44 %
Total interest-bearing liabilities	1,233,469	16,289	1.77 %	1,076,984	2,610	0.32 %
Non-interest-bearing deposits	490,891			540,082		
Other liabilities	31,108			32,057		
Shareholders' Equity	155,461			136,838		
Total Liabilities and Shareholders' Equity	<u>\$ 1,910,929</u>			<u>\$ 1,785,961</u>		
Net interest income and spread	<u>\$ 43,242</u>		2.77 %	<u>\$ 43,161</u>		3.42 %
Net interest margin			<u>3.30 %</u>			3.53 %

(1) The above table reflects the average rates earned or paid stated on an FTE basis assuming a 21% tax rate for 2023 and 2022. Non-GAAP interest income on a fully taxable equivalent was \$566 and \$708, respectively.
(2) Net interest margin is calculated as net interest income divided by average earning assets.
(3) The average yields on investments are based on amortized cost.

(dollars in thousands)	Three Months Ended September 30,					
	2023			2022		
	Average Balance	Interest	Average Yield/Rate	Average Balance	Interest	Average Yield/Rate
Assets						
Loans	\$ 1,363,821	\$ 18,071	5.26 %	\$ 1,240,706	\$ 14,073	4.50 %
Investment Securities:						
Taxable	333,468	1,792	2.13 %	343,581	1,587	1.83 %
Non taxable	13,826	219	6.28 %	26,471	489	7.33 %
Total	347,294	2,011	2.30 %	370,052	2,076	2.23 %
Federal funds sold	75,404	1,093	5.75 %	52,019	251	1.91 %
Interest-bearing deposits with other banks	1,812	25	5.47 %	1,552	7	1.79 %
Other interest earning assets	4,771	76	6.32 %	1,026	9	3.48 %
Total earning assets	1,793,102	21,276	4.71 %	1,665,355	16,416	3.91 %
Allowance for loan losses	(17,110)			(15,715)		
Non-earning assets	178,115			170,092		
Total Assets	<u>\$ 1,954,107</u>			<u>\$ 1,819,732</u>		
Liabilities and Shareholders' Equity						
Interest-bearing demand deposits	\$ 368,409	\$ 1,354	1.46 %	\$ 305,608	\$ 187	0.24 %
Interest-bearing money markets	325,810	2,430	2.96 %	305,185	210	0.27 %
Savings deposits	209,070	54	0.10 %	253,576	34	0.05 %
Time deposits - retail	154,503	918	2.36 %	134,600	190	0.56 %
Time deposits - brokered	68,850	916	5.28 %	—	—	— %
Short-term borrowings	49,190	33	0.27 %	66,172	47	0.28 %
Long-term borrowings	110,929	1,475	5.28 %	30,929	376	4.82 %
Total interest-bearing liabilities	1,286,761	7,180	2.21 %	1,096,070	1,044	0.38 %
Non-interest-bearing deposits	478,673			550,978		
Other liabilities	32,327			37,499		
Shareholders' Equity	156,346			135,186		
Total Liabilities and Shareholders' Equity	<u>\$ 1,954,107</u>			<u>\$ 1,819,733</u>		
Net interest income and spread	<u>\$ 14,096</u>	2.50 %		<u>\$ 15,372</u>	3.53 %	
Net interest margin		3.12 %			3.66 %	

(1) The above table reflects the average rates earned or paid stated on an FTE basis assuming a 21% tax rate for 2023 and 2022. Non-GAAP interest income on a fully taxable equivalent was \$111 and \$232, respectively.

(2) Net interest margin is calculated as net interest income divided by average earning assets.

(3) The average yields on investments are based on amortized cost.

Net interest income, on a non-GAAP, FTE basis, decreased by \$1.3 million for the third quarter of 2023 when compared to the third quarter of 2022. This decrease was driven by an increase of \$6.1 million in interest expense due to an increase of 175 basis points on interest paid on deposit accounts as well as an increase of \$127.7 million in average balances of interest-bearing deposit accounts when compared to the same period of 2022. Increased deposit pricing resulted from the continued pressure on deposits as well as a shift in the deposit portfolio mix from non-interest-bearing deposits to interest-bearing accounts including the Insured Cash Sweep ("ICS") product to ensure full FDIC insurance coverage. In August 2023, the Corporation obtained \$30.0 million of brokered deposits to pre-fund the maturity of a \$30.4 million brokered certificate of deposit that matured in September 2023. Interest income increased by \$4.9 million. Interest income on loans increased by \$4.0 million due to the increase of 76 basis points in overall yield on the loan portfolio as new loans were booked at higher rates as well as adjustable-rate loans repricing in correlation to the rising rate environment and an increase in average balances of \$123.1 million. Investment income decreased by \$0.1 million as cashflow from the portfolio was used to fund higher yielding loans. The net interest margin for the three months ended September 30, 2023 was 3.12%, compared to 3.66% for the three months ended September 30, 2022.

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Comparing the nine months ended September 30, 2023 to the nine months ended September 30, 2022, net interest income, on a non-GAAP, FTE basis, increased by \$0.1 million. Interest income increased by \$13.8 million and interest expense increased by \$13.7 million. The yield on earning assets increased 80 basis points to 4.54% during the first nine months of 2023 compared to 3.74% during the same period of 2022 in correlation with the rising interest rate environment and new loans booked at higher rates. Interest expense on deposits increased \$11.2 million while the average balances increased \$108.4 million and interest on long-term borrowings increased \$2.5 million related to \$80.0 million in Federal Home Loan Bank ("FHLB") borrowings obtained during the first quarter of 2023 and an increase in interest rates on variable rate trust preferred borrowings. The increased interest expense resulted in an overall increase of 145 basis points on interest bearing liabilities. The net interest margin for the nine months ended September 30, 2023 was 3.30% compared to 3.53% for the nine months ended September 30, 2022.

The following table sets forth an analysis of volume and rate changes in interest income and interest expense for our average interest-earning assets and average interest-bearing liabilities for the nine- and three-month periods ended September 30, 2023 and 2022:

(in thousands and tax equivalent basis)	For the Nine months ended September 30, 2023 compared to the Nine months ended September 30, 2022		
	Volume	Rate	Net
Interest Income:			
Loans	\$ 3,841	\$ 7,083	\$ 10,924
Taxable Investments	(199)	1,005	806
Non-taxable Investments	(283)	(28)	(311)
Federal funds sold	128	2,066	2,194
Interest-bearing deposits	(2)	60	58
Other interest earning assets	64	25	89
Total interest income	3,549	10,211	13,760
Interest Expense:			
Interest-bearing demand deposits	79	2,927	3,006
Interest-bearing money markets	36	5,154	5,190
Savings deposits	(6)	125	119
Time deposits - Retail	(45)	1,084	1,039
Time deposits - Brokered	0	1,849	1,849
Short-term borrowings	(14)	21	7
Long-term borrowings	1,946	523	2,469
Total interest expense	1,996	11,683	13,679
Net interest income	\$ 1,553	\$ (1,472)	\$ 81

(1) The change in interest income/expense due to both volume and rate has been allocated to volume and rate changes in proportion to the relationship of the absolute dollar amounts of the change in each.

(in thousands and tax equivalent basis)	For the Three months ended September 30, 2023 compared to the Three months ended September 30, 2022		
	Volume	Rate	Net
Interest Income:			
Loans	\$ 1,385	\$ 2,613	\$ 3,998
Taxable Investments	(46)	251	205
Non-taxable Investments	(232)	(39)	(270)
Federal funds sold	112	730	842
Interest-bearing deposits	1	18	18
Other interest earning assets	33	34	67
Total interest income	<u>1,253</u>	<u>3,607</u>	<u>4,860</u>
Interest Expense:			
Interest-bearing demand deposits	38	1,129	1,167
Interest-bearing money markets	14	2,206	2,220
Savings deposits	(6)	27	20
Time deposits - Retail	28	700	728
Time deposits - Brokered	0	916	916
Short-term borrowings	(12)	(2)	(14)
Long-term borrowings	966	132	1,099
Total interest expense	<u>1,028</u>	<u>5,108</u>	<u>6,136</u>
Net interest income	<u>\$ 225</u>	<u>\$ (1,501)</u>	<u>\$ (1,276)</u>

(1) The change in interest income/expense due to both volume and rate has been allocated to volume and rate changes in proportion to the relationship of the absolute dollar amounts of the change in each.

Provision for Credit Losses

Specific allocations have been made for loans where management has determined that the collateral supporting the loans is not adequate to cover the loan balance, and the qualitative factors affecting the estimated allowance for credit losses ("ACL") and allowance for loan losses ("ALL") have been adjusted based on the current economic environment and the characteristics of the loan portfolio. Net provision expense was \$1.2 million and \$0.3 million for the nine-month and three-month periods ending September 30, 2023, respectively, compared to net provision expense/(credit) of \$0.1 million and (\$0.1) million for the nine-month and three-month periods ending September 30, 2022. The increases in provision expense year-over-year were primarily driven by strong growth in our loan portfolio during 2023 as well as increases in qualitative risk factors related to increased economic uncertainty during 2023.

Other Income

The composition of other operating income for the nine- and three-month periods ended September 30, 2023 and 2022 is illustrated in the following table:

(in thousands)	Income as % of Total Other Income		Income as % of Total Other Income	
	Nine Months Ended September 30,		Three Months Ended September 30,	
	2023	2022	2023	2022
Service charges on deposit accounts	\$ 1,631	12%	\$ 1,451	11%
Other service charges	706	5%	686	5%
Trust department	6,134	45%	6,238	46%
Debit card income	2,981	22%	2,922	22%
Bank owned life insurance	936	7%	891	7%
Brokerage commissions	800	6%	805	6%
Other income	350	3%	406	3%
	<u>\$ 13,538</u>	<u>100%</u>	<u>\$ 13,399</u>	<u>100%</u>
	<u>\$ 4,716</u>	<u>100%</u>	<u>\$ 4,604</u>	<u>100%</u>

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Other Operating Expenses

The composition of other operating expenses for the nine- and three-month periods ended September 30, 2023 and 2022 is illustrated in the following table:

(in thousands)	Expense as % of Total Other Operating Expenses				Expense as % of Total Other Operating Expenses			
	Nine Months Ended September 30,				Three Months Ended September 30,			
	2023	2022	2023	2022	2023	2022	2023	2022
Salaries and employee benefits	\$ 21,112	56%	\$ 17,891	57%	\$ 6,957	54%	\$ 6,130	59%
FDIC premiums	724	2%	479	2%	254	2%	150	2%
Equipment	3,168	8%	3,110	10%	1,029	8%	1,037	10%
Occupancy expense of premises	2,274	6%	2,172	7%	747	6%	734	7%
Data processing expense	2,926	8%	2,516	8%	1,011	8%	890	9%
Marketing expense	474	1%	409	1%	220	2%	152	1%
Professional services	1,530	4%	873	3%	490	4%	(211)	(2)%
Contract labor	471	1%	482	2%	173	1%	159	2%
Telephone	341	1%	365	1%	115	1%	112	1%
Other real estate owned	281	1%	375	1%	139	1%	128	1%
Investor relations	272	1%	258	1%	83	1%	39	0%
Contributions	217	1%	184	1%	74	1%	121	1%
Other	4,144	11%	2,425	8%	1,493	12%	888	10%
	<u>\$ 37,934</u>	<u>100%</u>	<u>\$ 31,539</u>	<u>100%</u>	<u>\$ 12,785</u>	<u>100%</u>	<u>\$ 10,329</u>	<u>100%</u>

Provision for Income Taxes

In reporting interim financial information, income tax provisions should be determined under the procedures set forth in Financial Accounting Standards Board's Accounting Standards Codification ("ASC") Topic 740, *Income Taxes* (Section 740-270-30). This guidance provides that at the end of each interim period, an entity should make its best estimate of the effective tax rate expected to be applicable for the full fiscal year. The rate so determined should be used in providing for income taxes on a current year-to-date basis. The effective tax rate should reflect anticipated investment tax credits, capital gains rates, and other available tax planning alternatives. In arriving at this effective tax rate, however, no effect should be included for the tax related to significant, unusual or extraordinary items that will be separately reported or reported net of their related tax effect in reports for the interim period or for the fiscal year.

The effective income tax rates as a percentage of income for the nine months ended September 30, 2023 and September 30, 2022 were 23.6% and 25.8%, respectively. The decrease in the tax rate for the 2023 period was primarily related to a new low-income housing tax credit investment in 2022 that began generating tax credits during the fourth quarter of 2022. This tax credit will continue through 2032.

FINANCIAL CONDITION

Balance Sheet Overview

Total assets at September 30, 2023 were \$1.9 billion, representing an \$80.0 million increase since December 31, 2022. During the first nine months of 2023, cash and interest-bearing deposits in other banks increased by \$6.3 million as a result of management's strategic decision to obtain \$61.1 million in brokered certificates of deposit and \$80.0 million in FHLB borrowings during the first quarter of 2023 to strengthen on-balance sheet liquidity. The increase in cash obtained from this strategic decision was partially offset by the funding of strong loan growth in 2023. The investment portfolio decreased by \$31.5 million since December 31, 2022. Management elected to allow a \$17.8 million non-rated municipal tax increment funding bond to be called at par to increase on-balance sheet liquidity to fund future loan growth. Additional decreases in the investment portfolio were primarily associated with normal principal amortization. Loans increased by \$100.5 million since December 31, 2022 due primarily to growth in the commercial and consumer mortgage portfolios. Other assets, including deferred taxes, premises and equipment, and accrued

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interest receivable, increased by \$2.1 million as deferred tax assets increased by \$2.4 million, equity investments increased by \$1.1 million, and pension assets decreased by \$0.5 million.

Total liabilities at September 30, 2023 were \$1.8 billion, representing a \$76.9 million increase since December 31, 2022. Total deposits increased by \$4.3 million since December 31, 2022. Total certificates of deposit increased by \$100.5 million primarily due to an increase of \$60.6 million in brokered certificates of deposits and \$39.9 in retail certificates of deposit. Interest-bearing demand deposits also increased by \$54.1 million due to a shift in the deposit portfolio mix from non-interest-bearing deposits to interest-bearing accounts including the ICS product to ensure full FDIC insurance coverage as well as a new municipal customer bringing approximately \$40.0 million new deposits during the year. These increases were offset by decreases in non-interest-bearing deposits of \$76.9 million and savings and money market accounts of \$73.4 million. Short term borrowings decreased by \$11.2 million since December 31, 2022 primarily due to one municipal customer moving funds from an overnight investment product to a non-interest bearing deposit product in 2023. Long term borrowings increased by \$80.0 million in the first nine months of 2023 when compared to December 31, 2022 due to the acquisition of \$80.0 million in FHLB borrowings.

Loan Portfolio

The following table presents the composition of our loan portfolio at the dates indicated:

(dollars in thousands)	September 30, 2023	December 31, 2022
Commercial real estate	\$ 491,284	36%
Acquisition and development	79,796	6%
Commercial and industrial *	254,650	18%
Residential mortgage	491,686	36%
Consumer	62,603	4%
Total Loans	<u>\$ 1,380,019</u>	<u>100%</u>

Outstanding loans of \$1.4 billion at September 30, 2023 reflected growth of \$100.5 million for the first nine months of 2023. Since December 31, 2022, commercial real estate loans increased by \$32.5 million, acquisition and development loans increased by \$9.2 million and commercial and industrial loans increased by \$9.3 million. Growth in the commercial portfolios was driven by increased activity with existing clients as well as cultivating new business relationships. Residential mortgage loans increased \$47.3 million related to management's strategic decision to book new mortgage loans at higher rates to our in-house portfolio. The consumer loan portfolio increased slightly by \$2.3 million.

New commercial loan production for the three months ended September 30, 2023 was approximately \$40.3 million. The pipeline of commercial loans as of September 30, 2023 was \$41.7 million. At September 30, 2023, unfunded, committed commercial construction loans totaled approximately \$40.6 million. Commercial amortization and payoffs were approximately \$144.6 million through September 30, 2023 due primarily to pay-offs of short-term commercial loans as well as normal amortizations of the commercial loan portfolio.

New consumer mortgage loan production for the third quarter of 2023 was approximately \$27.5 million, with most of this production comprised of in-house loans. The pipeline of in-house, portfolio loans as of September 30, 2023, was \$13.5 million. The residential mortgage production level normalized in the third quarter of 2023 due to the increasing interest rates. Unfunded commitments related to residential construction loans totaled \$20.5 million on September 30, 2023. Management began shifting more activity towards the secondary market in the second and third quarters to reduce the need for additional funding.

Non-accrual loans totaled \$3.5 million at September 30, 2023 and December 31, 2022. Other real estate owned ("OREO") balances increased by \$0.1 million since December 31, 2022 due to the addition of a new OREO property during the second quarter, which was partially offset by a sale of an OREO property held by the Bank at December 31, 2022.

[Table of Contents](#)*Risk Elements of Loan Portfolio*

The following table presents the risk elements of our loan portfolio at the dates indicated. Management is not aware of any potential problem loans other than those listed in this table or discussed below.

(dollars in thousands)	September 30, 2023	% of Applicable Portfolio	December 31, 2022	% of Applicable Portfolio
Non-accrual loans:				
Commercial real estate	\$ —	0.00%	\$ 145	0.03%
Acquisition and development	120	0.15%	146	0.21%
Residential mortgage	3,285	0.67%	3,204	0.72%
Consumer	74	0.12%	—	0.00%
Total non-accrual loans	<u>\$ 3,479</u>	0.25%	<u>\$ 3,495</u>	0.27%
Accruing Loans Past Due 90 days or more:				
Residential mortgage	\$ 86		\$ 282	
Consumer	59		25	
Total loans past due 90 days or more	<u>\$ 145</u>		<u>\$ 307</u>	
Total non-accrual and accruing loans past due 90 days or more	<u>\$ 3,624</u>		<u>\$ 3,802</u>	
Other real estate owned	\$ 4,878		\$ 4,733	
Total Non-performing assets	<u>\$ 8,502</u>		<u>\$ 8,535</u>	
Non-accrual loans to total loans (as %)	0.25%		0.27%	
Non-performing loans to total loans (as %)	0.26%		0.30%	
Non-performing assets to total assets (as %)	0.44%		0.46%	
Allowance for credit/loan losses to non-accrual loans (as %)	492.84%		418.77%	
Allowance for credit/loan losses to non-performing assets (as %)	201.67%		171.48%	

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Allowance for Credit Losses

The ACL represents an amount which, in management's judgment, is adequate to absorb expected credit losses over the life of outstanding loans as of the balance sheet date based on the evaluation of current risk characteristics of the loan portfolio, past events, current conditions, reasonable and supportable forecasts of future economic conditions and prepayment experience.

The ACL is measured and recorded upon the initial recognition of a financial asset. The ACL is reduced by charge-offs, net of recoveries of previous losses, and is increased by a provision or decreased by a recovery for credit losses, which is recorded as a current period operating expense.

Determination of an appropriate ACL is inherently complex and requires the use of highly subjective estimates. The reasonableness of the ACL is reviewed quarterly by management.

Management believes it uses relevant information available to make determination about the ACL and that it has established the existing allowance in accordance with GAAP. However, the determination of the ACL requires significant judgment, and estimates of expected credit losses in the loan portfolio can vary from the amounts actually observed. While management uses available information to recognize expected credit losses, future additions to the ACL may be necessary based on changes in the loans comprising the portfolio, changes in the current and forecasted economic conditions, changes to the interest rate environment which may directly impact prepayment and curtailment rate assumptions, and changes in the financial condition of borrowers.

The ACL "base case" model is derived from various economic forecasts provided by widely recognized sources. Management evaluates the variability of market conditions by examining the peak and trough of economic cycles. These peaks and troughs are used to stress the base case model to develop a range of potential outcomes. Management then determines the appropriate reserve through an evaluation of these various outcomes relative to current economic conditions and known risks in the portfolio. Management enhances its calculation with the use of Moody's economic forecast data to provide additional support to substantiate its ACL.

The following table presents a summary of the activity in the ACL and ALL for the nine-month periods ended September 30:

(dollars in thousands)	2023	2022
Balance, January 1	\$ 14,636	\$ 15,955
Impact of CECL Adoption	2,066	—
Charge-offs:		
Commercial real estate	(87)	—
Acquisition and development	—	(20)
Commercial and industrial	(301)	(134)
Residential mortgage	(55)	(34)
Consumer	(681)	(726)
Total charge-offs	(1,124)	(914)
Recoveries:		
Commercial real estate	5	1
Acquisition and development	8	21
Commercial and industrial	176	92
Residential mortgage	56	172
Consumer	153	117
Total recoveries	398	403
Net losses	(726)	(511)
Credit/loan loss expense	1,170	97
Balance at end of period	\$ 17,146	\$ 15,541
Allowance for credit/loan losses to gross loans outstanding (as %)	1.24 %	1.22 %

Net (Charge-offs)/Recoveries as a % of Average Applicable Portfolio

	2023	2022
Commercial real estate	(0.02)%	0.00%
Acquisition and development	0.01%	0.00%
Commercial and industrial	(0.07)%	(0.02)%
Residential mortgage	0.00%	0.04%
Consumer	(1.15)%	(1.28)%

Investment Securities

At September 30, 2023, the total amortized cost basis of the available-for-sale investment portfolio was \$144.5 million, compared to a fair value of \$114.4 million. Unrealized gains and losses on securities available-for-sale are reflected in accumulated other comprehensive loss, a component of shareholders' equity. The amortized cost basis of the held to maturity portfolio was \$215.7 million, compared to a fair value of \$176.8 million.

The following table presents the composition of our securities portfolio at amortized cost and fair values at the dates indicated:

(dollars in thousands)	September 30, 2023			December 31, 2022		
	Amortized Cost	Fair Value (FV)	FV as % of Total	Amortized Cost	Fair Value (FV)	FV as % of Total
Securities Available for Sale:						
U.S. government agencies	\$ 11,020	\$ 9,360	9%	\$ 11,044	\$ 9,462	8%
Residential mortgage-backed agencies	42,073	33,369	29%	45,052	37,401	30%
Commercial mortgage-backed agencies	36,722	27,055	24%	37,393	30,732	23%
Collateralized mortgage obligations	24,223	18,987	17%	25,828	21,044	17%
Obligations of state and political subdivisions	10,832	10,066	9%	10,848	10,492	8%
Corporate bonds	1,000	749	1%	1,000	887	1%
Collateralized debt obligations	18,670	14,784	13%	18,664	15,871	13%
Total available for sale	<u><u>\$ 144,540</u></u>	<u><u>\$ 114,370</u></u>	<u><u>100%</u></u>	<u><u>\$ 149,829</u></u>	<u><u>\$ 125,889</u></u>	<u><u>100%</u></u>
Securities Held to Maturity:						
U.S. treasuries	\$ 37,397	\$ 36,727	21%	\$ 37,204	\$ 35,611	18%
U.S. government agencies	67,944	53,533	30%	67,734	54,473	27%
Residential mortgage-backed agencies	30,336	25,841	15%	28,624	25,122	12%
Commercial mortgage-backed agencies	21,454	14,960	8%	22,389	17,821	9%
Collateralized mortgage obligations	53,994	41,880	24%	57,085	47,084	23%
Obligations of state and political subdivisions	4,603	3,885	2%	22,623	22,969	11%
Total held to maturity	<u><u>\$ 215,728</u></u>	<u><u>\$ 176,826</u></u>	<u><u>100%</u></u>	<u><u>\$ 235,659</u></u>	<u><u>\$ 203,080</u></u>	<u><u>100%</u></u>

Total fair value of investment securities available for sale decreased by \$11.5 million since December 31, 2022 due to principal paydowns of the portfolio and declines in the fair value of investment securities of \$5.8 million in the first nine months of 2023. At September 30, 2023, the securities classified as available-for-sale included a net unrealized loss of \$30.2 million, which represents the difference between the fair value and amortized cost of securities in the portfolio.

As discussed in Note 6 to the consolidated financial statements presented elsewhere in this report, the Corporation measures fair market values based on the fair value hierarchy established in ASC Topic 820, *Fair Value Measurements and Disclosures*. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). Level 3 prices or valuation techniques require inputs that are both significant to the valuation assumptions and are not readily observable in the market (i.e. supported with little or no market activity). These Level 3 instruments are valued based on both observable and unobservable inputs derived from the best available data, some of which is internally developed, and considers risk premiums that a market participant would require.

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Approximately \$99.6 million of the available for sale portfolio was valued using Level 2 pricing and had net unrealized losses of \$26.3 million at September 30, 2023. The remaining \$14.8 million of the securities available for sale represents the entire collateralized debt obligation portfolio, which was valued using significant unobservable inputs (Level 3 assets). The \$3.9 million in net unrealized losses associated with this portfolio relates to nine pooled trust preferred securities that comprise the collateralized debt obligation portfolio. Net unrealized losses of \$2.4 million represent non-credit related impairment charges on seven of the securities, while \$1.5 million of unrealized losses relates to two securities which have had no impairment-related charges.

Deposits

The following table presents the composition of our deposits at the dates indicated:

(dollars in thousands)	September 30, 2023		December 31, 2022	
	Balance	Percent	Balance	Percent
Non-interest-bearing demand deposits	\$ 429,691	27%	\$ 506,613	32%
Interest-bearing deposits:				
Demand	381,782	24%	327,685	21%
Money Market	338,153	22%	365,192	23%
Savings deposits	204,389	13%	250,720	16%
Time deposits- retail	160,380	10%	120,523	8%
Time deposits- brokered	60,674	4%	—	0%
Total Deposits	\$ 1,575,069	100%	\$ 1,570,733	100%

Total deposits at September 30, 2023 increased by \$4.3 million when compared to December 31, 2022. In March 2023, the Corporation obtained \$61.1 million in new brokered deposits. In August 2023, the Corporation obtained \$30.0 million of brokered deposits to pre-fund the maturity of a \$30.4 million brokered certificate of deposit that matured in September 2023. In addition, retail certificates of deposits increased by \$39.9 million due primarily to promotional nine-month certificate of deposit product offered in 2023. Interest-bearing demand deposits increased by \$54.1 million due to a shift in the deposit portfolio mix from non-interest-bearing accounts to interest-bearing accounts including the ICS product to ensure full FDIC insurance coverage as well as a new municipal customer bringing approximately \$40.0 million in new deposits during the year. These increases were offset by decreases in non-interest-bearing deposits of \$76.9 million, money market accounts of \$27.0 million, and savings accounts of \$46.3 million due to the shift to interest-bearing demand deposit accounts, two relationships having large deposit withdrawals totaling \$39.5 million during 2023 to fund business activity, the effects of consumer and commercial spending and the competitive market for deposits.

The following table summarizes the percentage of deposits that are insured by deposit insurance or otherwise fully collateralized by securities compared to uninsured deposits as of September 30, 2023 and December 31, 2022.

(dollars in thousands)	September 30, 2023		December 31, 2022	
	Balance	Percent	Balance	Percent
Insured deposits	\$ 1,185,432	75%	\$ 1,076,113	69%
Uninsured but collateralized deposits	204,746	13%	153,067	10%
Uninsured and uncollateralized deposits	184,891	12%	341,553	21%
Total Deposits	\$ 1,575,069	100%	\$ 1,570,733	100%

The following table summarizes the percentage of deposit balances from retail customers compared to business customers as of September 30, 2023 and December 31, 2022.

(dollars in thousands)	September 30, 2023		December 31, 2022	
	Balance	Percent	Balance	Percent
Retail deposits	\$ 801,382	51%	\$ 855,014	54%
Business deposits	773,687	49%	715,719	46%
Total Deposits	\$ 1,575,069	100%	\$ 1,570,733	100%

Deposit outflows experienced in late 2022 and January 2023 were due to the competitive pricing landscape and inflationary spending. Changes in deposit levels were not directly related to the market disruptions during the first nine months of 2023.

Borrowed Funds

The following table presents the composition of our borrowings at the dates indicated:

(in thousands)	September 30, 2023	December 31, 2022
Securities sold under agreements to repurchase	\$ 53,330	\$ 64,565
Total short-term borrowings	<u>53,330</u>	<u>64,565</u>
FHLB advances	\$ 80,000	\$ —
Junior subordinated debt	30,929	30,929
Total long-term borrowings	<u>\$ 110,929</u>	<u>\$ 30,929</u>

Short term borrowings decreased \$11.2 million since December 31, 2022 primarily due to a municipal customer moving funds from an overnight investment product to a non-interest bearing deposit product in 2023.

During the first quarter of 2023, management implemented the Contingency Funding plan and borrowed \$80.0 million from FHLB in two advances with 12- and 18- month maturities.

Liquidity Management

Liquidity is a financial institution's capability to meet customer demands for deposit withdrawals while funding all credit-worthy loans. The factors that determine the institution's liquidity are:

- Reliability and stability of core deposits;
- Cash flow structure and pledging status of investments; and
- Potential for unexpected loan demand.

We actively manage our liquidity position through regular meetings of a sub-committee of executive management, known as the Treasury Team, which looks forward 12 months at 30-day intervals. The measurement is based upon the projection of funds sold or purchased position, along with ratios and trends developed to measure dependence on purchased funds and core growth. Monthly reviews by management and quarterly reviews by the Asset and Liability Committee under prescribed policies and procedures are designed to ensure that we will maintain adequate levels of available funds.

It is our policy to manage our affairs so that liquidity needs are fully satisfied through normal Bank operations. That is, the Bank will manage its liquidity to minimize the need to make unplanned sales of assets or to borrow funds under emergency conditions. The Bank will use funding sources where the interest cost is relatively insensitive to market changes in the short run (periods of one year or less) to satisfy operating cash needs. The remaining normal funding will come from interest-sensitive liabilities, either deposits or borrowed funds. When the marginal cost of needed wholesale funding is lower than the cost of raising this funding in the retail markets, the Corporation may supplement retail funding with external funding sources such as:

1. Unsecured Fed Funds lines of credit with upstream correspondent banks (M&T Bank, Pacific Coast Banker's Bank, PNC Financial Services, Atlantic Community Bankers Bank and Community Bankers Bank).
2. Secured advances with the FHLB, which are collateralized by eligible one to four family residential mortgage loans, home equity lines of credit, commercial real estate loans.
3. Secured line of credit with the Fed Discount Window for use in borrowing funds up to 90 days, using municipal securities as collateral.
4. Brokered deposits, including CDs and money market funds, provide a method to generate deposits quickly. These deposits are strictly rate driven but often provide the most cost-effective means of funding growth.

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5. One Way Buy CDARS/ICS funding – a form of brokered deposits that has become a viable supplement to brokered deposits obtained directly.
6. Bank Term Funding Program – A Federal Reserve program collateralized by government agency securities, if needed.

The following table presents sources of liquidity available to the Corporation as of September 30, 2023.

(dollars in thousands)	Total Availability	Amount Used	Net Availability
Internal Sources			
Excess cash	\$ 59,301	\$ -	\$ 59,301
Unpledged securities	59,933	-	59,933
External Sources			
Federal Reserve (discount window)	11,773	-	11,773
Correspondent unsecured lines of credit	105,000	-	105,000
FHLB	230,277	82,500	147,777
Bank Term Funding Program*	86,226	-	86,226
	\$ 552,510	\$ 82,500	\$ 470,010

*Bank Term Funding Program has been established and eligible securities with a total par balance of \$86.2 million have been pledged to the program as of September 30, 2023

Management is not aware of any demands, commitments, events or uncertainties that are likely to materially affect our ability to meet our future capital requirements.

Due to the market disruption and uncertainties, management implemented the Liquidity Contingency Plan in the first quarter and believes that we have adequate liquidity available to respond to current and anticipated liquidity demands and is not aware of any trends or demands, commitments, events or uncertainties that are likely to materially affect our ability to maintain liquidity at satisfactory levels.

Market Risk and Interest Sensitivity

Our primary market risk is interest rate fluctuation. Interest rate risk results primarily from the traditional banking activities that we engage in, such as gathering deposits and extending loans. Many factors, including economic and financial conditions, movements in interest rates and consumer preferences affect the difference between the interest earned on our assets and the interest paid on our liabilities. Interest rate sensitivity refers to the degree that earnings will be impacted by changes in the prevailing level of interest rates. Interest rate risk arises from mismatches in the repricing or maturity characteristics between interest-bearing assets and liabilities. Management seeks to minimize fluctuating net interest margins, and to enhance consistent growth of net interest income through periods of changing interest rates. Management uses interest sensitivity gap analysis and simulation models to measure and manage these risks. The interest rate sensitivity gap analysis assigns each interest-earning asset and interest-bearing liability to a time frame reflecting its next repricing or maturity date. The differences between total interest-sensitive assets and liabilities at each time interval represent the interest sensitivity gap for that interval. A positive gap generally indicates that rising interest rates during a given interval will increase net interest income, as more assets than liabilities will reprice. A negative gap position would benefit us during a period of declining interest rates.

At September 30, 2023, we were asset sensitive.

Our interest rate risk management goals are:

- Ensure that the Board of Directors and senior management will provide effective oversight and ensure that risks are adequately identified, measured, monitored and controlled;
- Enable dynamic measurement and management of interest rate risk;
- Select strategies that optimize our ability to meet our long-range financial goals while maintaining interest rate risk within policy limits established by the Board of Directors;

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- Use both income and market value oriented techniques to select strategies that optimize the relationship between risk and return; and
- Establish interest rate risk exposure limits for fluctuation in net interest income ("NII"), net income and economic value of equity.

To manage interest sensitivity risk, management formulates guidelines regarding asset generation and pricing, funding sources and pricing, and off-balance sheet commitments. These guidelines are based on management's outlook regarding future interest rate movements, the state of the regional and national economy, and other financial and business risk factors. Management uses computer simulations to measure the effect on net interest income of various interest rate scenarios. Key assumptions used in the computer simulations include cash flows and maturities of interest rate sensitive assets and liabilities, changes in asset volumes and pricing, and management's capital plans. This modeling reflects interest rate changes and the related impact on net interest income over specified periods.

We evaluate the effect of a change in interest rates of +/-100 basis points to +/-400 basis points on both NII and Net Portfolio Value ("NPV") / Economic Value of Equity ("EVE"). We concentrate on NII rather than net income as long as NII remains the significant contributor to net income.

NII modeling allows management to view how changes in interest rates will affect the spread between the yield paid on assets and the cost of deposits and borrowed funds. Unlike traditional Gap modeling, NII modeling takes into account the different degree to which installments in the same repricing period will adjust to a change in interest rates. It also allows the use of different assumptions in a falling versus a rising rate environment. The period considered by the NII modeling is the next eight quarters.

NPV / EVE modeling focuses on the change in the market value of equity. NPV / EVE is defined as the market value of assets less the market value of liabilities plus/minus the market value of any off-balance sheet positions. By effectively looking at the present value of all future cash flows on or off the balance sheet, NPV / EVE modeling takes a longer-term view of interest rate risk. This complements the shorter-term view of the NII modeling.

Measures of NII at risk produced by simulation analysis are indicators of an institution's short-term performance in alternative rate environments. These measures are typically based upon a relatively brief period, usually one year. They do not necessarily indicate the long-term prospects or economic value of the institution.

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Based on the simulation analysis performed at September 30, 2023 and December 31, 2022, management estimated the following changes in net interest income, assuming the indicated rate changes:

(Dollars in thousands)	September 30, 2023	December 31, 2022
+400 basis points	\$ 5,058	\$ 1,112
+300 basis points	\$ 3,768	\$ 225
+200 basis points	\$ 2,502	\$ 173
+100 basis points	\$ 1,263	\$ 121
-100 basis points	\$ (1,303)	\$ (776)
-200 basis points	\$ (3,288)	\$ (3,165)
-300 basis points	\$ (5,859)	\$ (7,382)
-400 basis points	\$ (9,425)	\$ N/A

This estimate is based on assumptions that may be affected by unforeseeable changes in the general interest rate environment and any number of unforeseeable factors. Rates on different assets and liabilities within a single maturity category adjust to changes in interest rates to varying degrees and over varying periods of time. The relationships between lending rates and rates paid on purchased funds are not constant over time. Management can respond to current or anticipated market conditions by lengthening or shortening the Bank's sensitivity through loan repricings or changing its funding mix. The rate of growth in interest-free sources of funds will influence the level of interest-sensitive funding sources. In addition, the absolute level of interest rates will affect the volume of earning assets and funding sources. As a result of these limitations, the interest-sensitive gap is only one factor to be considered in estimating the net interest margin.

Management believes that no material changes in our market risks, our procedures used to evaluate and mitigate those risks, or our actual or simulated sensitivity positions have occurred since December 31, 2022. Our NII simulation analysis as of December 31, 2022 is included in Item 7 of Part II of our Annual Report on Form 10-K for the year ended December 31, 2022 under the heading "Market Risk and Interest Sensitivity".

Impact of Inflation – Our assets and liabilities are primarily monetary in nature, and as such, future changes in prices do not affect the obligations to pay or receive fixed and determinable amounts of money. During inflationary periods, monetary assets lose value in terms of purchasing power and monetary liabilities have corresponding purchasing power gains. The concept of purchasing power is not an adequate indicator of the impact of inflation on financial institutions because it does not incorporate changes in our earnings.

Capital Resources

We require capital to fund loans, satisfy our obligations under the Bank's letters of credit, meet the deposit withdrawal demands of the Bank's customers, and satisfy our other monetary obligations. To the extent that deposits are not adequate to fund our capital requirements, we can rely on the funding sources identified above under the heading "Liquidity Management".

In addition to operational requirements, the Bank is subject to risk-based capital regulations, which were adopted and are monitored by federal banking regulators. These regulations are used to evaluate capital adequacy and require an analysis of an institution's asset risk profile and off-balance sheet exposures, such as unused loan commitments and stand-by letters of credit. Based on capital ratios at September 30, 2023, the Bank was considered to be well-capitalized.

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The following table presents the Bank's capital ratios as of the dates indicated:

	September 30, 2023	December 31, 2022	Required for Capital Adequacy Purposes	Required to be Well Capitalized
Total Capital (to risk-weighted assets)	14.12 %	14.37 %	8.00 %	10.00 %
Tier 1 Capital (to risk-weighted assets)	12.88 %	13.29 %	6.00 %	8.00 %
Common Equity Tier 1 Capital (to risk-weighted assets)	12.88 %	13.29 %	4.50 %	6.50 %
Tier 1 Capital (to average assets)	9.81 %	10.01 %	4.00 %	5.00 %

As of September 30, 2023 and December 31, 2022, the Bank was considered "well capitalized" under the regulatory framework for prompt corrective action. We adopted CECL effective January 1, 2023 and elected not to implement the regulatory agencies' capital transition and instead opted to record the impact to our capital ratios immediately upon implementation.

Effective with the implementation of CECL, a \$2.2 million, net of tax, adjustment was made to retained earnings. The adjustment did not have a material impact to our capital ratios.

Contractual Obligations, Commitments and Off-Balance Sheet Arrangements

Contractual Obligations

The Corporation enters into contractual obligations in the normal course of business. Among these obligations are FHLB advances and junior subordinated debentures, operating lease agreements for banking and subsidiaries' offices and for data processing and telecommunications equipment. Comparing September 30, 2023 to December 31, 2022, short-term borrowings decreased \$11.2 million, driven by a the utilization of cash balances by municipalities related to the overnight investments product. Long-term borrowings increased by \$80.0 million during the quarter due to management's decision to obtain \$80 million in FHLB advances during the first quarter of 2023.

Commitments

Loan commitments are made to accommodate the financial needs of our customers. Letters of credit commit us to make payments on behalf of customers when certain specified future events occur. The credit risks inherent in loan commitments and letters of credit are essentially the same as those involved in extending loans to customers, and these arrangements are subject to our normal credit policies. We are not a party to any other off-balance sheet arrangements.

Commitments to extend credit in the form of consumer, commercial and business at the dates indicated were as follows:

(in thousands)	September 30, 2023	December 31, 2022
Residential mortgage - home equity	\$ 72,739	\$ 70,845
Residential mortgage - construction	19,955	25,499
Commercial	171,636	153,235
Consumer - personal credit lines	4,220	4,323
Standby letters of credit	7,089	14,325
Total	\$ 275,639	\$ 268,227

The increase of \$7.4 million in commitments at September 30, 2023 when compared to December 31, 2022 was due to new business in construction commitments in the commercial portfolio as well as new home equity lines of credit.

Upon adoption of ASC 326 on January 1, 2023, the Corporation recorded an initial increase to the ACL for off-balance sheet exposures of \$0.9 million. Credit loss expense for off-balance sheet credit exposures was a credit of \$14 thousand for the nine-month period ended September 30, 2023.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

The information required by this item is included in Item 2 of Part I of this report under the caption “*Market Risk and Interest Sensitivity*” and in Item 7 of Part II of First United Corporation’s [Annual Report on Form 10-K for the year ended December 31, 2022](#) under the heading “Market Risk and Interest Sensitivity” both of which are incorporated in this Item 3 by reference.

Item 4. Controls and Procedures

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our reports filed under the Securities Exchange Act of 1934 with the SEC, such as this Quarterly Report, is recorded, processed, summarized and reported within the periods specified in those rules and forms, and that such information is accumulated and communicated to our management, including First United Corporation’s principal executive officer (“PEO”) and its principal financial officer (“PFO”), as appropriate, to allow for timely decisions regarding required disclosure. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the control. The design of any system of controls is also based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Over time, controls may become inadequate because of changes in conditions, or the degree of compliance with the policies or procedures may deteriorate.

An evaluation of the effectiveness of these disclosure controls as of September 30, 2023 was carried out under the supervision and with the participation of management, including the PEO and the PFO. Based on that evaluation, management, including the PEO and the PFO, has concluded that our disclosure controls and procedures are, in fact, effective at the reasonable assurance level.

During the nine months ended September 30, 2023, there was no change in our internal control over financial reporting that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Part II. OTHER INFORMATION

Item 1. Legal Proceedings

None.

Item 1A. Risk Factors

The risks and uncertainties to which our financial condition and operations are subject are discussed in detail in Item 1A of Part I of First United Corporation's Annual Report on Form 10-K for the year ended December 31, 2022. Management does not believe that any material changes in our risk factors have occurred since they were last disclosed.

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

The following table summarizes stock repurchases for the three-months ended September 30, 2023:

Issuer Purchases of Equity Securities

Period	Total Number of Shares (or Units) Purchased	Average Price Paid per Share (or Unit)	Total Number of Shares (or Units) Purchased as Part of Publicly Announced Plans or Programs	Maximum Number (or Approximate Dollar Value) of Shares (or Units) that May Yet Be Purchased Under the Plans or Programs (1)
July 2023	—	\$ —	—	—
August 2023	—	\$ —	—	825,000
September 2023	19,298	\$ 16.25	19,298	805,702
Total	19,298	\$ 16.25	19,298	805,702

(1) All shares were purchased in open-market transactions pursuant to First United Corporation's stock repurchase plan that was initially adopted effective August 18, 2023 and publicly announced on August 21, 2023. The plan authorizes the repurchase of up to 825,000 shares of common stock of First United Corporation through open market or private transactions at such times and in such amounts per transactions as the Chairman and Chief Executive Officer of First United Corporation determines to be appropriate.

Item 3. Defaults upon Senior Securities

None.

Item 4. Mine Safety Disclosures

Not Applicable.

Item 5. Other Information

None.

Item 6. Exhibits

The exhibits filed or furnished with this quarterly report are listed in the following Exhibit Index.

Exhibit	Description
31.1	Certifications of the Principal Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act (filed herewith)
31.2	Certifications of the Principal Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act (filed herewith)
32	Certification of the Principal Executive Officer and the Principal Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act (furnished herewith)
101.INS	Inline XBRL Instance Document (filed herewith)
101.SCH	Inline XBRL Taxonomy Extension Schema (filed herewith)
101.CAL	Inline XBRL Taxonomy Extension Calculation Linkbase (filed herewith)
101.DEF	Inline XBRL Taxonomy Extension Definition Linkbase (filed herewith)
101.LAB	Inline XBRL Taxonomy Extension Label Linkbase (filed herewith)
101.PRE	Inline XBRL Taxonomy Extension Presentation Linkbase (filed herewith)
104	The cover page of First United Corporation's Quarterly Report on Form 10Q for the quarter ended September 30, 2023 formatted in Inline XBRL, included within the Exhibit 101 attachments (filed herewith).

SIGNATURES

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

FIRST UNITED CORPORATION

Date: November 9, 2023

/s/ Carissa L. Rodeheaver

Carissa L. Rodeheaver, CPA
Chairman of the Board, President and Chief Executive Officer
(Principal Executive Officer)

Date: November 9, 2023

/s/ Tonya K. Sturm

Tonya K. Sturm, Senior Vice President,
Chief Financial Officer
(Principal Financial Officer and Principal Accounting Officer)

**Certifications of the Principal Executive Officer
Pursuant to Securities Exchange Act Rules 13a-14 and 15d-14
As adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002**

I, Carissa L. Rodeheaver, certify that:

1. I have reviewed this quarterly report on Form 10-Q of First United Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 9, 2023

/s/ Carissa L. Rodeheaver

Carissa L. Rodeheaver, CPA
Chairman of the Board, President and Chief Executive Officer
(Principal Executive Officer)

**Certifications of the Principal Financial Officer
Pursuant to Securities Exchange Act Rules 13a-14 and 15d-14
As adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002**

I, Tonya K. Sturm, certify that:

1. I have reviewed this quarterly report on Form 10-Q of First United Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 9, 2023

/s/ Tonya K. Sturm

Tonya K. Sturm, Senior Vice President,
Chief Financial Officer
(Principal Financial Officer)

**Certification of Periodic Report
Pursuant to 18 U.S.C. § Section 1350
As adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002**

Pursuant to, and for purposes only of, 18 U.S.C. § 1350, each of the undersigned hereby certifies that (i) the Quarterly Report of First United Corporation on Form 10-Q for the quarter ended September 30, 2023 filed with the Securities and Exchange Commission (the "Report") fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, and (ii) information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of First United Corporation.

Date: November 9, 2023

/s/ Carissa L. Rodeheaver

Carissa L. Rodeheaver, CPA

Chairman of the Board, President and Chief Executive Officer
(Principal Executive Officer)

Date: November 9, 2023

/s/ Tonya K. Sturm

Tonya K. Sturm, Senior Vice President,

Chief Financial Officer

(Principal Financial Officer)
