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DELTA REPORT

10-Q

FRAF - FRANKLIN FINANCIAL SERVIC

10-Q - SEPTEMBER 30, 2023 COMPARED TO 10-Q - JUNE 30, 2023

The following comparison report has been automatically generated

TOTAL DELTAS	792
CHANGES	369
DELETIONS	208
ADDITIONS	215

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended June 30, 2023 September 30, 2023

or

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

For the transition period from__________ to___________

Commission file number 001-38884

FRANKLIN FINANCIAL SERVICES CORPORATION

(Exact name of registrant as specified in its charter)

Pennsylvania	25-1440803
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
1500 Nitterhouse Drive, Chambersburg, PA	17201-0819
(Address of principal executive offices)	(Zip Code)

(717) 264-6116

(Registrant's telephone number, including area code)

Not Applicable

(Former name, former address and former fiscal year, if changed since last report)

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

Title of class	Symbol	Name of exchange on which registered
Common stock	FRAF	Nasdaq Capital Market

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

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

Large accelerated filer ¨ Accelerated filer ¨ Non-accelerated filer x Smaller reporting company x Emerging growth company ¨

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

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

There were 4,350,689 4,361,559 outstanding shares of the Registrant’s common stock as of July 31, 2023 October 31, 2023.

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Part I FINANCIAL INFORMATION

Item 1. Financial Statements

Consolidated Balance Sheets

(Dollars in thousands, except share and per share data)	*(unaudited)* **June 30, 2023**	December 31, 2022	*(unaudited)* **September 30, 2023**	December 31, 2022
Assets				
Cash and due from banks	$ **17,861**	$ 17,883	$ **20,113**	$ 17,883
Short-term interest-earning deposits in other banks	**46,971**	47,016	**53,840**	47,016
Total cash and cash equivalents	**64,832**	64,899	**73,953**	64,899
Long-term interest-earning deposits in other banks	**8,978**	13,975	**7,728**	13,975
Debt securities available for sale, at fair value	**439,471**	486,836	**458,276**	486,836
Equity securities	**380**	411	**386**	411
Restricted stock	**694**	644	**2,294**	644
Loans held for sale	**126**	283	**792**	283
Loans	**1,145,162**	1,051,041	**1,206,850**	1,051,041

Allowance for credit losses	**(14,615)**	(14,175)	**(15,528)**	(14,175)
Net Loans	**1,130,547**	1,036,866	**1,191,322**	1,036,866
Premises and equipment, net	**29,279**	30,026	**29,026**	30,026
Right of use asset	**4,982**	6,010	**4,830**	6,010
Bank owned life insurance	**22,530**	22,311	**22,644**	22,311
Goodwill	**9,016**	9,016	**9,016**	9,016
Deferred tax asset, net	**14,730**	15,630	**14,877**	15,630
Other assets	**10,600**	12,672	**12,766**	12,672
Total assets	**$ 1,736,165**	$ 1,699,579	**$1,827,910**	$1,699,579
Liabilities				
Deposits				
Noninterest-bearing checking	**$ 287,385**	$ 299,231	**$ 295,181**	$ 299,231
Money management, savings, and interest checking	**1,136,008**	1,194,827	**1,161,927**	1,194,827
Time	**89,742**	57,390	**110,306**	57,390
Total deposits	**1,513,135**	1,551,448	**1,567,414**	1,551,448
Short-term borrowings	**70,000**	—		
Federal Reserve Bank borrowings			**70,000**	—
FHLB advances			**40,000**	—
Subordinate notes	**19,643**	19,623	**19,653**	19,623
Lease liability	**5,104**	6,144	**4,960**	6,144
Other liabilities	**8,513**	8,167	**11,114**	8,167
Total liabilities	**1,616,395**	1,585,382	**1,713,141**	1,585,382
Commitments and contingent liabilities				
Shareholders' equity				
Common stock, $1 par value per share,15,000,000 shares authorized with				
4,710,972 shares issued and 4,349,988 shares outstanding at June 30, 2023 and				
4,710,972 shares issued and 4,361,511 shares outstanding at September 30, 2023 and				
4,710,972 shares issued and 4,390,397 shares outstanding at December 31, 2022	**4,711**	4,711	**4,711**	4,711
Capital stock no par value, 5,000,000 shares authorized with no				
shares issued and outstanding	**—**	—	**—**	—
Additional paid-in capital	**43,422**	43,535	**43,512**	43,535
Retained earnings	**129,452**	125,892	**131,919**	125,892
Accumulated other comprehensive loss	**(47,961)**	(51,287)	**(55,834)**	(51,287)
Treasury stock, 360,984 shares at June 30, 2023 and 320,575 shares at				
Treasury stock, 349,461 shares at September 30, 2023 and 320,575 shares at				
December 31, 2022, at cost	**(9,854)**	(8,654)	**(9,539)**	(8,654)
Total shareholders' equity	**119,770**	114,197	**114,769**	114,197
Total liabilities and shareholders' equity	**$ 1,736,165**	$ 1,699,579	**$1,827,910**	$1,699,579

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

Consolidated Statements of Income

(Dollars in thousands, except per share data) (unaudited)	For the Three Months Ended June 30,		For the Six Months Ended June 30,		For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2023	2022	**2023**	2022	**2023**	2022	**2023**	2022
Interest income								

Loans, including fees	**$ 14,069**	$ 9,754	**$ 26,405**	$ 18,821	**$15,308**	$10,767	**$41,712**	$29,589
Interest and dividends on investments:								
Taxable interest	**3,327**	2,168	**6,777**	4,010	**3,838**	2,728	**10,615**	6,739
Tax exempt interest	**313**	524	**679**	1,049	**277**	521	**956**	1,570
Dividend income	**11**	8	**19**	9	**11**	5	**30**	14
Interesting-earnings deposits in other banks	**791**	421	**1,214**	520	**720**	1,022	**1,934**	1,542
Total interest income	**18,511**	12,875	**35,094**	24,409	**20,154**	15,043	**55,247**	39,454
Interest expense								
Deposits	**4,378**	504	**7,808**	967	**5,127**	717	**12,934**	1,684
Short-term borrowings	**677**	—	**728**	—				
Federal Reserve Bank borrowings					**789**	—	**1,518**	—
FHLB advances					**267**	—	**267**	—
Subordinate notes	**261**	260	**526**	523	**264**	263	**790**	787
Total interest expense	**5,316**	764	**9,062**	1,490	**6,447**	980	**15,509**	2,471
Net interest income	**13,195**	12,111	**26,032**	22,919	**13,707**	14,063	**39,738**	36,983
Provision for credit losses - loans	**524**	—	**991**	—	**866**	—	**1,857**	—
Provision for credit losses - unfunded commitments	**8**	—	**70**	—	**9**	—	**79**	—
Net interest income after credit loss expense	**12,663**	12,111	**24,971**	22,919	**12,832**	14,063	**37,802**	36,983
Noninterest income								
Investment and trust services fees	**1,959**	1,918	**3,793**	3,746	**1,783**	1,661	**5,576**	5,407
Loan service charges	**120**	240	**422**	356	**235**	177	**658**	533
Gain on sale of loans	**45**	255	**118**	509	**33**	183	**150**	692
Deposit service charges and fees	**616**	634	**1,199**	1,257	**649**	629	**1,848**	1,885
Other service charges and fees	**430**	437	**862**	849	**472**	443	**1,334**	1,293
Debit card income	**547**	438	**1,050**	896	**568**	497	**1,618**	1,393
Increase in cash surrender value of Bank owned life insurance	**111**	109	**220**	217	**114**	109	**333**	326
Net losses on sales of debt securities	**(517)**	(19)	**(1,119)**	(19)	**—**	(15)	**(1,119)**	(34)
Change in fair value of equity securities	**(8)**	4	**(32)**	15	**7**	(61)	**(25)**	(46)
Other	**226**	75	**241**	150	**152**	40	**393**	190
Total noninterest income	**3,529**	4,091	**6,754**	7,976	**4,013**	3,663	**10,766**	11,639
Noninterest Expense								
Salaries and employee benefits	**7,283**	7,045	**14,220**	13,410	**6,982**	7,050	**21,202**	20,403
Net occupancy	**1,112**	979	**2,222**	1,952	**1,093**	1,124	**3,315**	3,077
Marketing and advertising	**550**	460	**1,069**	957	**531**	433	**1,600**	1,391
Legal and professional	**454**	484	**1,005**	999	**588**	581	**1,593**	1,580
Data processing	**1,118**	1,261	**2,178**	2,398	**1,300**	1,146	**3,478**	3,544
Pennsylvania bank shares tax	**174**	335	**397**	478	**174**	335	**571**	813
FDIC Insurance	**198**	170	**380**	353	**230**	197	**610**	550
ATM/debit card processing	**307**	360	**601**	706	**320**	359	**920**	1,065
Telecommunications	**98**	106	**197**	199	**103**	114	**300**	313
Nonservice pension	**(29)**	69	**(59)**	138	**(29)**	69	**(88)**	207
Lease termination	**495**	—	**495**	—	**—**	—	**495**	—
Other	**888**	760	**1,962**	1,706	**906**	792	**2,868**	2,553
Total noninterest expense	**12,648**	12,029	**24,667**	23,296	**12,198**	12,200	**36,864**	35,496
Income before federal income taxes	**3,544**	4,173	**7,058**	7,599	**4,647**	5,526	**11,704**	13,126
Federal income tax expense	**568**	595	**790**	1,009	**788**	895	**1,577**	1,905
Net income	**$ 2,976**	$ 3,578	**$ 6,268**	$ 6,590	**$ 3,859**	$ 4,631	**$10,127**	$11,221

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Per share								
Basic earnings per share	**$ 0.68**	$ 0.80	**$ 1.43**	$ 1.48	**$ 0.89**	$ 1.05	**$ 2.31**	$ 2.53
Diluted earnings per share	**$ 0.68**	$ 0.80	**$ 1.42**	$ 1.47	**$ 0.88**	$ 1.05	**$ 2.31**	$ 2.52

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

Consolidated Statements of Comprehensive Income (Loss)

	For the Three Months Ended June 30,		For the Six Months Ended June 30,		For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
(Dollars in thousands) (unaudited)	**2023**	2022	**2023**	2022	**2023**	2022	**2023**	2022
Net Income	**$ 2,976**	$ 3,578	**$ 6,268**	$ 6,590	**$ 3,859**	$ 4,631	**$10,127**	$ 11,221
Debt Securities:								
Unrealized (losses) gains arising during the period	**(5,534)**	(20,965)	**3,092**	(48,683)				
Unrealized losses arising during the period					**(9,966)**	(20,409)	**(6,874)**	(69,090)
Reclassification adjustment for losses included in net income (1)	**517**	19	**1,119**	19	**—**	15	**1,119**	34
Net unrealized (losses)/gains	**(5,017)**	(20,946)	**4,211**	(48,664)				
Net unrealized losses					**(9,966)**	(20,394)	**(5,755)**	(69,056)
Tax effect	**1,052**	4,400	**(885)**	10,221	**2,093**	4,283	**1,208**	14,502
Net of tax amount	**(3,965)**	(16,546)	**3,326**	(38,443)	**(7,873)**	(16,111)	**(4,547)**	(54,554)
Total other comprehensive (loss) income	**(3,965)**	(16,546)	**3,326**	(38,443)				
Total other comprehensive loss					**(7,873)**	(16,111)	**(4,547)**	(54,554)
Total Comprehensive (Loss) Income	**$ (989)**	$ (12,968)	**$ 9,594**	$ (31,853)	**$(4,014)**	$(11,480)	**$ 5,580**	$(43,333)
(1) Reclassified to net losses on sales of debt securities								

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

Consolidated Statements of Changes in Shareholders' Equity

For the three and six first nine months ended June 30, 2023 September 30, 2023 and 2022

(Dollars in thousands, except per share data) (unaudited)	Shares Outstanding	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Treasury Stock	Total	Shares Outstanding	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Treasury Stock	Total
Balance at April 1, 2023	**4,402,675**	**$ 4,711**	**$ 43,356**	**$ 127,877**	**$ (43,996)**	**$ (8,365)**	**$ 123,583**							
Balance at July 1, 2023								**4,349,988**	**$ 4,711**	**$ 43,422**	**$129,452**	**$ (47,961)**	**$(9,854)**	**$119,770**
Net income		**—**	**—**	**2,976**	**—**	**—**	**2,976**		**—**	**—**	**3,859**	**—**	**—**	**3,859**
Other comprehensive income		**—**	**—**	**—**	**(3,965)**	**—**	**(3,965)**		**—**	**—**	**—**	**(7,873)**	**—**	**(7,873)**
Cash dividends declared, $0.32 per share		**—**	**—**	**(1,401)**	**—**	**—**	**(1,401)**		**—**	**—**	**(1,392)**	**—**	**—**	**(1,392)**
Treasury shares issued under dividend reinvestment plan								**9,613**	**—**	**13**	**—**	**—**	**263**	**276**
Stock Compensation Plans:														
Treasury shares issued								**1,910**	**—**	**(36)**	**—**	**—**	**52**	**16**

Compensation expense									—	113	—	—	—	113
Balance at September 30, 2023								**4,361,511$**	**4,711 $**	**43,512 $**	**131,919 $**	**(55,834)$**	**(9,539)$**	**114,769**
Balance at January 1, 2023								**4,390,397$**	**4,711 $**	**43,535 $**	**125,892 $**	**(51,287)$**	**(8,654)$**	**114,197**
Cumulative change in accounting principle, net of tax									—	—	98	—	—	98
Net income									—	—	10,127	—	—	10,127
Other comprehensive income									—	—	—	(4,547)	—	(4,547)
Cash dividends declared, $0.96 per share									—	—	(4,198)	—	—	(4,198)
Acquisition of treasury stock	(74,306)	—	—	—	—	(2,078)	(2,078)	(84,414)	—	—	—	—	(2,394)	(2,394)
Treasury shares issued under dividend reinvestment plan	20,195	—	(17)	—	—	550	533	38,292	—	45	—	—	1,042	1,087
Stock Compensation Plans:														
Treasury shares issued	1,424	—	(35)	—	—	39	4	17,236	—	(434)	—	—	467	33
Compensation expense		—	118	—	—	—	118		—	366	—	—	—	366
Balance at June 30, 2023	**4,349,988 $**	**4,711 $**	**43,422 $**	**129,452 $**	**(47,961) $**	**(9,854) $**	**119,770**							
Balance at January 1, 2023	**4,390,397 $**	**4,711 $**	**43,535 $**	**125,892 $**	**(51,287) $**	**(8,654) $**	**114,197**							
Cumulative change in accounting principle, net of tax		—	—	98	—	—	98							
Net income		—	—	6,268	—	—	6,268							
Other comprehensive income		—	—	—	3,326	—	3,326							
Cash dividends declared, $0.64 per share		—	—	(2,806)	—	—	(2,806)							
Acquisition of treasury stock	(84,414)	—	—	—	—	(2,394)	(2,394)							
Treasury shares issued under dividend reinvestment plan	28,679	—	32	—	—	779	811							
Stock Compensation Plans:														
Treasury shares issued	15,326	—	(398)	—	—	415	17							
Compensation expense		—	253	—	—	—	253							
Balance at June 30, 2023	**4,349,988 $**	**4,711 $**	**43,422 $**	**129,452 $**	**(47,961) $**	**(9,854) $**	**119,770**							
Balance at September 30, 2023								**4,361,511$**	**4,711 $**	**43,512 $**	**131,919 $**	**(55,834)$**	**(9,539)$**	**114,769**
Balance at April 1, 2022	**4,456,918 $**	**4,711 $**	**43,077 $**	**118,203 $**	**(22,444) $**	**(6,411) $**	**137,136**							
Balance at July 1, 2022								**4,422,280$**	**4,711 $**	**43,248 $**	**120,354 $**	**(38,990)$**	**(7,526)$**	**121,797**
Net income		—	—	3,578	—	—	3,578		—	—	4,631	—	—	4,631
Other comprehensive income		—	—	—	(16,546)	—	(16,546)		—	—	—	(16,111)	—	(16,111)
Cash dividends declared, $0.32 per share		—	—	(1,427)	—	—	(1,427)		—	—	(1,406)	—	—	(1,406)
Acquisition of treasury stock	(47,431)	—	—	—	—	(1,441)	(1,441)	(38,409)	—	—	—	—	(1,202)	(1,202)
Treasury shares issued under dividend reinvestment plan	11,133	—	49	—	—	284	333	9,245	—	49	—	—	246	295
Stock Compensation Plans:														
Treasury shares issued	1,660	—	(30)	—	—	42	12	2,534	—	(51)	—	—	67	16
Compensation expense		—	152	—	—	—	152		—	131	—	—	—	131
Balance at June 30, 2022	**4,422,280 $**	**4,711 $**	**43,248 $**	**120,354 $**	**(38,990) $**	**(7,526) $**	**121,797**							
Balance at September 30, 2022								**4,395,650$**	**4,711 $**	**43,377 $**	**123,579 $**	**(55,101)$**	**(8,415)$**	**108,151**
Balance at January 1, 2022	**4,441,443 $**	**4,711 $**	**43,085 $**	**116,612 $**	**(547) $**	**(6,796) $**	**157,065**	**4,441,443$**	**4,711 $**	**43,085 $**	**116,612 $**	**(547)$**	**(6,796)$**	**157,065**
Net income		—	—	6,590	—	—	6,590		—	—	11,221	—	—	11,221
Other comprehensive income		—	—	—	(38,443)	—	(38,443)		—	—	—	(54,554)	—	(54,554)

Cash dividends declared, $0.64 per share		—	—	(2,848)	—	—	(2,848)							
Cash dividends declared, $0.96 per share									—	—	(4,254)	—	—	(4,254)
Acquisition of treasury stock	(48,040)	—	—	—	—	(1,461)	(1,461)	(86,449)	—	—	—	—	(2,664)	(2,664)
Treasury shares issued under dividend reinvestment plan	20,512	—	128	—	—	521	649	29,757	—	176	—	—	766	942
Stock Compensation Plans:														
Treasury shares issued	8,365	—	(186)	—	—	210	24	10,899	—	(236)	—	—	279	43
Compensation expense		—	221	—	—	—	221		—	352	—	—	—	352
Balance at June 30, 2022	**4,422,280**	**$ 4,711**	**$ 43,248**	**$ 120,354**	**$ (38,990)**	**$ (7,526)**	**$ 121,797**							
Balance at September 30, 2022								**4,395,650**	**$4,711**	**$43,377**	**$123,579**	**$(55,101)**	**$(8,415)**	**$108,151**

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

Consolidated Statements of Cash Flows

	Six Months Ended June 30,		Nine Months Ended September 30,	
	2023	2022	**2023**	2022
(Dollars in thousands) (unaudited)				
Cash flows from operating activities				
Net income	**$ 6,268**	$ 6,590	**$ 10,127**	$ 11,221
Adjustments to reconcile net income to net cash provided by operating activities:				
Depreciation and amortization	**988**	544	**1,506**	1,049
Net amortization of loans and investment securities	**1,720**	2,121	**1,891**	3,207
Amortization of subordinate debt issuance costs	**20**	17	**30**	27
Provision for credit losses	**1,061**	—	**1,936**	—
Change in fair value of equity securities	**32**	(15)	**25**	46
Realized losses on sales of debt securities	**1,119**	19	**1,119**	34
Loans originated for sale	**(8,341)**	(28,850)	**(10,686)**	(40,342)
Proceeds from sale of loans	**8,616**	30,132	**10,327**	41,512
Gain on sale of loans held for sale	**(118)**	(509)	**(150)**	(692)
Increase in cash surrender value of life insurance	**(220)**	(217)	**(333)**	(326)
Decrease in fair value of derivative	**—**	(13)		
Change in fair value of derivative			**(3)**	(17)
Stock based compensation	**253**	221	**366**	352
Decrease in other assets	**1,573**	606	**1,563**	1,679
Increase (decrease) in other liabilities	**414**	(1,360)	**2,924**	(4)
Net cash provided by operating activities	**13,385**	9,286	**20,642**	17,746
Cash flows from investing activities				
Net decrease (increase) in long-term interest-earning deposits in other banks	**4,997**	(1,984)	**6,247**	(1,984)
Proceeds from sales and calls of investment securities available for sale	**40,117**	82	**40,117**	1,082
Proceeds from maturities and pay-downs of securities available for sale	**16,062**	20,600	**24,779**	31,013
Purchase of investment securities available for sale	**(7,248)**	(51,496)	**(45,419)**	(66,499)
Net increase in restricted stock	**(50)**	(149)	**(1,650)**	(149)
Net increase in loans	**(94,417)**	(35,827)	**(155,677)**	(49,886)
Capital expenditures	**(228)**	(8,584)	**(479)**	(11,007)
Net cash used in investing activities	**(40,767)**	(77,358)	**(132,082)**	(97,430)
Cash flows from financing activities				

Net (decrease) increase in demand deposits, interest-bearing checking, and savings accounts	**(70,665)**	106,000	**(36,950)**	135,019
Net increase (decrease) in time deposits	**32,352**	(11,172)	**52,916**	(14,395)
Net increase in short-term borrowings	**70,000**	—	**110,000**	—
Dividends paid	**(2,806)**	(2,848)	**(4,198)**	(4,254)
Purchase of Treasury shares	**(2,394)**	(1,461)	**(2,394)**	(2,664)
Cash received from option exercises	**17**	24	**33**	43
Treasury shares issued under dividend reinvestment plan	**811**	649	**1,087**	942
Net cash provided by financing activities	**27,315**	91,192	**120,494**	114,691
(Decrease) increase in cash and cash equivalents	**(67)**	23,120		
Increase in cash and cash equivalents			**9,054**	35,007
Cash and cash equivalents at the beginning of the period	**64,899**	175,149	**64,899**	175,149
Cash and cash equivalents at the end of the period	**$ 64,832**	$ 198,269	**$ 73,953**	**$**210,156
Supplemental Disclosures of Cash Flow Information				
Cash paid during the year for:				
Interest on deposits and other borrowed funds	**$ 7,813**	$ 1,503	**$ 12,865**	$ 2,208
Income taxes	**1,316**	43	**1,338**	58
Noncash Activities				
Lease liabilities arising from obtaining right-of-use assets	**$ —**	$ 426	**$ —**	$ 1,867
Noncash extinguishment of lease liability	**537**	—	**537**	—
Noncash decrease in right-of-use asset	**507**	—	**507**	—

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

FRANKLIN FINANCIAL SERVICES CORPORATION and SUBSIDIARIES

UNAUDITED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 1. Basis of Presentation

The consolidated financial statements include the accounts of Franklin Financial Services Corporation (the Corporation), and its wholly owned subsidiaries, Farmers and Merchants Trust Company of Chambersburg (the Bank) and Franklin Future Fund Inc. Farmers and Merchants Trust Company of Chambersburg is a commercial bank that has one wholly owned subsidiary, Franklin Financial Properties Corp. Franklin Financial Properties Corp. holds real estate assets that are leased by the Bank. Franklin Future Fund Inc. is a non-bank investment company. The activities of the non-bank subsidiary are not significant to the consolidated totals. All significant intercompany transactions and account balances have been eliminated.

In the opinion of management, all adjustments (which include only normal recurring adjustments) necessary to present fairly the consolidated financial position, results of operations, and cash flows as of June 30, 2023 September 30, 2023, and for all other periods presented have been made.

Certain information and footnote disclosures normally included in consolidated financial statements prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”) have been condensed or omitted. It is suggested that these consolidated financial statements be read in conjunction with the audited consolidated financial statements and notes thereto included in the Corporation’s 2022 Annual Report on Form 10-K. The consolidated results of operations for the three- and six-month periods first nine-month period ended June 30, 2023 September 30, 2023 are not necessarily indicative of the operating results for the full year. Management has evaluated subsequent events for potential recognition and/or disclosure through the date these consolidated financial statements were issued.

The consolidated balance sheet at December 31, 2022 has been derived from the audited consolidated financial statements at that date but does not include all of the information and footnotes required by GAAP for complete consolidated financial statements.

For purposes of reporting cash flows, cash and cash equivalents include cash and due from banks, interest-bearing deposits in other banks and cash items with original maturities less than 90 days.

Earnings per share are computed based on the weighted average number of shares outstanding during each period end. A reconciliation of the weighted average shares outstanding used to calculate basic earnings per share and diluted earnings per share follows:

(Dollars and shares in thousands, except per share data)	For the Three Months Ended June 30, 2023	For the Three Months Ended June 30, 2022	For the Six Months Ended June 30, 2023	For the Six Months Ended June 30, 2022	For the Three Months Ended September 30, 2023	For the Three Months Ended September 30, 2022	For the Nine Months Ended September 30, 2023	For the Nine Months Ended September 30, 2022
Weighted average shares outstanding (basic)	**4,380**	4,450	**4,388**	4,448	**4,355**	4,401	**4,377**	4,432
Impact of common stock equivalents	**8**	16	**13**	21	**14**	23	**14**	21
Weighted average shares outstanding (diluted)	**4,388**	4,466	**4,401**	4,469	**4,369**	4,424	**4,391**	4,453
Anti-dilutive options excluded from calculation	**74**	30	**25**	30	**49**	29	**49**	30
Net income	**$ 2,976**	$ 3,578	**$ 6,268**	$ 6,590	**$3,859**	$4,631	**$10,127**	$11,221
Basic earnings per share	**$ 0.68**	$ 0.80	**$ 1.43**	$ 1.48	**$ 0.89**	$ 1.05	**$ 2.31**	$ 2.53
Diluted earnings per share	**$ 0.68**	$ 0.80	**$ 1.42**	$ 1.47	**$ 0.88**	$ 1.05	**$ 2.31**	$ 2.52

Note 2. Recent Accounting Pronouncements

Recently adopted accounting standards	Recently adopted accounting standards	Recently adopted accounting standards
ASU 2016-13, Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments		
Description	This standard requires credit losses on most financial assets measured at amortized cost and certain other instruments to be measured using an expected credit loss model (referred to as the current expected credit loss (CECL) model). Under this model, entities will estimate credit losses over the entire contractual term of the instrument (considering estimated prepayments, but not expected extensions or modifications) from the date of initial recognition of that instrument. The ASU replaces the current accounting model for purchased credit impaired loans and debt securities. The allowance for credit losses for purchased financial assets with a more-than insignificant amount of credit deterioration since origination (“PCD assets”), should be determined in a similar manner to other financial assets measured on an amortized cost basis. However, upon initial recognition, the allowance for credit losses is added to the purchase price to determine the initial amortized cost basis. The subsequent accounting for PCD financial assets is the same expected loss model described above.	This standard requires credit losses on most financial assets measured at amortized cost and certain other instruments to be measured using an expected credit loss model (referred to as the current expected credit loss (CECL) model). Under this model, entities will estimate credit losses over the entire contractual term of the instrument (considering estimated prepayments, but not expected extensions or modifications) from the date of initial recognition of that instrument. The ASU replaces the current accounting model for purchased credit impaired loans and debt securities. The allowance for credit losses for purchased financial assets with a more-than insignificant amount of credit deterioration since origination (“PCD assets”), should be determined in a similar manner to other financial assets measured on an amortized cost basis. However, upon initial recognition, the allowance for credit losses is added to the purchase price to determine the initial amortized cost basis. The subsequent accounting for PCD financial assets is the same expected loss model described above.

In addition, ASC 326 made changes to the accounting for available-for-sale debt securities. One such change is to require credit losses to be presented as an allowance rather than as a write-down on available-for-sale debt securities. Management does not intend to sell or believes that it is more likely than not they will be required to sell.

The Corporation adopted ASC 326 using the modified retrospective method for all financial assets measured at amortized cost and off-balance-sheet (OBS) credit exposures. Results for reporting periods beginning after January 1, 2023 are presented under ASC 326 while prior period amounts continue to be reported in accordance with previously applicable GAAP.

In addition, ASC 326 made changes to the accounting for available-for-sale debt securities. One such change is to require credit losses to be presented as an allowance rather than as a write-down on available-for-sale debt securities. Management does not intend to sell or believes that it is more likely than not they will be required to sell.
The Corporation adopted ASC 326 using the modified retrospective method for all financial assets measured at amortized cost and off-balance-sheet (OBS) credit exposures. Results for reporting periods beginning after January 1, 2023 are presented under ASC 326 while prior period amounts continue to be reported in accordance with previously applicable GAAP.

Effective Date

January 1, 2023

January 1, 2023

Effect on the Consolidated Financial Statements

The Corporation adopted the ASU as of January 1, 2023 and recorded a decrease to the allowance for credit loss (ACL) for loans of $536 thousand, an increase of $412 thousand to the ACL for unfunded commitments, an increase of $98 thousand to retained earnings, and a deferred tax liability of $26 thousand.

The following table illustrates the impact of ASC 326:

(Dollars in thousands)	As Reported Under ASC 326	Pre-ASC 326 Adoption	Impact of ASC 326 Adoption
Assets:			
Loans			
First liens	$ 1,555	$ 459	$ 1,096
Junior liens & lines of credit	727	234	493
Construction	248	343	(95)
Commercial real estate	8,077	7,493	584
Commercial	2,939	4,846	(1,907)
Consumer	93	133	(40)
Unallocated	—	667	(667)
Allowance for credit losses on loans	$ 13,639	$ 14,175	$ (536)
Liabilities:			

The Corporation adopted the ASU as of January 1, 2023 and recorded a decrease to the allowance for credit loss (ACL) for loans of $536 thousand, an increase of $412 thousand to the ACL for unfunded commitments, an increase of $98 thousand to retained earnings, and a deferred tax liability of $26 thousand.
The following table illustrates the impact of ASC 326:
(Dollars in thousands) As Reported Under ASC 326 | Pre-ASC 326 Adoption | Impact of ASC 326 Adoption
Assets:
Loans
First liens - residential real estate $ 1,555 $ 459 $ 1,096
Junior liens & lines of credit - residential real estate 727 234 493
Construction 248 343 (95)
Commercial real estate 8,077 7,493 584
Commercial 2,939 4,846 (1,907)
Consumer 93 133 (40)
Unallocated — 667 (667)
Allowance for credit losses on loans $ 13,639 $ 14,175 $ (536)
Liabilities:

	Allowance for credit losses on OBS credit exposures $ 1,887 $ 1,475 $ 412	Allowance for credit losses on OBS credit exposures $ 1,887 $ 1,475 $ 412
ASU 2019-05, Financial Instruments - Credit Losses (Topic 326): Targeted Transition Relief		
Description	This ASU allows entities to irrevocably elect, upon adoption of ASU 2016-13, the fair value option on financial instruments that (1) were previously recorded at amortized cost and (2) are within the scope of ASC 326-20 if the instruments are eligible for the fair value option under ASC 825-10. The fair value option election does not apply to held-to-maturity debt securities. Entities are required to make this election on an instrument-by-instrument basis. ASU 2019-05 has the same effective date as ASU 2016-13. On October 16, 2019, FASB approved its August 2019 proposal to grant certain small public companies a delay in the effective date of ASU 2016-13. For the Corporation, the delay makes the ASU effective January 2023. Since the Corporation currently meets the SEC definition of a small reporting company, the delay will be applied to the Corporation. Early adoption is permitted.	This ASU allows entities to irrevocably elect, upon adoption of ASU 2016-13, the fair value option on financial instruments that (1) were previously recorded at amortized cost and (2) are within the scope of ASC 326-20 if the instruments are eligible for the fair value option under ASC 825-10. The fair value option election does not apply to held-to-maturity debt securities. Entities are required to make this election on an instrument-by-instrument basis. ASU 2019-05 has the same effective date as ASU 2016-13.
Effective Date	January 1, 2023	January 1, 2023
Effect on the Consolidated Financial Statements	The Corporation adopted the ASU on January 1, 2023 and did not elect the fair value option on any financial instruments.	The Corporation adopted the ASU on January 1, 2023 and did not elect the fair value option on any financial instruments.
ASU 2022-02, Financial Instruments - Credit Losses (Topic 326): Troubled Debt Restructuring and Vintage Disclosures		**ASU 2022-02, Financial Instruments - Credit Losses (Topic 326): Troubled Debt Restructuring and Vintage Disclosures**

ASU 2022-02, Financial Instruments - Credit Losses (Topic 326): Troubled Debt Restructuring and Vintage Disclosures	
Description	ASU 2022-02 eliminates the accounting guidance for troubled debt restructurings in Accounting Standards Codification ("ASC") 310-40, "Receivables - Troubled Debt Restructurings by Creditors" for entities that have adopted the current expected credit loss model introduced by ASU 2016-13, "Financial Instruments - Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments." ASU 2022-02 also required that public business entities disclosure current-period gross charge-offs by year of origination for financing receivables and net investments in leases within the scope of Subtopic 326-20, "Financial Instruments - Credit Losses - Measured at Amortized Cost."
Effective Date	January 1, 2023
Effect on the Consolidated Financial Statements	The Corporation adopted the standard on January 1, 2023 and it decreased the balance of loans individually evaluated by $3.0 million, and decreased the balance of performing TDR loans by the same amount.

Recently issued but not yet effective accounting standards

ASU 2023-01, Leases (Topic 842): Common Control Arrangements	
Description	This ASU requires entities to determine whether a related party arrangement between entities under common control is a lease. If the arrangement is determined to be a lease, an entity must classify and account for the lease on the same basis as an arrangement with a related party (on the basis of legally enforceable terms and conditions).
Effective Date	January 1, 2024
Effect on the Consolidated Financial Statements	The ASU is not expected to have an impact on the Corporation's financial statements.

ASU 2023-02, Investments - Equity Method and Joint Ventures (Topic 323): Accounting for Investments in Tax Credit Structures Using the Proportional Amortization Method	
Description	This ASU permits reporting entities to elect to account for their tax equity investments, regardless of the tax credit program from which the income tax credits are received, using the proportional amortization method if certain conditions are met.
Effective Date	January 1, 2024
Effect on the Consolidated Financial Statements	The ASU is not expected to have an impact on the Corporation's financial statements.

Note 3. Accumulated Other Comprehensive Income (Loss)

The components of accumulated other comprehensive income (loss), net of income tax effects, included in shareholders' equity are as follows:

(Dollars in thousands)	**June 30, 2023**	December 31, 2022	**September 30, 2023**	December 31, 2022
Net unrealized losses on debt securities	$ (57,286)	$ (61,497)	$ (67,252)	$ (61,497)
Tax effect	12,029	12,914	14,122	12,914
Net of tax amount	$ (45,257)	$ (48,583)	$ (53,130)	$ (48,583)
Accumulated pension adjustment	$ (3,423)	$ (3,423)	$ (3,423)	$ (3,423)
Tax effect	719	719	719	719
Net of tax amount	$ (2,704)	$ (2,704)	$ (2,704)	$ (2,704)
Total accumulated other comprehensive (loss)	$ (47,961)	$ (51,287)	$ (55,834)	$ (51,287)

Note 4. Investments

Available for Sale (AFS) Securities

The amortized cost and estimated fair value of AFS securities as of June 30, 2023 September 30, 2023 and December 31, 2022 are as follows:

(Dollars in thousands)	Amortized cost	Gross unrealized gains	Gross unrealized losses	Fair Value	Amortized cost	Gross unrealized gains	Gross unrealized losses	Fair Value
June 30, 2023								
September 30, 2023								
U.S. Treasury	**$ 83,849**	$ —	$ **(11,157)**	$ **72,692**	**$ 83,672**	$ —	$ **(12,531)**	$ **71,141**
Municipal	**161,978**	**—**	**(25,622)**	**136,356**	**161,659**	**—**	**(32,942)**	**128,717**

	Amortized cost	Gross unrealized gains	Gross unrealized losses	Fair value	Amortized cost	Gross unrealized gains	Gross unrealized losses	Fair value
Corporate	**26,326**	**—**	**(3,496)**	**22,830**	**26,331**	**—**	**(3,348)**	**22,983**
Agency mortgage & asset-backed	**152,013**	**36**	**(12,164)**	**139,885**	**147,099**	**81**	**(12,810)**	**134,370**
Non-Agency mortgage & asset-backed	**72,591**	**7**	**(4,890)**	**67,708**	**106,767**	**7**	**(5,709)**	**101,065**
Total	**$ 496,757**	**$ 43**	**$ (57,329)**	**$ 439,471**	**$ 525,528**	**$ 88**	**$ (67,340)**	**$458,276**

(Dollars in thousands) December 31, 2022	Amortized cost	Gross unrealized gains	Gross unrealized losses	Fair value
U.S. Treasury	$ 101,980	$ —	$ (11,723)	$ 90,257
Municipal	186,007	14	(30,566)	155,455
Corporate	26,316	—	(2,077)	24,239
Agency mortgage & asset-backed	163,274	19	(12,358)	150,935
Non-Agency mortgage & asset-backed	70,756	1	(4,807)	65,950
Total	$ 548,333	$ 34	$ (61,531)	$ 486,836

At June 30, 2023 September 30, 2023 and December 31, 2022, the fair value of debt securities pledged to secure public funds and trust deposits totaled $151.7 million $199.1 million and $208.9 million, respectively. The Bank has no investment in a single issuer that exceeds 10% of shareholders' equity, except for securities issued by the U.S. Treasury and U.S. government sponsored entities.

The amortized cost and estimated fair value of debt securities at June 30, 2023 September 30, 2023, by contractual maturity, are shown below. Actual maturities may differ from contractual maturities because of prepayment or call options embedded in the securities. Securities not due at a single maturity date are presented separately.

(Dollars in thousands)	**Amortized cost**	**Fair value**	**Amortized cost**	**Fair value**
Due in one year or less	$ —	$ —	$ —	$ —
Due after one year through five years	31,288	27,477	44,354	38,583
Due after five years through ten years	123,670	106,461	117,050	97,821
Due after ten years	117,195	97,940	110,258	86,437
	272,153	231,878	271,662	222,841
Mortgage & asset-backed	224,604	207,593	253,866	235,435
	$ 496,757	$ 439,471	$ 525,528	$458,276

The composition of the net realized gains (losses) on debt securities for the three and six nine months ended are as follows:

(Dollars in thousands)	For the Three Months Ended June 30, **2023**	2022	For the Six Months Ended June 30, **2023**	2022	For the Three Months Ended September 30, **2023**	2022	For the Nine Months Ended September 30, **2023**	2022
Proceeds	**$ 7,262**	$ 82	**$ 40,117**	$ 82	**$ —**	$1,000	**$40,117**	$1,082
Gross gains realized	**$ —**	$ —	**$ 12**	$ —	**$ —**	$ —	**$ 12**	$ —
Gross losses realized	**(517)**	(19)	**(1,131)**	(19)	**—**	(15)	**(1,131)**	(34)
Net (losses) gains realized	**$ (517)**	$ (19)	**$ (1,119)**	$ (19)	**$ —**	$ (15)	**$ (1,119)**	$ (34)
Tax benefit (provision) on net (losses) gains realized	**$ 109**	$ 4	**$ 235**	$ 4	**$ —**	$ 3	**$ 235**	$ 7

9

<u>Impairment</u>:

The debt securities portfolio contained 570 578 securities with $434.0 million $448.9 million of temporarily impaired fair value and $57.3 million $67.3 million in unrealized losses at June 30, 2023 September 30, 2023. The total unrealized loss position has decreased $4.2

million increased $5.8 million since year-end 2022 due primarily to an increase in long-term interest rates during the period despite the Bank realizing $1.1 million of losses due to restructuring of the portfolio and a decrease in long-term market interest rates. portfolio.

AFS securities in an unrealized loss position are evaluated for credit impairment at least quarterly. For these securities, the Bank considers: (1) the extent to which the fair value is less than amortized cost; (2) adverse conditions specifically related to the security, industry or geographic area; (3) the payment structure of the debt security and the likelihood of the issuer being able to make payments that increase in the future; (4) failure of the issuer of the security to make scheduled interest or principal payments; and (5) any changes to the rating of the security by a rating agency. In addition, the Bank considers whether it intends to sell these securities or whether it will be forced to sell these securities before the earlier of amortized cost recovery or maturity. The Bank does not have the intent to sell and does not believe it will more likely than not be required to sell any of these securities prior to a recovery of their fair value to amortized cost. The impairment identified on debt securities and subject to evaluation at June 30, 2023 September 30, 2023, was determined not to be attributable to credit related factors; therefore, the Bank does not have an allowance for credit loss for these investments. During 2023, approximately $40 million of securities was sold as part of a portfolio restructuring to take advantage of higher market interest rates. The realized loss on these sales was $1.1 million.

The following table reflects impairment in the AFS portfolio, aggregated by investment category, length of time that individual securities have been in a continuous unrealized loss position and the number of securities in each category as of June 30, 2023 September 30, 2023 and December 31, 2022:

	June 30, 2023									**September 30, 2023**								
	Less than 12 months			**12 months or more**			**Total**			**Less than 12 months**			**12 months or more**			**Total**		
(Dollars in thousands)	**Fair Value**	**Unrealized Losses**	**Count**	**Fair Value**	**Unrealized Losses**	**Count**	**Fair Value**	**Unrealized Losses**	**Count**	**Fair Value**	**Unrealized Losses**	**Count**	**Fair Value**	**Unrealized Losses**	**Count**	**Fair Value**	**Unrealized Losses**	**Count**
U.S. Treasury	**$ —**	**$ —**	**—**	**$ 72,692**	**$ (11,157)**	**28**	**$ 72,692**	**$ (11,157)**	**28**	**$ —**	**$ —**	**—**	**$ 71,141**	**$ (12,531)**	**28**	**$ 71,141**	**$ (12,531)**	**28**
Municipal	**842**	**(161)**	**2**	**135,515**	**(25,461)**	**166**	**136,357**	**(25,622)**	**168**	**810**	**(193)**	**2**	**127,907**	**(32,749)**	**166**	**128,717**	**(32,942)**	**168**
Corporate	**4,279**	**(521)**	**11**	**18,551**	**(2,975)**	**40**	**22,830**	**(3,496)**	**51**	**1,483**	**(167)**	**5**	**21,500**	**(3,181)**	**46**	**22,983**	**(3,348)**	**51**
Agency mortgage & asset-backed	**14,773**	**(474)**	**48**	**121,344**	**(11,690)**	**205**	**136,117**	**(12,164)**	**253**	**7,716**	**(195)**	**22**	**120,909**	**(12,615)**	**228**	**128,625**	**(12,810)**	**250**
Non-Agency mortgage & asset-backed	**26,547**	**(1,307)**	**27**	**39,473**	**(3,583)**	**43**	**66,020**	**(4,890)**	**70**	**49,219**	**(859)**	**25**	**48,230**	**(4,850)**	**56**	**97,449**	**(5,709)**	**81**
Total temporarily impaired	**$ 46,441**	**$ (2,463)**	**88**	**$ 387,575**	**$ (54,866)**	**482**	**$ 434,016**	**$ (57,329)**	**570**	**$59,228**	**$ (1,414)**	**54**	**$389,687**	**$ (65,926)**	**524**	**$448,915**	**$ (67,340)**	**578**

	December 31, 2022									December 31, 2022								
	Less than 12 months			12 months or more			Total			Less than 12 months			12 months or more			Total		
(Dollars in thousands)	Fair Value	Unrealized Losses	Count	Fair Value	Unrealized Losses	Count	Fair Value	Unrealized Losses	Count	Fair Value	Unrealized Losses	Count	Fair Value	Unrealized Losses	Count	Fair Value	Unrealized Losses	Count
U.S. Treasury	$ 17,598	$ (183)	3	$ 72,659	$ (11,540)	28	$ 90,257	$ (11,723)	31	$ 17,598	$ (183)	3	$ 72,659	$ (11,540)	28	$ 90,257	$ (11,723)	31
Municipal	73,644	(9,586)	90	80,503	(20,981)	104	154,147	(30,566)	194	73,644	(9,586)	90	80,503	(20,980)	104	154,147	(30,566)	194
Corporate	12,221	(851)	25	10,368	(1,226)	21	22,589	(2,077)	46	12,221	(851)	25	10,368	(1,226)	21	22,589	(2,077)	46
Agency mortgage & asset-backed	55,393	(2,747)	139	88,953	(9,611)	113	144,346	(12,358)	252	55,393	(2,747)	139	88,953	(9,611)	113	144,346	(12,358)	252
Non-Agency mortgage & asset-backed	49,301	(3,092)	52	14,207	(1,715)	16	63,508	(4,807)	68	49,301	(3,092)	52	14,207	(1,715)	16	63,508	(4,807)	68
Total temporarily impaired	$ 208,157	$ (16,459)	309	$ 266,690	$ (45,072)	282	$ 474,847	$ (61,531)	591	$208,157	$ (16,459)	309	$266,690	$ (45,072)	282	$474,847	$ (61,531)	591

Equity Securities at Fair Value

The Corporation owns one equity investment with a readily determinable fair value. At June 30, 2023 September 30, 2023 and December 31, 2022, this investment was reported at fair value of $380 $386 thousand and $411 thousand, respectively, with changes in value reported through income.

Note 5. Loans

The Bank reports its loan portfolio based on the primary collateral of the loan. It further classifies these loans by the primary purpose, either consumer or commercial. The Bank's mortgage loans include long-term loans to individuals and

businesses secured by mortgages on the borrower's real property. Construction loans are made to finance the purchase of land and the construction of residential and commercial buildings thereon and are secured by mortgages on real estate.

Commercial loans are made to businesses of various sizes for a variety of purposes including construction, property, plant and equipment, and working capital. Commercial loans also include loans to government municipalities. Commercial lending is concentrated in the Bank's primary market, but also includes purchased loan participations. Consumer loans are comprised of installment, home equity and unsecured personal lines of credit.

Each class of loans involves a different kind of risk. However, risk factors such as changes in interest rates, general economic conditions and changes in collateral values are common across all classes. The risk of each loan class is presented below.

Residential Real Estate 1-4 family

The largest risk in residential real estate loans to retail customers is the borrower's inability to repay the loan due to the loss of the primary source of income. The Bank attempts to mitigate this risk through prudent underwriting standards including employment history, current financial condition and credit history. These loans are generally owner occupied and serve as the borrower's primary residence. The Bank usually holds a first lien position on these properties but may hold a second lien position in some home equity loans or lines of credit. Commercial purpose loans, secured by residential real estate, are usually dependent upon repayment from the rental income or other business purposes. These loans are generally non-owner occupied. In addition to the real estate collateral, these loans may have personal guarantees or UCC filings on other business assets. If a payment default occurs on a 1-4 family residential real estate loan, the collateral serves as a source of repayment, but may be subject to a change in value due to economic conditions.

Residential Real Estate Construction

This class includes loans to individuals for construction of a primary residence and to contractors and developers to improve real estate and construct residential properties. Construction loans to individuals generally bear the same risk as 1-4 family residential loans. Additional risks may include cost overruns, delays in construction or contractor problems.

Loans to contractors and developers are primarily dependent on the sale of improved lots or finished homes for repayment. Risks associated with these loans include the borrower's character and capacity to complete a development, the effect of economic conditions on the valuation of lots or homes, cost overruns, delays in construction or contractor problems. In addition to real estate collateral, these loans may have personal guarantees or UCC filings on other business assets, depending on the financial strength and experience of the developer. Real estate construction loans are monitored on a regular basis by either an independent third party or the responsible loan officer, depending on the size and complexity of the project. This monitoring process includes, at a minimum, the submission of invoices or AIA documents detailing the cost incurred by the borrower, on-site inspections, and an authorizing signature for disbursement of funds.

Commercial Real Estate

Commercial real estate loans may be secured by various types of commercial property including retail space, office buildings, warehouses, hotels and motel, manufacturing facilities and, agricultural land.

Commercial real estate loans present a higher level of risk than residential real estate loans. Repayment of these loans is normally dependent on cash flow generated by the operation of a business that utilizes the real estate. The successful operation of the business, and therefore repayment ability, may be affected by general economic conditions outside of the control of the operator. On most commercial real estate loans ongoing monitoring of cash flow and other financial performance indictors is completed annually through financial statement analysis. In addition, the value of the collateral may be negatively affected by economic conditions and may be insufficient to repay the loan in the event of default. In the event of foreclosure, commercial real estate may be more difficult to liquidate than residential real estate.

Commercial

Commercial loans are made for various business purposes to finance equipment, inventory, accounts receivables, and operating liquidity. These loans are generally secured by business assets or equipment, non-real estate collateral and/or personal guarantees.

Commercial loans present a higher level of credit risk than other loans because repayment ability is usually dependent on cash-flow from a business operation that can be affected by general economic conditions. On most commercial loans ongoing monitoring of cash flow and other financial performance indicators occur at least annually through financial statement analysis. In the event of a default, collateral for these loans may be more difficult to liquidate, and the valuation of the collateral may decline more quickly than loans secured by other types of collateral.

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Loans to governmental municipalities are also included in the Commercial class. These loans generally have less risk than Commercial & Industrial (C&I) loans due to the taxing authority of the municipality and its ability to assess fees on services.

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This class also includes loans made as part of the Paycheck Protection Program (PPP). The PPP is a small business loan program, administered by the Small Business Administration (SBA). The PPP loans are 100 percent guaranteed by the SBA and have a maturity of two years or five years with a fixed interest rate of 1.00% for the life of the loan. Because the PPP loans are 100% guaranteed by the SBA, they present no credit risk to the Bank once the SBA guarantee is fulfilled. However, if the SBA does not grant loan forgiveness, the PPP loan would present the same risk factors as any other commercial loan.

Consumer

These loans are made for a variety of reasons to consumers and include term loans and personal lines-of credit. The loans may be secured or unsecured. Repayment is primarily dependent on the income of the borrower and to a lesser extent the sale of collateral. The underwriting of these loans is based on the consumer's ability and willingness to repay and is determined by the borrower's employment history, current financial condition and credit background. history. Collateral for these loans, if any, usually depreciates quickly and therefore, may not be adequate to repay the loan if it is repossessed. Therefore, the overall health of the economy, including unemployment rates and wages, will have an effect on the credit quality in this loan class.

A summary of loans outstanding, by class, at the end of the reporting periods is as follows:

(Dollars in thousands)	**June 30, 2023**	December 31, 2022	**September 30, 2023**	December 31, 2022
Residential Real Estate 1-4 Family				
Consumer first liens	**$ 106,546**	$ 82,795	**$ 124,289**	$ 82,795
Commercial first lien	**63,218**	61,702	**62,942**	61,702
Total first liens	**169,764**	144,497	**187,231**	144,497
Consumer junior liens and lines of credit	**68,463**	69,561	**68,141**	69,561
Commercial junior liens and lines of credit	**3,888**	4,127	**3,685**	4,127
Total junior liens and lines of credit	**72,351**	73,688	**71,826**	73,688
Total residential real estate 1-4 family	**242,115**	218,185	**259,057**	218,185
Residential real estate - construction				
Consumer	**7,868**	13,908	**11,264**	13,908
Commercial	**10,165**	10,485	**9,820**	10,485
Total residential real estate construction	**18,033**	24,393	**21,084**	24,393
Commercial real estate	**638,132**	566,662	**671,182**	566,662

Commercial	**240,555**	235,602	**249,119**	235,602
Total commercial	**878,687**	802,264	**920,301**	802,264
Consumer	**6,327**	6,199	**6,408**	6,199
	1,145,162	1,051,041	**1,206,850**	1,051,041
Less: Allowance for credit losses	**(14,615)**	(14,175)	**(15,528)**	(14,175)
Net Loans	**$ 1,130,547**	$ 1,036,866	**$1,191,322**	$1,036,866
Included in the loan balances are the following:				
Net unamortized deferred loan costs	**$ 1,751**	$ 2,027	**$ 1,651**	$ 2,027
Loans pledged as collateral for borrowings and commitments from:				
FHLB	**$ 609,064**	$ 585,601	**$ 651,297**	$ 585,601
Federal Reserve Bank	**88,182**	92,922	**85,595**	92,922
	$ 697,246	$ 678,523	**$ 736,892**	$ 678,523
Paycheck Protection Program (included in commercial loans)	**$ 78**	$ 179	**$ 68**	$ 179

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Note 6. Loan Quality and Allowance for Credit Losses

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

Management estimates the allowance balance using relevant available information, from internal and external sources, relating to past events, current conditions, and reasonable and supportable forecasts. Historical credit loss experience, derived from peer group data, provides the basis for the estimation of expected credit losses. Adjustments to historical loss information are made for differences in: lending policy, procedures and practice; economic conditions; nature and volume of loans; experience of lending team; volume of past due loans; quality of the loan review system; concentrations of credit; and other external factors.

Expected credit losses are estimated over the contractual term of the loans, adjusted for expected prepayments when appropriate. The contractual term excludes expected extensions, renewals, and modifications unless either of the following applies: management has a reasonable expectation at the reporting date that a modification will be executed with an individual borrower, or the extension or renewal options are included int eh original or modified contract at the reporting date and are not unconditionally cancellable by the Bank.

The allowance for credit losses is measured on a collective (pool) basis when similar risk characteristics exist. The Bank measures the ALCAllowance for Credit Loss (ACL) using the following inputs to calculate the quantitative component for the pool:

- Segregating loans into homogeneous pools by the FRB Call Code which is primarily a collateral-based and secondarily a purpose-based segmentation.
- The average remaining life of each pool is calculated using the weighted average remaining maturity method (WARM). The WARM method produces an estimated remaining balance by pool, by year, until maturity.
- Using third party data, the Bank determines a reasonable and supportable economic forecast that it believes is likely to exist for the next 4 four quarters.
- A historical credit loss rate is calculated for each pool, using the average historical loss, by FRB Call Code, for a peer group of Pennsylvania community banks over the last eight quarters. The historical loss rate is calculated over a historical period the Bank believes best represents a period that will be similar to the next 4 four quarters.
- The historical peer credit loss rate is applied to each WARM bucket though through the initial 4 four quarter forecast period.
- At the end of the four quarter forecast period, the credit loss rate applied to each WARM bucket reverts to the peer group historical loss rate for the respective pool.
- Collectively these estimated losses represent the quantitative component of the pooled reserve.

The qualitative component for the pool utilizes a risk matrix comprised of eight risk factors and assigns a risk level to each factor. The risk factors consider changes in: lending policy, procedures and practice; economic conditions; nature and volume of loans; experience of lending team; volume of past due loans; quality of the loan review system; concentrations of credit; and other external factors. The risk factors are weighted to reflect Management's estimate of how the factor affects potential losses. The risk levels within each factor are measured in basis points and range from minimal risk to very high risk and are determined independently for commercial loans, residential mortgage loans and consumer loans.

The ACL for pooled loans is the sum of the quantitative and qualitative loss estimates.

The Bank categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt such as: current financial information, historical payment experience, credit documentation, and current economic trends, among other factors. Management utilizes a risk rating scale ranging from 1-Prime to 9-Loss to evaluate loan quality. This risk factor rating scale is used primarily for each portfolio segment commercial purpose loans. Consumer purpose loans are presented in Note 5 identified as either performing or nonperforming based on the payment status of the accompanying financial statements. loans. Nonperforming consumer loans are loans that are nonaccrual or 90 days or more past due and still accruing. The Bank uses the following definitions for risk ratings:

Pass (1-5): are considered pass credits with lower or average risk and are not otherwise classified.

OAEM (6): Loans classified as OAEM have a potential weakness that deserves management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or of the Company's credit position at some future date.

Substandard (7): Loans classified as Substandard are inadequately protected by the current net worth and paying capacity of the borrower or of the collateral pledged, if any. Loans so classified have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the Company will sustain some loss if the deficiencies are not corrected.

Doubtful (8): Loans classified as Doubtful have all the weaknesses inherent in those classified as Substandard, with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions and values, highly questionable and improbable.

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

Management monitors loan performance on a monthly basis and performs a quarterly evaluation of the adequacy of the Allowance for Credit Loss for loans (ACL). The Bank begins enhanced monitoring of all loans rated 6–OAEM or worse and obtains a new appraisal or asset valuation for any loans placed on nonaccrual and rated 7 - Substandard or worse. Management, at its discretion, may determine that additional adjustments to the appraisal or valuation are required. Valuation adjustments will be made as necessary based on factors, including, but not limited to: the economy, deferred maintenance, industry, type of property/equipment, age of the appraisal, etc. and the knowledge Management has about a particular situation. In addition, the cost to sell or liquidate the collateral is also estimated and deducted from the valuation in order to determine the net realizable value to the Bank. When determining the ACL, certain factors involved in the evaluation are inherently subjective and require material estimates that may be susceptible to significant change, including the amounts and timing of future cash flows. Management monitors the adequacy of the ACL on an ongoing basis and reports its adequacy quarterly to the Board Enterprise Risk Management Committee of the Board of Directors. Management believes the ACL at June 30, 2023 September 30, 2023 is adequate.

Expected credit losses are estimated over the contractual term of the loans, adjusted for expected prepayments when appropriate. The contractual term excludes expected extensions, renewals, and modifications unless either of the following applies: management has a reasonable expectation at the reporting date that a modification will be executed with an individual borrower or the extension or renewal options are included int eh original or modified contract at the reporting date and are not unconditionally cancellable by the Bank.

The Bank categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt such as: current financial information, historical payment experience, credit documentation, and current economic trends, among other factors. Management utilizes a risk rating scale ranging from 1-Prime to 9-Loss to evaluate loan quality.

This risk rating scale is used primarily for commercial purpose loans. Consumer purpose loans are identified as either performing or nonperforming based on the payment status of the loans. Nonperforming consumer loans are loans that are nonaccrual or 90 days or more past due and still accruing. The Bank uses the following definitions for risk ratings:

Pass (1-5): are considered pass credits with lower or average risk and are not otherwise classified.

OAEM (6): Loans classified as OAEM have a potential weakness that deserves management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or of the Company's credit position at some future date.

Substandard (7): Loans classified as Substandard are inadequately protected by the current net worth and paying capacity of the borrower or of the collateral pledged, if any. Loans so classified have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the Company will sustain some loss if the deficiencies are not corrected.

Doubtful (8): Loans classified as Doubtful have all the weaknesses inherent in those classified as Substandard, with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions and values, highly questionable and improbable.

The following table presents loans by year of origination and internally assigned risk ratings:

(Dollars in thousands, except per share)	Term Loans Amortized Cost Basis by Origination Year						Revolving Loans Amortized	Revolving Loans Converted		
As of June 30 September 30, 2023	**2023**	2022	2021	2020	2019	Prior	Cost Basis	to Term	Total	
Residential real estate 1-4 family:										
Commercial:										
Risk rating:										
Pass (1-5)	$ 5,901 7,702	$ 9,647 9,386	$ 12,319 11,426	$ 9,919 9,807	$ 2,615 2,454	$ 24,539 23,930	$ 2,064 1,824	$ —	$ 67,004 66,529	
OAEM (6)	—	—	—	—	—	—	—	—	—	
Substandard (7)	—	—	—	—	—	—	102 98	—	102 —	98
Doubtful (8)	—	—	—	—	—	—	—	—	—	
Total Commercial	5,901 7,702	9,647 9,386	12,319 11,426	9,919 9,807	2,615 2,454	24,539 24,028	2,166 1,824	—	67,106 66,627	
Consumer:										
Performing	18,695 37,186	29,125 30,157	16,198 15,746	11,070 10,893	5,772 5,684	30,601 29,605	46,357 42,554	17,097 20,605	174,915 192,430	
Nonperforming	—	—	—	—	—	94 —	—	—	94 —	
Total Consumer	18,695 37,186	29,125 30,157	16,198 15,746	11,070 10,893	5,772 5,684	30,695 29,605	46,357 42,554	17,097 20,605	175,009 192,430	
Total	$ 24,596 44,888	$ 38,772 39,543	$ 28,517 27,172	$ 20,989 20,700	$ 8,387 8,138	$ 55,234 53,633	$ 48,523 44,378	$ 17,097 20,605	$ 242,115 259,057	
Current period gross charge-offs	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —	
Residential real estate construction:										
Commercial:										

Risk rating:										
Pass (1-5)	$ 2,450 3,420 $	3,465 2,849 $	984 1,503 $	236 229 $	530 —$	1,590 1,819 $	—$	—$	9,255 9,820	
OAEM (6)	—	—	910	—	—	—	—	—	910 —	— ——
Substandard (7)	—	—	—	—	—	—	—	—	—	
Doubtful (8)	—	—	—	—	—	—	—	—	—	
Total Commercial	2,450 3,420	3,465 2,849	1,894 1,503	236 229	530 —	1,590 1,819	—	—	10,165 9,820	
Consumer:										
Performing	2,227 7,434	5,641 3,830	—	—	—	—	—	—	7,868 11,264	
Nonperforming	—	—	—	—	—	—	—	—	—	
Total Consumer	2,227 7,434	5,641 3,830	—	—	—	—	—	—	7,868 11,264	
Total	$ 4,677 10,854 $	9,106 6,679 $	1,894 1,503 $	236 229 $	530 —$	1,590 1,819 $	—$	—$	18,033 21,084	
Current period gross charge-offs $	—$	—$	—$	—$	—$	—$	—$	—$	—	
Commercial real estate:										
Risk rating:										
Pass (1-5)	$90,721 140,948 $	118,926 118,484 $	99,902 99,775 $	52,720 41,944 $	41,114 39,762 $	224,465 219,830 $	6,378 5,310 $	—$	634,226 666,053	
OAEM (6)	—	—	—	—	—	1,085 2,203	144	—	—	1,085 2,347
Substandard (7)	—	—	—	—	—	2,771 2,732	50	—	2,821 2,782	
Doubtful (8)	—	—	—	—	—	—	—	—	—	
Total	$90,721 140,948 $	118,926 118,484 $	99,902 99,775 $	52,720 41,944 $	41,114 39,762 $	228,321 224,765 $	6,428 5,504 $	—$	638,132 671,182	
Current period gross charge-offs $	—$	—$	—$	—$	—$	—$	—$	—$	—	
Commercial:										
Risk rating:										
Pass (1-5)	$ 21,936 28,531 $	36,927 35,229 $	45,142 47,478 $	25,698 23,762 $	4,642 4,121 $	68,894 65,513 $	32,299 39,315 $	—$	235,538 243,949	
OAEM (6)	—	—	—	—	—	—	—	—	—	
Substandard (7)	— 116	359 340	—	—	—	3,701 3,642	957 1,072	—	5,017 5,170	
Doubtful (8)	—	—	—	—	—	—	—	—	—	
Total	$ 21,936 28,647 $	37,286 35,569 $	45,142 47,478 $	25,698 23,762 $	4,642 4,121 $	72,595 69,155 $	33,256 40,387 $	—$	240,555 249,119	
Current period gross charge-offs $	(6) (8)$	—$	(81)$	—$	—$	—$	—$	—$	(87) (89)	
Consumer:										
Performing	1,069 1,421	848 759	2,140 2,053	224 181	139 114	12 8	1,895 1,858	—	6,327 6,394	
Nonperforming	—	—	—	—	—	—	— 14	—	— 14	
Total	$ 1,069 1,421 $	848 759 $	2,140 2,053 $	224 181 $	139 114 $	12 8 $	1,895 1,872 $	—$	6,327 6,408	
Current period gross charge-offs $	(22) (37)$	(16)$	(10)$	(2)$	(6)$	—$	— (26)$	—$	(32)$	—$(76) (97)

The following table presents the amortized cost basis of loans on nonaccrual status and loans past due over 90 days and still accruing as of June 30, 2023 September 30, 2023:

(Dollars in thousands)	Nonaccrual and Loans Past Due Over 90 Days+			Nonaccrual and Loans Past Due Over 90 Days+		
	Nonaccrual Without ACL	Nonaccrual With ACL	Loans Past Due Over 90 Days Still Accruing	Nonaccrual Without ACL	Nonaccrual With ACL	Loans Past Due Over 90 Days Still Accruing
June 30, 2023						
September 30, 2023						
Residential Real Estate 1-4 Family						
First liens	$ 102	$ —	$ 94	$ 98	$ —	$ —
Junior liens and lines of credit	—	—	—	—	—	—
Total	102	—	94	98	—	—
Residential real estate - construction	—	—	—	—	—	—
Commercial real estate	—	—	—	—	—	—
Commercial	—	—	—	115	—	—
Consumer	—	—	—	—	—	14
Total	$ 102	$ —	$ 94	$ 213	$ —	$ 14

The following table reports the risk rating for those loans in the portfolio that were assigned an individual risk rating at December 31, 2022:

(Dollars in thousands)	Pass (1-5)	OAEM (6)	Substandard (7)	Doubtful (8)	Total
December 31, 2022					
Residential Real Estate 1-4 Family					
First liens	$ 144,377	$ —	$ 120	$ —	$ 144,497
Junior liens and lines of credit	73,688	—	—	—	73,688
Total	218,065	—	120	—	218,185
Residential real estate - construction	24,393	—	—	—	24,393
Commercial real estate	562,665	1,095	2,902	—	566,662
Commercial	228,085	2,751	4,766	—	235,602
Consumer	6,199	—	—	—	6,199
Total	$ 1,039,407	$ 3,846	$ 7,788	$ —	$ 1,051,041

At June 30, 2023 and December 31, 2022, September 30, 2023 the Bank had $94 thousand $0 of residential properties in the process of foreclosure. foreclosure compared to $94 thousand at December 31, 2022. The following table presents the aging of payments of the loan portfolio:

(Dollars in thousands)	Loans Past Due						Loans Past Due					
	30-59 Days	60-89 Days	90 Days+	Total Past Due	Current	Total Loans	30-59 Days	60-89 Days	90 Days+	Total Past Due	Current	Total Loans

June 30, 2023												
September 30, 2023												
Residential Real Estate 1-4 Family												
First liens	$ 72	$ 364	$ 196	$ 632	$ 169,132	$ 169,764	$ 21	$232	$ 98	$ 351	$ 186,880	$ 187,231
Junior liens and lines of credit	202	—	—	202	72,149	72,351	399	—	—	399	71,427	71,826
Total	274	364	196	834	241,281	242,115	420	232	98	750	258,307	259,057
Residential real estate - construction	—	—	—	—	18,033	18,033	—	—	—	—	21,084	21,084
Commercial real estate	235	—	—	235	637,897	638,132	311	—	—	311	670,871	671,182
Commercial	612	—	—	612	239,943	240,555	662	—	115	777	248,342	249,119
Consumer	30	6	—	36	6,291	6,327	10	16	14	40	6,368	6,408
Total	$ 1,151	$ 370	$ 196	$ 1,717	$ 1,143,445	$ 1,145,162	$1,403	$248	$ 227	$1,878	$1,204,972	$1,206,850

December 31, 2022	30-59 Days	60-89 Days	90 Days+	Nonaccrual	Total Past Due & Nonaccrual	Current	Total Loans	30-59 Days	60-89 Days	90 Days+	Nonaccrual	Total Past Due & Nonaccrual	Current	Total Loans
Residential Real Estate 1-4 Family														
First liens	$ 340	$ 177	$ —	$ 120	$ 637	$ 143,860	$ 144,497	$ 340	$177	$ —	$ 120	$ 637	$ 143,860	$ 144,497
Junior liens and lines of credit	490	—	—	—	490	73,198	73,688	490	—	—	—	490	73,198	73,688
Total	830	177	—	120	1,127	217,058	218,185	830	177	—	120	1,127	217,058	218,185
Residential real estate - construction	—	—	—	—	—	24,393	24,393	—	—	—	—	—	24,393	24,393
Commercial real estate	649	—	—	—	649	566,013	566,662	649	—	—	—	649	566,013	566,662
Commercial	681	50	—	—	731	234,871	235,602	681	50	—	—	731	234,871	235,602
Consumer	29	5	13	—	47	6,152	6,199	29	5	13	—	47	6,152	6,199
Total	$ 2,189	$ 232	$ 13	$ 120	$ 2,421	$ 1,048,487	$ 1,051,041	$2,189	$232	$ 13	$ 120	$ 2,554	$1,048,487	$1,051,041

The following table presents, by class, the activity in the Allowance for Credit Losses (ACL) for the periods shown:

(Dollars in thousands)	Residential Real Estate 1-4 Family: First Liens	Residential Real Estate 1-4 Family: Junior Liens & Lines of Credit	Construction	Commercial Real Estate	Commercial	Consumer	Unallocated	Total	Residential Real Estate 1-4 Family: First Liens	Residential Real Estate 1-4 Family: Junior Liens & Lines of Credit	Construction	Commercial Real Estate	Commercial	Consumer	Unallocated	Total
ACL at March 31, 2023	$ 1,624	$ 690	$ 190	$ 8,236	$ 3,275	$ 94	$ —	$ 14,109								
ACL at June 30, 2023									$1,720	$ 683	$ 177	$ 9,083	$ 2,854	$ 98	$ —	$14,615
Charge-offs	—	—	—	—	(1)	(42)	—	(43)	—	—	—	—	(2)	(21)	—	(23)
Recoveries	—	—	3	—	12	10	—	25	—	—	4	—	15	51	—	70
Provision	96	(7)	(16)	847	(432)	36	—	524	(519)	(265)	61	1,124	503	(38)	—	866

ACL at June 30, 2023	**$ 1,720 $**	**683 $**	**177 $**	**9,083 $**	**2,854 $**	**98 $**	**—$**	**14,615**								
ACL at September 30, 2023									**$1,201 $**	**418 $**	**242 $**	**10,207 $**	**3,370 $**	**90 $**	**—**	**$15,528**
ALL at December 31, 2022	**$ 459 $**	**234 $**	**343 $**	**7,493 $**	**4,846 $**	**133 $**	**667**	**14,175**	**$ 459 $**	**234 $**	**343 $**	**7,493 $**	**4,846 $**	**133 $**	**667**	**$14,175**
Impact of adopting ASU 2016-13	**1,096**	**493**	**(95)**	**584**	**(1,907)**	**(40)**	**(667)**	**(536)**	**1,096**	**493**	**(95)**	**584**	**(1,907)**	**(40)**	**(667)**	**(56)**
Charge-offs	**—**	**—**	**—**	**—**	**(87)**	**(76)**	**—**	**(163)**	**—**	**—**	**—**	**—**	**(89)**	**(97)**	**—**	**(186)**
Recoveries	**2**	**—**	**42**	**—**	**79**	**25**	**—**	**148**	**2**	**—**	**46**	**—**	**94**	**76**	**—**	**218**
Provision	**163**	**(44)**	**(113)**	**1,006**	**(77)**	**56**	**—**	**991**	**(356)**	**(309)**	**(52)**	**2,130**	**426**	**18**	**—**	**1,857**
ACL at June 30, 2023	**$ 1,720 $**	**683 $**	**177 $**	**9,083 $**	**2,854 $**	**98 $**	**—$**	**14,615**								
ACL at September 30, 2023									**$1,201 $**	**418 $**	**242 $**	**10,207 $**	**3,370 $**	**90 $**	**—**	**$15,528**
ALL at March 31, 2022	$ 480 $	253 $	329 $	7,962 $	5,183 $	125 $	718 $	15,050								
ALL at June 30, 2022									$ 465 $	245 $	289 $	8,096 $	5,076 $	119 $	725	$15,015
Charge-offs	—	—	—	—	(62)	(22)	—	(84)	—	—	—	—	(6)	(33)	—	(39)
Recoveries	32	—	—	—	7	10	—	49	—	1	—	—	8	4	—	13
Provision	(47)	(8)	(40)	134	(52)	6	7	—	(4)	3	75	9	(33)	38	(88)	—
ALL at June 30, 2022	$ 465 $	245 $	289 $	8,096 $	5,076 $	119 $	725 $	15,015								
ALL at September 30, 2022									$ 461 $	249 $	364 $	8,105 $	5,045 $	128 $	637	$14,989
ALL at December 31, 2021	$ 475 $	252 $	325 $	8,168 $	5,127 $	130 $	589 $	15,066	$ 475 $	252 $	325 $	8,168 $	5,127 $	130 $	589	$15,066
Charge-offs	(20)	—	—	—	(63)	(46)	—	(129)	(20)	—	—	—	(69)	(79)	—	(168)
Recoveries	47	1	—	—	12	18	—	78	47	2	—	—	20	22	—	91
Provision	(37)	(8)	(36)	(72)	—	17	136	—	(41)	(5)	39	(63)	(33)	55	48	—
ALL at June 30, 2022	$ 465 $	245 $	289 $	8,096 $	5,076 $	119 $	725 $	15,015								
ALL at September 30, 2022									$ 461 $	249 $	364 $	8,105 $	5,045 $	128 $	637	$14,989

The following table presents, by class, loans that were evaluated for the ALL under the specific reserve (individually) and those that were evaluated under the general reserve (collectively) and the amount of the ALL established in each class as of December 31, 2022:

	Residential Real Estate 1-4 Family							
(Dollars in thousands)	**First Liens**	**Junior Liens & Lines of Credit**	**Construction**	**Commercial Real Estate**	**Commercial**	**Consumer**	**Unallocated**	**Total**
December 31, 2022								
Loans evaluated for ALL:								
Individually	$ 619	$ —	$ —	$ 2,331	$ —	$ —	$ —	$ 2,950
Collectively	143,878	73,688	24,393	564,331	235,602	6,199	—	1,048,091
Total	$ 144,497	$ 73,688	$ 24,393	$ 566,662	$ 235,602	$ 6,199	$ —	$ 1,051,041
ALL established for loans evaluated:								
Individually	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —

Collectively	459	234	343	7,493	4,846	133	667	14,175
ALL at December 31, 2022	$ 459	$ 234	$ 343	$ 7,493	$ 4,846	$ 133	$ 667	$ 14,175

At June 30, 2023 September 30, 2023, there were no loans evaluated individually for the ACL.

On January 1, 2023, The Bank adopted ASU 2022-02, “Financial Instruments - Credit Losses (Topic 326): Troubled Debt Restructurings and Vintage Disclosures” (“ASU 2022-02”), which eliminated the accounting guidance for troubled debt restructurings (“TDRs”) while enhancing disclosure requirements for certain loan refinancing and restructurings by creditors when a borrower is experiencing financial difficulty. Modifications to borrowers experiencing financial difficulty may include interest rate reductions, principal or interest forgiveness, forbearances, term extensions, and other actions intended to minimize economic loss and to avoid foreclosure or repossession of collateral.

As of June 30, 2023, the Bank did not have any loans made to borrowers experiencing financial difficulties and there No loan modifications were no loans modifications made to borrowers experiencing financial difficulties during the first half nine months of 2023.

Prior to the adoption of ASU 2022-02, certain modified loans were reported as TDRs and impaired. The following table presents impaired loans as of December 31, 2022.

(Dollars in thousands)	**Impaired Loans**				
	With No Allowance		**With Allowance**		
December 31, 2022	**Recorded Investment**	**Unpaid Principal Balance**	**Recorded Investment**	**Unpaid Principal Balance**	**Related Allowance**
Residential Real Estate 1-4 Family					
First liens	$ 619	$ 619	$ —	$ —	$ —
Junior liens and lines of credit	—	—	—	—	—
Total	619	619	—	—	—
Residential real estate - construction	—	—	—	—	—
Commercial real estate	2,331	2,331	—	—	—
Commercial	—	—	—	—	—
Total	$ 2,950	$ 2,950	$ —	$ —	$ —

The following table presents TDR loans as of December 31, 2022:

(Dollars in thousands)	**Troubled Debt Restructurings**				**Troubled Debt Restructurings Within the Last 12 Months That Have Defaulted On Modified Terms**	
December 31, 2022	**Number of Contracts**	**Recorded Investment**	**Performing***	**Nonperforming***	**Number of Contracts**	**Recorded Investment**
Residential real estate - construction	—	$ —	$ —	$ —	—	$ —
Residential real estate	5	619	619	—	—	—
Commercial real estate - owner occupied	3	783	783	—	—	—
Commercial real estate - farm land	3	1,466	1,466	—	—	—
Commercial real estate - construction and land development	—	—	—	—	—	—
Commercial real estate - other	1	82	82	—	—	—
Total	12	$ 2,950	$ 2,950	$ —	—	$ —

**The performing status is determined by the loans compliance with the modified terms. Nonperforming is considered 90 days or more past due.*

Note 7. Leases

The Corporation leases various assets in the course of its operations that are subject to recognition on the balance sheet. The Corporation considers all of its leases to be operating leases and it has no finance leases. The leased assets may include equipment, and buildings and land (collectively real estate). The equipment leases are shorter-term than the real estate leases, and generally have a fixed payment over a defined term without renewal options. Certain equipment leases have purchase options and it was determined the option was not reasonably certain to be exercised. The real estate leases are longer-term and an may contain renewal options after the initial term, but none of the real estate leases contain a purchase option. The renewal options on real estate leases were reviewed and if it was determined the option was reasonably certain to be renewed, the option term was considered in the determination of the lease liability. There is only one real estate lease with a variable payment based on an index included in the lease liability. None of the leases contain any restrictive covenants and there are no significant leases that have not yet commenced. The discount rate used to determine the lease liability is

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based on the Bank's fully secured borrowing rate from the Federal Home Loan Bank for a term similar to the lease term. Operating lease expense is included in net occupancy expense in the consolidated statements of income.

Lease costs:

The components of total lease cost were as follows:

(Dollars in thousands)	Three Months Ended June 30, 2023	Three Months Ended June 30, 2022	Six Months Ended June 30, 2023	Six Months Ended June 30, 2022	Three Months Ended September 30, 2023	Three Months Ended September 30, 2022	Nine Months Ended September 30, 2023	Nine Months Ended September 30, 2022
Operating lease cost	**$ 212**	$ 200	**$ 429**	$ 373	**$191**	$193	**$619**	$566
Short-term lease cost	**4**	126	**8**	252	**4**	44	**12**	296
Variable lease cost	**37**	28	**74**	53	**36**	40	**110**	95
Total lease cost	**$ 253**	$ 354	**$ 511**	$ 678	**$231**	$277	**$741**	$957

Supplemental Lease Information:

(Dollars in thousands)	Six Months Ended June 30, 2023	Six Months Ended June 30, 2022	Nine Months Ended September 30, 2023	Nine Months Ended September 30, 2022
Cash paid for amounts included in the measurement of lease liabilities:				
Operating cash flows from operating leases	**$ 413**	$ 359	**$ 602**	$ 550
Weighted-average remaining lease term (years)	**11.9**	10.2	**11.9**	12.1
Weighted-average discount rate	**3.37%**	3.29%	**3.38%**	3.35%

Lease Obligations:

Future undiscounted lease payments for operating leases with initial terms of one year or more as of June 30, 2023 September 30, 2023 are as follows:

(Dollars in thousands)		
2023	**$ 374**	**$ 188**
2024	**717**	**717**
2025	**666**	**666**
2026	**564**	**564**
2027	**421**	**421**
2028 and beyond	**3,598**	**3,598**
Undiscounted cash flow	**6,340**	**6,154**

Imputed Interest	(1,236)	(1,194)
Total lease liability	$ 5,104	$ 4,960

A lease termination expense of $525 $495 thousand was recorded in the second quarter of 2023. The lease termination was a long-term real estate lease held for a new community banking office that will not be constructed. Due to the lease termination, the right of use asset decreased $507 thousand and the lease liability decreased $537 thousand.

Note 8. Other Real Estate Owned

The Bank had no other real estate owned at June 30, 2023 September 30, 2023 and December 31, 2022.

Note 9. Derivatives

The Corporation is exposed to certain risks arising from both its business operations and economic conditions. The Corporation principally manages its exposures to a wide variety of business and operational risks through management of its core business activities. The Corporation manages economic risks, including interest rate, liquidity, and credit risk, primarily by managing the amount, sources, and duration of its assets and liabilities.

The Corporation's existing credit derivatives result from participations in interest rate swaps provided by external lenders as part of loan participation arrangements. Derivatives not designated as hedges are not speculative and result from a service the Corporation provides to certain lenders which participate in loans.

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The table below presents the fair value of the Corporation's derivative financial instruments as well as their classification on the Balance Sheet.

	Fair Value of Derivative Instruments Derivative Liabilities						**Fair Value of Derivative Instruments** Derivative Liabilities					
(Dollars in thousands)	**June 30, 2023**			December 31, 2022			**September 30, 2023**			December 31, 2022		
	Notional amount	Balance Sheet Location	Fair Value	Notional amount	Balance Sheet Location	Fair Value	Notional amount	Balance Sheet Location	Fair Value	Notional amount	Balance Sheet Location	Fair Value
Derivatives not designated as hedging instruments												
Other Contracts	**$ 6,367**	Other Liabilities	**$ 3**	$ 6,465	Other Liabilities	$ 3	**$ 6,318**	Other Liabilities	**$ 1**	$ 6,465	Other Liabilities	$ 3
Total derivatives not designated as hedging instruments			**$ 3**			$ 3			**$ 1**			$ 3

The table below presents the effect of the Corporation's derivative financial instruments that are not designated as hedging instruments on the Income Statement.

Effect of Derivatives as Hedging Instruments on the Income Statement	**Effect of Derivatives as Hedging Instruments on the Income Statement**	**Effect of Derivatives as Hedging Instruments on the Income Statement**

Derivatives Not Designated as Hedging Instruments under Subtopic 815-20	Location of Gain or (Loss) Recognized in Income on Derivative	Amount of Gain or (Loss) Recognized in Income on Derivatives				Location of Gain or (Loss) Recognized in Income on Derivative	Amount of Gain or (Loss) Recognized in Income on Derivatives			
(Dollars in thousands)		Three Months Ended		Six Months Ended			Three Months Ended		Nine Months Ended	
		June 30, 2023	June 30, 2022	**June 30, 2023**	June 30, 2022		**September 30, 2023**	September 30, 2022	**September 30, 2023**	September 30, 2022
Other Contracts	Other income	$ **2**	$ 5	$ **-**	$ 13	Other income	$ **2**	$ 4	$ **3**	$ 17

As of June 30, 2023 September 30, 2023, the fair value of derivatives in a net liability position, which includes accrued interest but excludes any adjustment for nonperformance risk, related to these agreements was $3 $1 thousand.

Note 10. Pension

The components of pension expense for the periods presented are as follows:

	Three Months Ended June 30,		Six Months Ended June 30,		Three Months Ended September 30,		Nine Months Ended September 30,	
(Dollars in thousands)	**2023**	2022	**2023**	2022	**2023**	2022	**2023**	2022
Components of net periodic cost:								
Service cost	**$ 53**	$ 85	**$ 108**	$ 171	**$ 54**	$ 86	**$ 162**	$ 257
Interest cost	**201**	168	**403**	336	**202**	168	**605**	504
Expected return on plan assets	**(230)**	(248)	**(462)**	(497)	**(231)**	(249)	**(693)**	(746)
Recognized net actuarial loss	**—**	149	**—**	299	**—**	150	**—**	449
Total pension expense	**$ 24**	$ 154	**$ 49**	$ 309	**$ 25**	$ 155	**$ 74**	$ 464

The service cost component of pension expense is recorded in the salaries and employee benefits line and all other cost components are recorded in the nonservice pension line of the Consolidated Statements of Income.

Note 11. Fair Value Measurements and Fair Values of Financial Instruments

Management uses its best judgment in estimating the fair value of the Corporation's financial instruments; however, there are inherent weaknesses in any estimation technique. Therefore, for substantially all financial instruments, the fair value estimates herein are not necessarily indicative of the amounts the Corporation could have realized in a sales transaction on the dates indicated. The estimated fair value amounts have been measured as of their respective period-ends and have not been re-evaluated or updated for purposes of these financial statements subsequent to those respective dates. As such, the estimated fair values of these financial instruments subsequent to the respective reporting dates maybe different than the amounts reported at each year-end. The Corporation uses the exit price notion to measure the fair value of financial instruments.

FASB ASC Topic 820, "Financial Instruments", requires disclosure of the fair value of financial assets and liabilities, including those financial assets and liabilities that are not measured and reported at fair value on a recurring and nonrecurring basis. The Corporation does not report any nonfinancial assets at fair value. FASB ASC Topic 820 establishes a fair value hierarchy that prioritizes the inputs to valuation methods used to measure fair value. 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 the fair value hierarchy under FASB ASC Topic 820 are as follows:

Level 1: Valuation is based on unadjusted, quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities.

Level 2: Valuation is based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market. There may be substantial differences in the assumptions used for securities within the same level. For example, prices for U.S. Agency securities have fewer assumptions and are closer to level 1 valuations than the private label mortgage-backed securities that require more assumptions and are closer to level 3 valuations.

Level 3: Valuation is generated from model-based techniques that use significant assumptions not observable in the market. These unobservable assumptions reflect the Corporation's assumptions regarding what market participants would assume when pricing a financial instrument.

An asset's or liability's level within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement.

The following information regarding the fair value of the Corporation's financial instruments should not be interpreted as an estimate of the fair value of the entire Corporation since a fair value calculation is only provided for a limited portion of the Corporation's assets and liabilities. Due to a wide range of valuation techniques and the degree of subjectivity used in making the estimates, comparisons between the Corporation's disclosures and those of other companies may not be meaningful.

The following methods and assumptions were used to estimate the fair values of the Corporation's financial instruments measured at fair value on a recurring and nonrecurring basis.

Equity Securities: Equity securities are valued using quoted market prices from nationally recognized markets (Level 1). Equity securities are measured at fair value on a recurring basis.

Investment securities: Fair values of investment securities available-for-sale were primarily measured using information from a third-party pricing service. This service provides pricing information by utilizing evaluated pricing models supported with market data information. Standard inputs include benchmark yields, reported trades, broker/dealer quotes, issuer spreads, two-sided markets, benchmark securities, bids, offers, and reference data from market research publications. Level 2 investment securities are primarily comprised of debt securities issued by states and municipalities, corporations, mortgage-backed securities issued by government agencies, and government-sponsored enterprises. Fair values were estimated primarily by obtaining quoted prices for similar assets in active markets or through the use of pricing models. Investment securities are measured at fair value on a recurring basis.

Collateral Dependent Loans: The fair value of collateral dependent loans with specific allocations of the allowance for credit losses is generally based on recent real estate appraisals conducted by an independent, licensed appraiser, less cost to sell. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach (Level 2). If the appraiser makes an adjustment to account for differences between the comparable sales and income data available for similar loans, or if management adjusts the appraised value, then the fair value is considered Level 3. Non-real estate collateral may be valued using an appraisal, net book value per the borrower's financial statements, or aging reports, adjusted or discounted based on management's historical knowledge, changes in market conditions from the time of the valuation, and management's expertise and knowledge of the client and client's business, resulting in a Level 3 fair value classification. Collateral dependent loans are evaluated on a quarterly basis for additional impairment and adjusted in accordance with the allowance policy. No partial charge-offs on these loans was taken in the first third quarter of 2023. Collateral dependent loans are measured at fair value on a nonrecurring basis.

Recurring Fair Value Measurements

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

(Dollars in thousands)	Fair Value at June 30, 2023				Fair Value at September 30, 2023			
Asset Description	**Level 1**	**Level 2**	**Level 3**	**Total**	**Level 1**	**Level 2**	**Level 3**	**Total**
Equity securities, at fair value	$ 380	$ —	$ —	$ 380	$ 386	$ —	$ —	$ 386
Available for sale:								
U.S. Treasury	72,692	—	—	72,692	71,141	—	—	71,141
Municipal	—	136,356	—	136,356	—	128,717	—	128,717
Corporate	—	22,830	—	22,830	—	22,983	—	22,983
Agency mortgage & asset-backed	—	139,885	—	139,885	—	134,370	—	134,370
Non-Agency mortgage & asset-backed	—	67,708	—	67,708	—	101,065	—	101,065
Total assets	$ 73,072	$ 366,779	$ —	$ 439,851	$ 71,527	$ 387,135	$ —	$ 458,662

(Dollars in thousands)	Fair Value at December 31, 2022			
Asset Description	Level 1	Level 2	Level 3	Total
Equity securities, at fair value	$ 411	$ —	$ —	$ 411
Available for sale:				
U.S. Treasury	90,257	—	—	90,257
Municipal	—	155,455	—	155,455
Corporate	—	24,239	—	24,239
Agency mortgage and asset-backed	—	150,935	—	150,935
Non-Agency mortgage and asset-backed	—	65,950	—	65,950
Total assets	$ 90,668	$ 396,579	$ —	$ 487,247

The fair value of derivative liabilities measured at fair value at June 30, 2023 September 30, 2023 and December 31, 2022 was $3 $1 thousand during each period and was considered immaterial.

Nonrecurring Fair Value Measurements

The Corporation did not record any assets or liabilities at fair value for which measurement of the fair value was made on a nonrecurring basis at June 30, 2023 September 30, 2023. For financial assets and liabilities measured at fair value on a recurring basis, there were no transfers of financial assets or liabilities between Level 1 and Level 2 during the period ending June 30, 2023 September 30, 2023.

The carrying amounts and estimated fair value of financial instruments not carried at fair value are as follows:

	June 30, 2023					September 30, 2023				
(Dollars in thousands)	**Carrying Amount**	**Fair Value**	**Level 1**	**Level 2**	**Level 3**	**Carrying Amount**	**Fair Value**	**Level 1**	**Level 2**	**Level 3**
Financial assets, carried at cost:										
Cash and cash equivalents	$ 64,832	$ 64,832	$ 64,832	$ —	$ —	$ 73,953	$ 73,953	$ 73,953	$ —	$ —
Long-term interest-bearing deposits in other banks	8,978	8,978	8,978	—	—					
Long-term interest-earning deposits in other banks						7,728	7,728	7,728	—	—

Loans held for sale	126	126	—	126	—	792	792	—	792	—
Net loans	1,130,547	1,081,607	—	—	1,081,607	1,191,322	1,131,171	—	—	1,131,171
Accrued interest receivable	6,147	6,147	—	—	6,147	6,764	6,764	—	—	6,764
Financial liabilities:										
Deposits	$ 1,513,135	$ 1,511,696	$ —	$ 1,511,696	$ —	$ 1,567,414	$ 1,566,099	$ —	$ 1,566,099	$ —
Short-term borrowings	70,000	70,000	—	70,000	—					
Federal Reserve Bank borrowings						70,000	69,597		69,597	
FHLB advances						40,000	40,117	—	40,117	—
Subordinate notes	19,643	18,132	—	18,132	—	19,653	18,119	—	18,119	—
Accrued interest payable	1,441	1,441	—	1,441	—	2,836	2,836	—	2,836	—

	December 31, 2022					December 31, 2022				
(Dollars in thousands)	Carrying Amount	Fair Value	Level 1	Level 2	Level 3	Carrying Amount	Fair Value	Level 1	Level 2	Level 3
Financial assets, carried at cost:										
Cash and cash equivalents	$ 64,899	$ 64,899	$ 64,899	$ —	$ —	$ 64,899	$ 64,899	$64,899	$ —	$ —
Long-term interest-bearing deposits in other banks	13,975	13,975	13,975	—	—					
Long-term interest-earning deposits in other banks						13,975	13,975	13,975	—	—
Loans held for sale	283	287	—	287	—	283	287	—	287	—
Net loans	1,036,866	986,141	—	—	986,141	1,036,866	986,141	—	—	986,141
Accrued interest receivable	6,354	6,354	—	—	6,354	6,354	6,354	—	—	6,354
Financial liabilities:										
Deposits	$ 1,551,448	$ 1,550,030	$ —	$ 1,550,030	$ —	$1,551,448	$1,550,030	$ —	$1,550,030	$ —
Subordinate notes	19,623	17,876	—	17,876	—	19,623	17,876	—	17,876	—
Accrued interest payable	192	192	—	192	—	192	192	—	192	—

Note 12. Deposits

(Dollars in thousands)	**June 30, 2023**	December 31, 2022	**September 30, 2023**	December 31, 2022
Noninterest-bearing checking	**$ 287,385**	$ 299,231	**$ 295,181**	$ 299,231
Interest-bearing checking	**445,003**	496,533	**465,897**	496,533
Money management	**573,582**	569,585	**585,872**	569,585
Savings	**117,423**	128,709	**110,158**	128,709
Total interest-bearing checking and savings	**1,136,008**	1,194,827	**1,161,927**	1,194,827
Time deposits	**89,742**	57,390	**110,306**	57,390
Total deposits	**$ 1,513,135**	$ 1,551,448	**$1,567,414**	$1,551,448
Overdrawn deposit accounts reclassified as loans	**$ 158**	$ 103	**$ 120**	$ 103

Time deposits greater than $250,000 at June 30, 2023 and December 31, 2022 were $16.3 million and $8.8 million, respectively.

Time deposits greater than $250,000 at September 30, 2023 and December 31, 2022 were $30.0 million and $8.8 million, respectively.

Note 13. Borrowings

At June 30, 2023 September 30, 2023, the Bank had $70.0 million borrowed from the Federal Reserve's Bank Term Funding Program (BTFP) to temporarily support its liquidity position. This position and $40.0 million in short-term borrowing from the Federal Home Loan Bank of Pittsburgh (FHLB). The BTFP borrowing is comprised of $50.0 million with a rate of 4.38% due March 22, 2024, and $20.0 million with a rate of 4.71% due May 10, 2024. At June 30, 2023 September 30, 2023, the fair value of debt securities pledged for the BTFP was $69.7 million $79.8 million. The FHLB borrowings have a blended rate of 5.80% and are due during the third quarter of 2024.

At June 30, 2023 September 30, 2023, the Corporation had $20.0 million of unsecured subordinated debt notes payable, $15.0 million which mature on September 1, 2030 and $5.0 million which mature on September 1, 2035. The notes are recorded on the consolidated balance sheet net of remaining debt issuance costs totaling $357 $347 thousand at June 30, 2023 September 30, 2023, which is being amortized on a pro-rata basis, based on the maturity date of the notes, on an effective interest method. The subordinated notes totaling $15.0 million have a fixed interest rate of 5.00% through September 1, 2025, then convert to a variable rate of 90-day Secured Overnight Financing Rate (SOFR) plus 4.93% for the applicable interest periods through maturity. The subordinated notes totaling $5.0 million have a fixed interest rate of 5.25% through September 1, 2030, then convert to a variable rate of 90-day SOFR plus 4.92% for the applicable interest periods through maturity. The Corporation may, at its option, redeem the notes, in whole or in part, at any time 5-years prior to the maturity. The notes are structured to qualify as Tier 2 Capital for the Corporation and there are no debt covenants on the notes.

Note 14. Capital Ratios

Capital adequacy for the Bank is currently defined by regulatory agencies through the use of several minimum required ratios. The capital ratios to be considered "well capitalized" are: (1) Common Equity Tier 1 (CET1) of 6.5%, (2) Tier 1 Leverage of 5%, (3) Tier 1 Risk-Based Capital of 8%, and (4) Total Risk-Based Capital of 10%. In addition, a capital conservation buffer of 2.5% is applicable to all of the capital ratios except for the Tier 1 Leverage ratio. The capital conservation buffer is equal to the lowest value of the three applicable capital ratios less the regulatory minimum for each respective capital measurement. The Bank's capital conservation buffer at June 30, 2023 September 30, 2023 was 7.50% 6.28% compared to the regulatory buffer of 2.5%. Compliance with the capital conservation buffer is required in order to avoid limitations to certain capital distributions and is in addition to the minimum required capital requirements. As of June 30, 2023 September 30, 2023, the Bank was "well capitalized."

In 2019, the Community Bank Leverage Ratio (CBLR) was approved by federal banking agencies as an optional capital measure available to Qualifying Community Banking Organizations (QCBO). If a bank qualifies as a QCBO and maintains a CBLR of 9% or greater, the bank would be considered "well-capitalized" for regulatory capital purposes and exempt from complying with the risk-based capital rule described above. The CBLR rule took effect January 1, 2020 and banks could opt-in through an election in the first quarter 2020 regulatory filing. The Bank met the criteria of a QCBO but did not opt-in to the CBLR.

The consolidated asset limit on small bank holding companies is $3.0 billion and a company with assets under that limit is not subject to the consolidated capital rules but may file reports that include capital amounts and ratios. The Corporation has elected to file those reports.

The following table summarizes the regulatory capital requirements and results as of June 30, 2023 September 30, 2023 and December 31, 2022 for the Corporation and the Bank:

			Regulatory Ratios				Regulatory Ratios	
			Adequately	**Well**			**Adequately**	**Well**
(Dollars in thousands)	**June 30, 2023**	December 31, 2022	**Capitalized Minimum**	**Capitalized Minimum**	**September 30, 2023**	December 31, 2022	**Capitalized Minimum**	**Capitalized Minimum**
Common Equity Tier 1 Risk-based Capital Ratio (1)								
Franklin Financial Services Corporation	**13.88%**	14.22%	N/A	N/A	**12.43%**	14.22%	N/A	N/A

Farmers & Merchants Trust Company	**14.25%**	14.63%	4.50%	6.50%	**13.03%**	14.63%	4.50%	6.50%
Tier 1 Risk-based Capital Ratio (2)								
Franklin Financial Services Corporation	**13.88%**	14.22%	N/A	N/A	**12.43%**	14.22%	N/A	N/A
Farmers & Merchants Trust Company	**14.25%**	14.63%	6.00%	8.00%	**13.03%**	14.63%	6.00%	8.00%
Total Risk-based Capital Ratio (3)								
Franklin Financial Services Corporation	**16.84%**	17.21%	N/A	N/A	**15.16%**	17.21%	N/A	N/A
Farmers & Merchants Trust Company	**15.50%**	15.88%	8.00%	10.00%	**14.28%**	15.88%	8.00%	10.00%
Tier 1 Leverage Ratio (4)								
Franklin Financial Services Corporation	**9.39%**	8.95%	N/A	N/A	**9.10%**	8.95%	N/A	N/A
Farmers & Merchants Trust Company	**9.64%**	9.21%	4.00%	5.00%	**9.53%**	9.21%	4.00%	5.00%

(1) Common equity Tier 1 capital / total risk-weighted assets

(2) Tier 1 capital / total risk-weighted assets

(3) Total risk-based capital / total risk-weighted assets

(4) Tier 1 capital / average quarterly assets

Note 15. Revenue Recognition

All of the Corporation's revenue from contracts with customers within the scope of ASC 606 is recognized in non-interest income as presented in its consolidated statements of income. Revenue generating activities that fall within the scope of ASC 606 are described as follows:

Investment and Trust Service Fees – these represent fees from wealth management (assets under management), fees from the management and settlement of estates and commissions from the sale of investment and insurance products. Asset management fees are generally assessed based on a tiered fee schedule, based on the value of assets under management, and are recognized monthly when the service obligation is completed. Fees for estate management services are based on the estimated fair value of the estate. These fees are generally recognized monthly over an 18-month period that Management has determined to represent the average time to fulfill the performance obligations of the contract. Management has the discretion to adjust this time period as needed based upon the nature and complexity of an individual estate. Commissions from the sale of investment and insurance products are recognized upon the completion of the transaction.

The following table presents Investment and Trust Service Fees for the three and six nine months ended June 30, 2023 September 30, 2023 and 2022:

(Dollars in thousands)	For the Three Months Ended June 30,		For the Six Months Ended June 30,		For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
Investment and Trust Service Fees	**2023**	2022	**2023**	2022	**2023**	2022	**2023**	2022
Asset Management Fees	**$ 1,844**	$ 1,744	**$ 3,481**	$ 3,368	**$1,660**	$1,519	**$5,141**	$4,888
Estate Management Fees	**61**	129	**152**	302	**65**	113	**218**	415
Commissions	**54**	45	**160**	76	**58**	29	**217**	104
Total	**$ 1,959**	$ 1,918	**$ 3,793**	$ 3,746	**$1,783**	$1,661	**$5,576**	$5,407

Loan Service Charges – these represent fees on loans for services or charges that occur after the loan has been booked, for example, late payment fees. These also include fees for mortgages settled for third-party mortgage companies. All of

these fees are transactional in nature and are recognized upon completion of the transaction which represents the performance obligation.

Deposit Service Charges and Fees – these represent fees from deposit customers for transaction based, account maintenance, and overdraft services. Transaction based fees include, but are not limited to, stop payment fees and overdraft fees. These fees are recognized at the time of the transaction when the performance obligation has been fulfilled. Account maintenance fees and account analysis fees are earned over the course of a month, representing the period of the performance obligation, and are recognized monthly.

Debit Card Income – this represents interchange fees from cardholder transactions conducted through the card payment network. Cardholders use the debit card to conduct point-of-sale transactions that produce interchange fees. The fees are transaction based and the fee is recognized with the processing of the transaction. These fees are reported net of cardholder rewards.

Other Service Charges and Fees – these are comprised primarily of merchant card fees, credit card fees, ATM surcharges and interchange fees and wire transfer fees. Merchant card fees represent fees the Bank earns from a third party for enrolling a customer in the processor's program. Credit card fees represent a fee earned by the Bank for a successful referral to a card-issuing company. ATM surcharges and interchange fees are the result of Bank customers conducting ATM transactions that generate fee income and are processed through multiple card networks. All of these fees are transaction based and are recognized at the time of the transaction.

Gains/Losses on the Sale of Other Real Estate – these are recognized when control of the property transfers to the buyer.

Contract Balances

A contract asset balance occurs when an entity performs a service for a customer before the customer pays consideration (resulting in a contract receivable) or before payment is due (resulting in a contract asset). A contract liability balance is an entity's obligation to transfer a service to a customer for which the entity has already received payment (or payment is due) from the customer. The Company's noninterest revenue streams are largely based on transactional activity, or standard month-end revenue accruals such as asset management fees based on month-end market values. Consideration is often received immediately or shortly after the Company satisfies its performance obligation and revenue is recognized. The Company does not typically enter into longer-term revenue contracts with customers, and therefore, does not experience significant contract balances.

Contract Acquisition Costs

The Corporation expenses all contract acquisition costs as costs are incurred.

Note 16. Commitments and Contingencies

In the normal course of business, the Bank is a party to financial instruments that are not reflected in the accompanying financial statements and are commonly referred to as off-balance-sheet instruments. These financial instruments are entered into primarily to meet the financing needs of the Bank's customers and include commitments to extend credit and standby letters of credit. Those instruments involve, to varying degrees, elements of credit and interest rate risk not recognized in the consolidated balance sheet.

The Corporation's exposure to credit loss in the event of nonperformance by other parties to the financial instruments for commitments to extend credit and standby letters of credit is represented by the contract or notional amount of those instruments. The Bank uses the same credit policies in making commitments and conditional obligations as they do for on-balance-sheet instruments.

The Bank had the following outstanding commitments for the periods presented:

(Dollars in thousands)	**June 30, 2023**	December 31, 2022	**September 30, 2023**	December 31, 2022
Financial instruments whose contract amounts represent credit risk				
Commercial commitments to extend credit	**$ 356,488**	$ 275,867	**$ 318,116**	$ 275,867
Consumer commitments to extend credit (secured)	**95,459**	93,124	**101,059**	93,124
Consumer commitments to extend credit (unsecured)	**4,907**	5,247	**4,970**	5,247
	$ 456,854	$ 374,238	**$ 424,145**	$ 374,238
Standby letters of credit	**$ 28,264**	$ 30,734	**$ 28,341**	$ 30,734
ACL - Unfunded Commitments*	**$ 1,957**	$ 1,475	**$ 1,965**	$ 1,475

*Reported in Other Liabilities on the Consolidated Balance Sheet

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses with the exception of home equity lines and personal lines of credit and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Bank evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Bank, is based on Management's credit evaluation of the counterparty. Collateral for most commercial commitments varies but may include accounts receivable, inventory, property, plant, and equipment, and income-producing commercial properties. Collateral for secured consumer commitments consists of liens on residential real estate.

Standby letters of credit are instruments issued by the Bank, which guarantee the beneficiary payment by the Bank in the event of default by the Bank's customer in the nonperformance of an obligation or service. Most standby letters of credit are extended for one-year periods. Generally, the credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. The Bank holds collateral supporting those commitments for which collateral is deemed necessary primarily in the form of certificates of deposit and liens on real estate. Management believes that the proceeds obtained through a liquidation of such collateral would be sufficient to cover the maximum potential amount of future payments required under the corresponding guarantees.

On January 1, 2023, the Corporation adopted ASU 2016-13 Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments, referred to as the current expected credit loss (CECL) methodology. Upon adoption, $412 thousand was added to the allowance for credit losses (ACL) – unfunded commitments. For the second third quarter of 2023, the provision for credit losses-unfunded commitments was $8 $9 thousand compared to $0 for the second third quarter of 2022. Year-to-date 2023, the provision for credit losses on unfunded commitments was $70 $79 thousand compared to $0 for the same period in 2022.

Most of the Bank's business activity is with customers located within its primary market and does not involve any significant concentrations of credit to any one entity or industry.

Legal Proceedings

The nature of the Corporation's business generates a certain amount of litigation.

The Corporation establishes accruals for legal proceedings when information related to the loss contingencies represented by those matters indicates both that a loss is probable, and the amount of the loss can be reasonably estimated. When the Corporation is able to do so, it also determines estimates of possible losses, whether in excess of any accrued liability or where there is no accrued liability.

These assessments are based on the analysis of currently available information and are subject to significant judgment and a variety of assumptions and uncertainties. As new information is obtained, the Corporation may change its assessments and, as a result, take or adjust the amounts of its accruals and change its estimates of possible losses or ranges of possible losses. Due to the inherent subjectivity of the assessments and the unpredictability of outcomes of legal proceedings, any amounts that may be accrued or included in estimates of possible losses or ranges of possible losses may not represent the actual loss to the Corporation from any legal proceeding. Its exposure and ultimate losses may be higher, possibly significantly higher, than amounts it may accrue or amounts it may estimate.

In management's opinion, the Corporation does not anticipate, at the present time, that the ultimate aggregate liability, if any, arising out of all litigation to which the Corporation is a party at this time will have a material adverse effect on its financial position. The Corporation cannot now determine, however, whether or not any claim asserted against it will have a material adverse effect on its results of operations in any future reporting period, which will depend on, among other things, the amount of loss resulting from the claim and the amount of income otherwise reported for the reporting period. Thus, at June 30, 2023 September 30, 2023, the Corporation is unable to provide an evaluation of the likelihood of an unfavorable outcome or an estimate of the amount or range of potential loss with respect to such other matters and, accordingly, have not yet established any specific accrual for such other matters.

Note 17. Reclassification

Certain prior period amounts may have been reclassified to conform to the current year presentation. Such reclassifications did not affect prior year net income or shareholders' equity.

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

Forward Looking Statements

Certain statements appearing herein which are not historical in nature are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Such forward-looking statements refer to a future period or periods, reflecting management's current views as to likely future developments, and use words such as "may," "will," "expect," "believe," "estimate," "anticipate," or similar terms. Because forward-looking statements involve certain risks, uncertainties and other factors over which the Corporation has no direct control, actual results could differ materially from those contemplated in such statements. These factors include (but are not limited to) the following: general economic conditions, changes in the rates of inflation and the effects of inflation, changes in interest rates, ongoing disruption in the financial services industry caused by the recent failure bank failures and continuing uncertainty of various banks, changes in the Corporation's cost of funds, changes in government monetary policy, changes in government regulation and taxation of financial institutions, changes in technology, the intensification of competition within the Corporation's market area, and other similar factors. We caution readers not to place undue reliance on these forward-looking statements. They only reflect management's analysis as of this date. The Corporation does not revise or update these forward-looking statements to reflect events or changed circumstances.

Critical Accounting Policies

Management has identified critical accounting policies for the Corporation. These policies are particularly sensitive, requiring significant judgements, estimates and assumptions to be made by Management.

On January 1, 2023, the Corporation adopted ASU 2016-13 Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments, as amended, which replaces the incurred loss methodology with an expected loss methodology that is referred to as the current expected credit loss (CECL) methodology. The measurement of expected credit losses under the CECL methodology is applicable to financial assets measured at amortized cost, including loan receivables and held-to-maturity debt securities. It also applies to off-balance sheet credit commitments not accounted for as insurance (loan commitments, standby letters of credit, financial guarantees, and other similar instruments) and net investments in leases recognized by a lessor in accordance with Topic 842 on leases.

The Company adopted ASC 326 using the modified retrospective method for all financial assets measured at amortized cost, and unfunded credit exposures. Results for reporting periods beginning after January 1, 2023 are presented under ASC 326 while prior period amounts continue to be reported in accordance with the previously applicable incurred loss methodology.

The Corporation has determined this accounting policy to be critical to the results of operations. A summary of the adoption of the new ASU follows:

Investment Securities – Management classifies its debt securities at the time of purchase as available for sale (AFS) or held to maturity (HTM). At June 30, 2023 September 30, 2023 and December 31, 2022, all debt securities were classified as available for sale, meaning that the Corporation intends to hold them for an indefinite period of time, but not necessarily to maturity. Available for sale debt securities are stated at estimated fair value, adjusted for amortization of premiums and accretion of discounts which are recognized as adjustments of interest income through call date or maturity. The related unrealized gains and losses are reported as other comprehensive income or loss, net of tax, until realized.

With the adoption of CECL on January 1, 2023, the previous concept of other-than-temporary impairment for AFS securities has been eliminated. Under CECL, credit losses on AFS debt securities are recognized in (Allowance for Credit Losses) ACL for investments, through the provision for credit losses, rather than through a direct write-down of the security. In evaluating AFS securities for credit losses, Management considers factors such as delinquency, guarantees, invest grade rating, and specific conditions related to a specific security or industry. If an impaired debt security is sold, any previous ACL on that security is charged-off and any incremental loss will be recognized through earnings. Any improvement in expected credit losses will be recognized by reducing the ACL.

For HTM securities an estimate of current expected credit loss must be established at the time of purchase with changes in estimated credit loss recognized in the ACL through the provision for credit losses.

Prior to January 1, 2023, declines in the fair value of securities was recorded under the other-than-temporary impairment concept more fully described in the Corporation's report on Form 10-K as of December 31, 2022.

Realized securities gains and losses are computed using the specific identification method. Gains or losses on the disposition of debt investment securities are recorded on the trade date, based on the net proceeds and the adjusted carrying amount of the specific security sold. Equity investments are carried at fair value with changes in fair value recognized in net income.

Allowance for Credit Losses – Loans

The ACL for loans is established through provisions for credit losses charged against income. Loans deemed to be uncollectible are charged against the ACL, and subsequent recoveries, if any, are credited to the ACL.

The ACL for loans is an estimate of the losses expected to be realized over the life of the loan portfolio. The ACL is determined for two distinct categories of loans: 1) loans evaluated individually for expected credit losses (specific reserve), and 2) loans evaluated collectively for expected credit losses (pooled reserve). Management's periodic evaluation of the adequacy of the ACL for loans is based on the Bank's past loan loss experience, known and inherent risks in the portfolio, adverse situations that may affect the borrower's ability to repay, the estimated value of any underlying collateral, composition of the loan portfolio, current economic conditions, diversification of the loan portfolio, delinquency statistics, results of internal loan reviews, borrowers' actual or perceived financial and managerial strengths, and other relevant factors. This evaluation is inherently subjective, as it requires material assumptions and estimates that may be susceptible to significant change, including the amounts and timing of future cash flows expected to be received on impaired loans.

Loans evaluated individually for credit losses are primarily commercial purpose loans that do not share similar characteristics with those loans evaluated in the pool. These loans may exhibit performance characteristics where it is probable that the Bank will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. All commercial purpose loans greater than $250 thousand and rated Substandard (7), Doubtful (8) or on nonaccrual status may be considered for individual evaluation. Impairment is measured on a loan-by-loan basis by one of the following methods: the fair value of the collateral if the loan is collateral dependent, the present value of expected future cash flows discounted at the loan's effective interest rate or the loan's obtainable market price. Commercial purpose loans with a balance less than $250 thousand, and consumer purpose loans are not evaluated individually for a specific reserve but are included in the pooled reserve calculation. Loans that are evaluated for a specific reserve, but not needing a specific reserve are not included in the pooled reserve calculation.

The Corporation has elected to exclude accrued interest receivable from the measurement of the ACL. When a loan is placed on nonaccrual status, any outstanding accrued interest is reversed against income. In addition, ASC 326 made changes to the accounting for available-for-sale debt securities. One such change is to require credit losses to be presented as an allowance rather than as a write-down on available-for-sale debt securities management does not intend to sell or believes that it is more likely than not they will be required to sell.

The pooled reserve represents the ACL for pools of homogenous loans, not evaluated individually. The pooled reserve is calculated using a quantitative and qualitative component for the loan pools.

The following inputs are used to calculate the quantitative component for the pool:

- Segregating loans into homogeneous pools by the FRB Call Code which is primarily a collateral-based and secondarily a purpose-based segmentation.
- The average remaining life of each pool is calculated using the weighted average remaining maturity method (WARM). The WARM method produces an estimated remaining balance by pool, by year, until maturity.
- Using third party data, the Bank determines a reasonable and supportable economic forecast that it believes is likely to exist for the next 4 four quarters.
- A historical credit loss rate is calculated for each pool, using the average historical loss, by FRB Call Code, for a peer group of Pennsylvania community banks over the last eight quarters. The historical loss rate is calculated over a historical period the Bank believes best represents a period that will be similar to the next 4 four quarters.
- The historical peer credit loss rate is applied to each WARM bucket though the initial 4 four quarter forecast period.
- At the end of the forecast period, the credit loss rate applied to each WARM bucket reverts to the peer group historical loss rate for the respective pool.
- Collectively these estimated losses represent the quantitative component of the pooled reserve.

The qualitative component for the pool utilizes a risk matrix comprised of eight risk factors and assigns a risk level to each factor. The risk factors give consideration to consider changes in: lending policy, procedures and practice; economic conditions; nature and volume of loans; experience of lending team; volume of past due loans; quality of the loan review system; concentrations system; concentrations of credit; and other external factors. The risk factors are weighted to reflect Management's estimate of how the factor affects potential losses. The risk levels within each factor are measured in basis points and range from minimal risk (0 basis points) to very high risk (20 basis points); and collectively range from 0 to 160 basis points. The qualitative risk level is are determined independently for commercial loans, residential mortgage loans and consumer loans.

The ACL for pooled loans is the sum of the quantitative and qualitative loss estimates.

Allowance for Credit Losses – Unfunded Commitments

The ACL for unfunded commitments is recorded in other liabilities on the consolidated balance sheet. The ACL represents management's estimate of expected losses from unfunded commitments and is determined by estimating future usage of the commitments, based on historical usage. The estimated loss is calculated in a manner similar to that used for the ACL for loans, previously described. The ACL is increased or decreased through the provision for credit losses.

There were no other changes to the critical accounting policies disclosed in the 2022 Annual Report on Form 10-K in regards to application or related judgments and estimates used. Please refer to Item 7 of the Corporation's 2022 Annual Report on Form 10-K for a more detailed disclosure of the critical accounting policies.

Results of Operations

Summary

Franklin Financial Services Corporation reported consolidated earnings of $3.0 million $3.9 million ($0.68 0.88 per diluted share) for the second third quarter of 2023 compared to $3.6 million $4.6 million ($0.80 1.05 per diluted share) for the same period in 2022. Year-to-date 2023 net income was $6.3 million $10.1 million ($1.43 2.31 per diluted share) compared to $6.6 million $11.2 million ($1.47 2.52 per diluted share) for the same six-month nine-month period in 2022, a decrease of 9.6% 9.7%.

A summary of operating results for the second third quarter and year-to-date 2023 are as follows:

- Net income for the second third quarter of 2023 was $3.0 million $3.9 million ($0.68 0.88 per diluted share) compared to $3.3 million $3.0 million ($0.75 per diluted share) for the first quarter of 2023 (a decrease of 9.6%), and $3.6 million ($.80 0.68 per diluted share) for the second quarter of 2023 (an increase of 22.9%), and $4.6 million ($1.05 per diluted share) for the third quarter of 2022 (a decrease of 16.8% 16.7%).

- Net income For the third quarter of 2023, the provision for credit losses was $875 thousand compared to $524 thousand for the second quarter of 2023 was affected by a $517 thousand loss on and $0 for the sale third quarter of investment securities realized as part of a portfolio restructuring, and a loss of $495 thousand from the termination of a long-term real estate lease. 2022.

- Net income year-to-date for 2023 was $6.3 million $10.1 million ($1.42 2.31 per diluted share) compared to $6.6 million $11.2 million ($1.47 2.52 per diluted share) for the same period in 2022, a decrease of 4.9% 9.7%. Year-to-date net income As compared to the prior year-to-date results, 2023 was affected by a loss of $1.1 million on securities sales, taken as part of the portfolio restructuring, and the previously mentioned a lease termination expense. expense of $495 thousand and an increase of $1.9 million in the provision for credit losses.

- Total net loans increased $93.7 million (9.0%) to $1.131 billion 5.4% from $1.037 billion at the end of the second quarter of 2023 and 14.9% from December 31, 2022.

- Total deposits decreased $38.3 million (2.5%) to $1.513 billion increased 3.6% from $1.551 billion the end of the second quarter of 2023, and 1.0% from December 31, 2022. Borrowings from the Federal Reserve and FHLB totaled $110.0 million at December 31, 2022 September 30, 2023.

   Shareholder equity increased by $5.6 million, year-to-date, to $119.8 million, and the book value per share increased to $27.53.

- For the year-to-date period, Return on Average Assets (ROA) was 0.75% 0.78%, Return on Average Equity (ROE) was 10.56% 11.25% and the Net Interest Margin (NIM) was 3.35% 3.33%, compared to ROA of 0.74% 0.83%, ROE of 9.36% 11.12% and NIM of 2.80% 2.96% for the same period in 2022.

- On July 13, October 19, 2023, the Board of Directors declared a $0.32 per share regular quarterly cash dividend for the third fourth quarter of 2023 to be paid on August 23, 2023, November 22, 2023 to shareholders of record at the close of business on August 4, 2023 November 3, 2023.

Key performance ratios as of, or for the six three months ended June 30, 2023 September 30, 2023 and 2022 and the year ended December 31, 2022 are listed below:

(Dollars in thousands, except per share)	**June 30, 2023**	June 30, 2022	December 31, 2022	**September 30, 2023**	September 30, 2022	December 31, 2022
Balance Sheet Highlights						
Total assets	**$ 1,736,165**	$ 1,832,296	$ 1,699,579	**$1,827,910**	$1,847,162	$1,699,579
Investment and equity securities	**439,851**	510,282	487,247	**458,662**	492,467	487,247
Loans, net	**1,130,547**	1,019,608	1,036,866	**1,191,322**	1,033,518	1,036,866
Deposits	**1,513,135**	1,679,187	1,551,448	**1,567,414**	1,704,983	1,551,448
Shareholders' equity	**119,770**	121,797	114,197	**114,769**	108,151	114,197
Summary of Operations						
Interest income	**$ 35,094**	$ 24,409	$ 56,449	**$ 55,247**	$ 39,454	$ 56,449
Interest expense	**9,062**	1,490	4,863	**15,509**	2,471	4,863
Net interest income	**26,032**	22,919	51,586	**39,738**	36,983	51,586
Provision for credit losses - loans	**991**	—	—	**1,857**	—	—
Provision for credit losses - unfunded commitments	**70**	—	650	**79**	—	650
Net interest income after provision for loan losses	**24,971**	22,919	50,936	**37,802**	36,983	50,936
Noninterest income	**6,754**	7,976	15,250	**10,766**	11,639	15,250
Noninterest expense	**24,667**	23,296	48,691	**36,864**	35,496	48,691
Income before income taxes	**7,058**	7,599	17,495	**11,704**	13,126	17,495
Federal income tax expense	**790**	1,009	2,557	**1,577**	1,905	2,557
Net income	**$ 6,268**	$ 6,590	$ 14,938	**$ 10,127**	$ 11,221	$ 14,938
Performance Measurements						
Return on average assets*	**0.75%**	0.74%	0.83%	**0.78%**	0.83%	0.83%
Return on average equity*	**10.56%**	9.36%	11.64%	**11.25%**	11.12%	11.64%
Return on average tangible equity (1)*	**11.26%**	9.99%	12.52%	**12.13%**	11.89%	12.52%
Efficiency ratio (1)	**71.48%**	73.70%	71.21%	**70.24%**	71.34%	71.21%
Net interest margin*	**3.35%**	2.80%	3.11%	**3.33%**	2.96%	3.11%
Shareholders' Value (per common share)						
Diluted earnings per share	**$ 1.42**	$ 1.47	$ 3.36	**$ 2.31**	$ 2.52	$ 3.36
Basic earnings per share	**1.43**	1.48	3.38	**2.31**	2.53	3.38
Regular cash dividends declared	**0.64**	0.64	1.28	**0.96**	0.96	1.28
Book value	**27.53**	27.54	26.01	**26.31**	24.60	26.01
Tangible book value (1)	**25.46**	25.50	23.96	**24.24**	22.55	23.96
Market value	**27.74**	30.16	36.10	**28.50**	31.56	36.10
Market value/book value ratio	**100.76%**	109.51%	138.79%	**108.32%**	128.29%	138.79%
Market value/tangible book value ratio	**108.95%**	118.25%	150.67%	**117.55%**	139.95%	150.67%
Price/earnings multiple*	**9.77**	10.26	10.74	**9.25**	9.39	10.74
Current quarter dividend yield	**4.61%**	4.24%	3.55%	**4.49%**	4.06%	3.55%
Dividend payout ratio year-to-date	**44.77%**	43.22%	37.88%	**41.45%**	37.91%	37.88%

Safety and Soundness						
Average equity/average assets	**7.10%**	7.96%	7.17%	**6.98%**	7.49%	7.17%
Risk-based capital ratio (Total)	**16.84%**	17.36%	17.21%	**14.34%**	17.34%	17.21%
Leverage ratio (Tier 1)	**9.39%**	8.53%	8.95%	**9.10%**	8.59%	8.95%
Common equity ratio (Tier 1)	**13.88%**	14.30%	14.22%	**11.70%**	14.29%	14.22%
Nonperforming loans / gross loans	**0.02%**	0.55%	0.01%	**0.02%**	0.53%	0.01%
Nonperforming assets/total assets	**0.01%**	0.31%	0.01%	**0.01%**	0.30%	0.01%
Allowance for credit losses as a % of loans	**1.28%**	1.45%	1.35%	**1.29%**	1.43%	1.35%
Net loans (charged-off) recovered / average loans*	**0.00%**	-0.01%	-0.15%	**0.00%**	-0.01%	-0.15%
Assets under Management						
Trust assets under management (fair value)	$ **977,461**	$ 838,830	$ 904,317	$ **963,805**	$ 810,954	$ 904,317
Held at third-party brokers (fair value)	**127,807**	104,881	116,398	**126,394**	104,127	116,398

**Year-to-date annualized*

(1) See the section titled "GAAP versus Non-GAAP Presentation" that follows.

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GAAP versus non-GAAP Presentations – The Corporation supplements its traditional GAAP measurements with certain non-GAAP measurements to evaluate its performance and to eliminate the effect of intangible assets. By eliminating intangible assets (Goodwill), the Corporation believes it presents a measurement that is comparable to companies that have no intangible assets or to companies that have eliminated intangible assets in similar calculations. However, not all companies may use the same calculation method for each measurement. The non-GAAP measurements are not intended to be used as a substitute for the related GAAP measurements. Non-GAAP financial measures should be viewed in addition to, and not as an alternative for, our reported results prepared in accordance with GAAP. In the event of such a disclosure or release, the Securities and Exchange Commission's Regulation G requires: (i) the presentation of the most directly comparable financial measure calculated and presented in accordance with GAAP and (ii) a reconciliation of the differences between the non-GAAP financial measure presented and the most directly comparable financial measure calculated and presented in accordance with GAAP. The following table shows the calculation of the non-GAAP measurements as of, or for the six first nine months ended June 30, 2023 September 30, 2023 and 2022 and the year ended December 31, 2022.

(Dollars in thousands, except per share)

	June 30, 2023	December 31, 2022	June 30, 2022	September 30, 2023	December 31, 2022	September 30, 2022
Return on Tangible Equity (non-GAAP)						
Net income	$ **6,268**	$ 14,938	$ 6,590	$ **10,127**	$ 14,938	$ 11,221
Average shareholders' equity	**120,374**	128,283	141,986	**120,351**	128,283	134,898
Less average intangible assets	**(9,016)**	(9,016)	(9,016)	**(9,016)**	(9,016)	(9,016)
Average tangible equity (non-GAAP)	**111,358**	119,267	132,970	**111,335**	119,267	125,882
Return on average tangible equity (non-GAAP)*	**11.26%**	12.52%	9.99%	**12.13%**	12.52%	11.89%
Tangible Book Value (per share) (non-GAAP)						
Shareholders' equity	$ **119,770**	$ 114,197	$ 121,797	$ **114,769**	$114,197	$108,151
Less intangible assets	**(9,016)**	(9,016)	(9,016)	**(9,016)**	(9,016)	(9,016)
Tangible book value (non-GAAP)	**110,754**	105,181	112,781	**105,753**	105,181	99,135
Shares outstanding (in thousands)	**4,350**	4,390	4,422	**4,362**	4,390	4,396
Tangible book value per share (non-GAAP)	$ **25.46**	$ 23.96	$ 25.50	$ **24.24**	$ 23.96	$ 22.55
Efficiency Ratio						
Noninterest expense	$ **24,667**	$ 48,691	$ 23,296	$ **36,864**	$ 48,691	$ 35,496
Net interest income	**26,032**	51,586	22,919	**39,738**	51,586	36,983
Plus tax equivalent adjustment to net interest income	**573**	1,381	710	**835**	1,381	1,055

Plus noninterest income, net of securities transactions	**7,905**	15,410	7,980	**11,910**	15,410	11,719
Total revenue	**34,510**	68,377	31,609	**52,483**	68,377	49,757
Efficiency ratio (Noninterest expense/total revenue)	**71.48%**	71.21%	73.70%	**70.24%**	71.21%	71.34%
* Year-to-date annualized						

Net Interest Income

The largest source of the Corporation's earnings is net interest income, which is defined as the difference between income on interest-earning assets and the expense of interest-bearing liabilities supporting those assets. Principal categories of interest-earning assets are loans and securities, while deposits, short-term borrowings and long-term debt are the principal categories of interest-bearing liabilities. Demand deposits enhance net interest income because they are noninterest-bearing deposits. For the purpose of this discussion, balance sheet items refer to the average balance for the year and net interest income is adjusted to a fully taxable-equivalent basis. This tax-equivalent adjustment facilitates performance comparisons between taxable and tax-free assets by increasing the tax-free income by an amount equivalent to the Federal income taxes that would have been paid if this income were taxable at the Corporation's 21% Federal statutory rate.

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Comparison of the three months ended June 30, 2023 September 30, 2023 to the three months ended June 30, 2022 September 30, 2022:

Tax equivalent net interest income increased $1.0 million decreased $441 thousand to $13.5 million $14.0 million in the second third quarter of 2023 compared to $12.5 million $14.4 million for the same period in 2022. A The balance sheet volume change in rates contributed $1.5 million to the increase decreased tax-equivalent net interest income $1.1 million, which was partially offset by a balance sheet volume change an increase of $440 thousand.

The following table presents average balances, tax-equivalent (T/E) $637 thousand due to interest income, and yields earned or rates paid on the assets or liabilities. Loans are classified by type of collateral and residential loans include commercial purpose loans and nonaccrual loans are included in the average loan balance used to calculate the yield. All nontaxable interest income has been adjusted to a tax-equivalent basis using a tax rate of 21%.

	For the Three Months Ended June 30,					
	2023			2022		
(Dollars in thousands)	**Average balance**	**Income or expense**	**Average yield/rate**	Average balance	Income or expense	Average yield/rate
Interest-earning assets:						
Interest-earning obligations in other banks	**$ 64,851**	**$ 791**	**4.89%**	$ 189,584	$ 421	0.89%
Investment securities:						
Taxable	**398,289**	**3,338**	**3.36%**	425,097	2,172	2.05%
Tax exempt	**56,136**	**387**	**2.77%**	86,416	662	3.07%
Investments	**454,425**	**3,725**	**3.29%**	511,513	2,835	2.22%
Loans:						
Residential real estate 1-4 family:						
First liens	**165,322**	**1,809**	**4.39%**	138,820	1,393	4.02%
Junior liens and lines of credit	**72,923**	**1,006**	**5.53%**	72,921	482	2.65%
Residential real estate - construction	**18,537**	**285**	**6.16%**	19,784	286	5.80%
Commercial real estate	**608,963**	**7,962**	**5.24%**	545,658	5,601	4.12%
Commercial	**244,333**	**3,081**	**5.06%**	238,119	2,104	3.54%
Consumer	**6,219**	**129**	**8.31%**	5,899	101	6.87%
Loans	**1,116,297**	**14,272**	**5.13%**	1,021,200	9,967	3.91%
Total interest-earning assets	**1,635,573**	**$ 18,788**	**4.61%**	1,722,297	$ 13,224	3.08%
Other assets	**95,670**			86,101		
Total assets	**$ 1,731,243**			$ 1,808,398		
Interest-bearing liabilities:						

Deposits:						
Interest-bearing checking	**$ 446,491**	**$ 431**	**0.39%**	$ 540,491	$ 158	0.12%
Money Management	**563,760**	**3,316**	**2.36%**	601,685	259	0.17%
Savings	**120,193**	**45**	**0.15%**	129,732	18	0.06%
Time	**84,093**	**586**	**2.80%**	64,551	67	0.42%
Total interest-bearing deposits	**1,214,537**	**4,378**	**1.45%**	1,336,458	504	0.15%
Subordinated notes	**19,638**	**261**	**5.31%**	19,601	260	5.31%
Short-term borrowings	**61,209**	**677**	**4.44%**	—	—	-
Total interest-bearing liabilities	**1,295,384**	**5,316**	**1.65%**	1,356,059	764	0.23%
Noninterest-bearing deposits	**298,330**			313,023		
Other liabilities	**14,595**			10,120		
Shareholders' equity	**122,934**			129,196		
Total liabilities and shareholders' equity	**$ 1,731,243**			$ 1,808,398		
T/E net interest income/Net interest margin		**13,472**	**3.30%**		12,460	2.90%
Tax equivalent adjustment		**(277)**			(350)	
Net interest income		**$ 13,195**			$ 12,111	
Net Interest Spread			**2.96%**			2.85%
Cost of Funds			**1.34%**			0.18%
Cost of Deposits			**1.16%**			0.12%

Provision for Credit Losses

For the second quarter of 2023, the provision for credit losses was $532 thousand allocated between the provision for loans of $524 thousand and the provision for unfunded commitments of $8 thousand. The provision for loan loss expense for the second quarter of 2022 was $0. The ACL ratio for loans was 1.28% at June 30, 2023 compared to 1.35% at December 31, 2022. The ACL for unfunded commitments was $2.0 million compared to $1.5 million at December 31, 2022. For more information refer to the Loan Quality and Allowance for Credit Losses discussion in the Financial Condition section.

changes.

Noninterest Income

For the second quarter of 2023, noninterest income decreased $562 thousand from the same period in 2022. Debit card income increased but was offset by a decrease in gains on sale of loans as the volume of mortgages sold decreased. Losses on the sale of investment securities of $517 thousand were taken as part of a portfolio restructuring.

The following table presents a comparison of noninterest expense for the three months ended June 30, 2023 and 2022:

	For the Three Months Ended June 30,		Change	
(Dollars in thousands)	**2023**	2022	Amount	%
Noninterest Income				
Investment and trust services fees	**$ 1,959**	$ 1,918	$ 41	2.1
Loan service charges	**120**	240	(120)	(50.0)
Gain on sale of loans	**45**	255	(210)	(82.4)
Deposit service charges and fees	**616**	634	(18)	(2.8)
Other service charges and fees	**430**	437	(7)	(1.6)
Debit card income	**547**	438	109	24.9
Increase in cash surrender value of life insurance	**111**	109	2	1.8
Net losses on sales of debt securities	**(517)**	(19)	(498)	NA

Change in fair value of equity securities	**(8)**	4	(12)	(300.0)
Other	**226**	75	151	201.3
Total noninterest income	**$ 3,529**	$ 4,091	$ (562)	(13.7)

Noninterest Expense

Noninterest expense for the second quarter of 2023 increased $619 thousand compared to the same period in 2022. Salary expense increased primarily due to a highly competitive labor market, while net occupancy increased from costs associated with the new headquarters and operations center that was put in service in July 2022. A lease termination expense was recorded in the second quarter of 2023 for $495 thousand. The lease termination was a long-term real estate lease held for a new community banking office that will not be constructed.

The following table presents a comparison of noninterest expense for the three months ended June 30, 2023 and 2022:

	For the Three Months Ended			
(Dollars in thousands)	June 30,		Change	
Noninterest Expense	**2023**	2022	Amount	%
Salaries and benefits	**$ 7,283**	$ 7,045	$ 238	3.4
Net occupancy	**1,112**	979	133	13.6
Marketing and advertising	**550**	460	90	19.6
Legal and professional	**454**	484	(30)	(6.2)
Data processing	**1,118**	1,261	(143)	(11.3)
Pennsylvania bank shares tax	**174**	335	(161)	(48.1)
FDIC insurance	**198**	170	28	16.5
ATM/debit card processing	**307**	360	(53)	(14.7)
Telecommunications	**98**	106	(8)	(7.5)
Nonservice pension	**(29)**	69	(98)	(142.0)
Lease termination	**495**	—	495	NA
Other	**888**	760	128	16.8
Total noninterest expense	**$ 12,648**	**$** 12,029	**$** 619	5.1

Provision for Income Taxes

For the second quarter of 2023, the Corporation recorded a Federal income tax expense of $568 thousand compared to $595 thousand for the same quarter in 2022. The effective tax rate for the second quarter of 2023 was 16.0% compared to 14.3% for the same period in 2022. The federal statutory tax rate is 21% for 2023 and 2022.

Comparison of the six months ended June 30, 2023 to the six months ended June 30, 2022:

Tax equivalent net interest income increased $3.0 million to $26.6 million in the first half of 2023 compared to $23.6 million for the same period in 2022. A change in rates contributed $3.4 million to the increase which was offset by a balance sheet volume change of $431 thousand.

The following table presents average balances, tax-equivalent (T/E) interest income, and yields earned or rates paid on the assets or liabilities. Loans are classified by type of collateral and residential loans include commercial purpose loans and nonaccrual loans are included in the average loan balance used to calculate the yield. All nontaxable interest income has been adjusted to a tax-equivalent basis using a tax rate of 21%.

	For the Six Months Ended June 30,						**For the Three Months Ended September 30,**					
	2023			2022			**2023**			2022		
(Dollars in thousands)	**Average balance**	**Income or expense**	**Average yield/rate**	Average balance	Income or expense	Average yield/rate	**Average balance**	**Income or expense**	**Average yield/rate**	Average balance	Income or expense	Average yield/rate
Interest-earning assets:												
Interest-earning obligations in other banks	**$ 54,326**	**$ 1,214**	**4.50%**	$ 173,937	$ 520	0.60%	**$ 56,133**	**$ 720**	**5.09%**	$ 181,609	$ 1,022	2.23%
Investment securities:												

Taxable	402,784	6,796	3.40%	431,762	4,019	1.88%	406,761	3,849	3.75%	429,336	2,733	2.52%
Tax exempt	59,701	843	2.85%	86,980	1,324	3.07%	50,474	344	2.70%	84,624	659	3.09%
Investments	462,485	7,639	3.33%	518,741	5,343	2.08%	457,235	4,193	3.64%	513,959	3,392	2.62%
Loans:												
Residential real estate 1-4 family:												
First liens	157,841	3,423	4.37%	137,282	2,709	3.98%	179,698	2,059	4.55%	140,126	1,414	4.00%
Junior liens and lines of credit	72,926	1,931	5.34%	72,198	899	2.51%	72,460	1,045	5.72%	74,374	644	3.44%
Residential real estate - construction	21,456	591	5.56%	20,540	470	4.61%	19,058	333	6.93%	21,073	230	4.33%
Commercial real estate	586,218	14,894	5.12%	533,329	10,472	3.96%	650,470	8,827	5.38%	563,255	6,185	4.36%
Commercial	238,820	5,723	4.83%	242,065	4,505	3.75%	244,524	3,102	5.03%	245,173	2,396	3.88%
Consumer	6,165	252	8.23%	5,979	201	6.78%	6,387	137	8.51%	5,798	107	7.32%
Loans	1,083,426	26,814	4.99%	1,011,393	19,256	3.84%	1,172,597	15,503	5.25%	1,049,799	10,976	4.15%
Total interest-earning assets	1,600,237	$ 35,667	4.49%	1,704,071	$ 25,118	2.97%	1,685,965	$ 20,416	4.80%	1,745,367	$15,390	3.50%
Other assets	96,154			80,535			96,225			92,531		
Total assets	$ 1,696,391			$ 1,784,606			$1,782,190			$1,837,898		
Interest-bearing liabilities:												
Deposits:												
Interest-bearing checking	$ 458,211	$ 841	0.37%	$ 524,634	$ 302	0.12%	$ 455,299	$ 501	0.44%	$ 575,766	$ 206	0.14%
Money Management	560,672	6,054	2.18%	591,164	490	0.17%	578,408	3,818	2.62%	601,941	426	0.28%
Savings	123,527	94	0.15%	126,459	35	0.06%	113,797	44	0.15%	130,842	19	0.06%
Time	73,213	819	2.26%	68,457	139	0.41%	94,448	764	3.21%	61,688	66	0.42%
Total interest-bearing deposits	1,215,623	7,808	1.30%	1,310,714	966	0.15%	1,241,952	5,127	1.64%	1,370,237	717	0.21%
Subordinated notes	19,632	526	5.36%	19,596	523	5.34%	19,647	264	5.37%	19,609	263	5.36%
Short-term borrowings	33,094	728	4.44%	—	—	-						
Federal Reserve Bank borrowings							70,000	789	4.47%	—	—	-
FHLB advances							18,261	267	5.82%	—	—	-
Total interest-bearing liabilities	1,268,349	9,062	1.44%	1,330,310	1,489	0.23%	1,349,860	6,447	1.90%	1,389,846	980	0.28%
Noninterest-bearing deposits	293,196			302,669			297,190			313,781		
Other liabilities	14,472			9,641			14,835			10,659		
Shareholders' equity	120,374			141,986			120,305			123,612		
Total liabilities and shareholders' equity	$ 1,696,391			$ 1,784,606			$1,782,190			$1,837,898		
T/E net interest income/Net interest margin		26,605	3.35%		23,629	2.80%		13,969	3.29%		14,410	3.28%
Tax equivalent adjustment		(573)			(710)			(262)			(347)	
Net interest income		$ 26,032			$ 22,919			$13,707			$14,063	
Net Interest Spread			3.05%			2.75%			2.90%			3.22%
Cost of Funds			1.17%			0.18%			1.55%			0.23%
Cost of Deposits			1.04%			0.12%			1.32%			0.17%

Provision for Credit Losses

For the first half third quarter of 2023, the provision for credit losses was $1.1 million $875 thousand allocated between the provision for loans of $991 $866 thousand and the provision for unfunded commitments of $70 $9 thousand. The provision for loan loss expense

for the first half third quarter of 2022 was $0. The ACL ratio for loans was 1.28% 1.29% at June 30, 2023 September 30, 2023 compared to 1.35% at December 31, 2022. The ACL for unfunded commitments was $2.0 million compared to $1.5 million at December 31, 2022. For more information refer to the Loan Quality and Allowance for Credit Losses discussion in the Financial Condition section.

Noninterest Income

For the third quarter of 2023, noninterest income increased $350 thousand from the same period in 2022. Investment and trust income increased from asset management fees. Debit card income increased but was offset by a decrease in gains on sale of loans as the volume of mortgages sold decreased. The increase in other income was due in part to a state sales tax refund of $107 thousand.

The following table presents a comparison of noninterest expense for the three months ended September 30, 2023 and 2022:

	For the Three Months Ended September 30,		Change	
(Dollars in thousands)	**2023**	2022	Amount	%
Noninterest Income				
Investment and trust services fees	**$ 1,783**	$ 1,661	$ 122	7.3
Loan service charges	**235**	177	58	32.8
Gain on sale of loans	**33**	183	(150)	(82.0)
Deposit service charges and fees	**649**	629	20	3.2
Other service charges and fees	**472**	443	29	6.5
Debit card income	**568**	497	71	14.3
Increase in cash surrender value of life insurance	**114**	109	5	4.6
Net losses on sales of debt securities	**—**	(15)	15	NA
Change in fair value of equity securities	**7**	(61)	68	(111.5)
Other	**152**	40	112	280.0
Total noninterest income	**$ 4,013**	$ 3,663	$ 350	9.6

Noninterest Expense

Noninterest expense for the third quarter of 2023 was flat compared to the same period in 2022. Data processing costs increased due to the timing of several annual invoices. Other expenses increased due to small increases across multiple line items.

The following table presents a comparison of noninterest expense for the three months ended September 30, 2023 and 2022:

	For the Three Months Ended September 30,		Change	
Noninterest Expense *(Dollars in thousands)*	**2023**	2022	Amount	%
Salaries and benefits	**$ 6,982**	$ 7,050	$ (68)	(1.0)
Net occupancy	**1,093**	1,124	(31)	(2.8)
Marketing and advertising	**531**	433	98	22.6
Legal and professional	**588**	581	7	1.2
Data processing	**1,300**	1,146	154	13.4
Pennsylvania bank shares tax	**174**	335	(161)	(48.1)
FDIC insurance	**230**	197	33	16.8
ATM/debit card processing	**320**	359	(39)	(10.9)
Telecommunications	**103**	114	(11)	(9.6)
Nonservice pension	**(29)**	69	(98)	(142.0)
Lease termination	**—**	—	—	NA
Other	**906**	792	114	14.4
Total noninterest expense	**$ 12,198**	**$** 12,200	**$** (2)	(0.0)

Provision for Income Taxes

For the third quarter of 2023, the Corporation recorded a Federal income tax expense of $788 thousand compared to $895 thousand for the same quarter in 2022. The effective tax rate for the third quarter of 2023 was 17.0% compared to 16.2% for the same period in 2022. The federal statutory tax rate is 21% for 2023 and 2022.

Comparison of the nine months ended September 30, 2023 to the nine months ended September 30, 2022:

Tax equivalent net interest income increased $2.5 million to $40.6 million in the first nine months of 2023 compared to $38.0 million for the same period in 2022. A change in rates contributed $4.1 million to the increase which was offset by a balance sheet volume change of $1.6 million.

The following table presents average balances, tax-equivalent (T/E) interest income, and yields earned or rates paid on the assets or liabilities. Loans are classified by type of collateral and residential loans include commercial purpose loans and nonaccrual loans are included in the average loan balance used to calculate the yield. All nontaxable interest income has been adjusted to a tax-equivalent basis using a tax rate of 21%.

	For the Nine Months Ended September 30,					
	2023			2022		
(Dollars in thousands)	Average balance	Income or expense	Average yield/rate	Average balance	Income or expense	Average yield/rate
Interest-earning assets:						
Interest-earning obligations in other banks	$ 54,935	$ 1,934	4.71%	$ 176,523	$ 1,542	1.17%
Investment securities:						
Taxable	404,126	10,645	3.52%	428,572	6,753	2.11%
Tax exempt	56,590	1,184	2.80%	88,558	1,980	2.99%
Investments	460,716	11,829	3.43%	517,130	8,733	2.26%
Loans:						
Residential real estate 1-4 family:						
First liens	165,206	5,482	4.44%	138,241	4,124	3.99%
Junior liens and lines of credit	72,769	2,976	5.47%	72,932	1,543	2.83%
Residential real estate - construction	20,648	924	5.98%	20,720	701	4.52%
Commercial real estate	607,870	23,720	5.22%	543,412	16,657	4.10%
Commercial	240,742	8,828	4.90%	243,113	6,901	3.80%
Consumer	6,240	389	8.33%	5,918	307	6.94%
Loans	1,113,475	42,319	5.08%	1,024,336	30,233	3.95%
Total interest-earning assets	1,629,126	$ 56,082	4.60%	1,717,989	$ 40,509	3.15%
Other assets	96,178			83,627		
Total assets	$ 1,725,304			$ 1,801,614		
Interest-bearing liabilities:						
Deposits:						
Interest-bearing checking	$ 457,230	$ 1,342	0.39%	$ 541,865	$ 508	0.13%
Money Management	566,649	9,872	2.33%	594,796	917	0.21%
Savings	120,248	137	0.15%	127,936	55	0.06%
Time	80,369	1,583	2.63%	66,176	205	0.41%
Total interest-bearing deposits	1,224,496	12,934	1.41%	1,330,773	1,684	0.17%
Subordinated notes	19,637	790	5.35%	19,600	787	5.34%
Federal Reserve Bank borrowings	45,531	1,518	4.46%	—	—	-
FHLB advances	6,154	267	5.80%	—	—	-
Total interest-bearing liabilities	1,295,818	15,509	1.60%	1,350,373	2,471	0.24%
Noninterest-bearing deposits	294,542			306,358		
Other liabilities	14,593			9,985		
Shareholders' equity	120,351			134,898		
Total liabilities and shareholders' equity	$ 1,725,304			$ 1,801,614		
T/E net interest income/Net interest margin		40,573	3.33%		38,038	2.96%
Tax equivalent adjustment		(835)			(1,055)	
Net interest income		$ 39,738			$ 36,983	

Net Interest Spread	**3.00%**	2.91%
Cost of Funds	**1.30%**	0.20%
Cost of Deposits	**1.14%**	0.14%

Provision for Credit Losses

For the first nine months of 2023, the provision for credit losses was $1.9 million allocated between the provision for loans of $1.9 million and the provision for unfunded commitments of $79 thousand. The provision for loan loss expense for the first nine months of 2022 was $0. The ACL ratio for loans was 1.29% at September 30, 2023 compared to 1.35% at December 31, 2022. The ACL for unfunded commitments was $2.0 million compared to $1.5 million at December 31, 2022. For more information refer to the Loan Quality and Allowance for Credit Losses discussion in the Financial Condition section.

Noninterest Income

For the first half nine months of 2023, noninterest income decreased $1.2 million $873 thousand from the same period in 2022. Debit card income increased but was offset by a decrease in gains on sale of loans as the volume of mortgages sold decreased. Losses on the sale of investment securities of $1.1 million were taken as part of a portfolio restructuring.

The following table presents a comparison of noninterest income for the six nine months ended June 30, 2023 September 30, 2023 and 2022:

	For the Six Months Ended June 30,		Change		For the Nine Months Ended September 30,		Change	
(Dollars in thousands)	**2023**	2022	Amount	%	**2023**	2022	Amount	%
Noninterest Income								
Investment and trust services fees	**$ 3,793**	$ 3,746	$ 47	1.3	**$ 5,576**	$ 5,407	$ 169	3.1
Loan service charges	**422**	356	66	18.5	**658**	533	125	23.5
Gain on sale of loans	**118**	509	(391)	(76.8)	**150**	692	(542)	(78.3)
Deposit service charges and fees	**1,199**	1,257	(58)	(4.6)	**1,848**	1,885	(37)	(2.0)
Other service charges and fees	**862**	849	13	1.5	**1,334**	1,293	41	3.2
Debit card income	**1,050**	896	154	17.2	**1,618**	1,393	225	16.2
Increase in cash surrender value of life insurance	**220**	217	3	1.4	**333**	326	7	2.1
Net losses on sales of debt securities	**(1,119)**	(19)	(1,100)	5,789.5	**(1,119)**	(34)	(1,085)	3,191.2
Change in fair value of equity securities	**(32)**	15	(47)	(313.3)	**(25)**	(46)	21	(45.7)
Other	**241**	150	91	60.7	**393**	190	203	106.8
Total noninterest income	**$ 6,754**	$ 7,976	$ (1,222)	(15.3)	**$10,766**	$11,639	$ (873)	(7.5)

Noninterest Expense

Noninterest expense for the first half nine months of 2023 increased $1.4 million compared to the same period in 2022. Salary expense increased primarily due to a highly competitive labor market, while net occupancy increased from costs associated with the new headquarters and operations center that was put in service in July 2022. A lease termination expense was recorded in the second quarter of 2023 for $495 thousand. The lease termination was a long-term real estate lease held for a new community banking office that will not be constructed.

The following table presents a comparison of noninterest expense for the six first nine months ended June 30, 2023 September 30, 2023 and 2022:

(Dollars in thousands)	For the Six Months Ended June 30,	Change	For the Nine Months Ended September 30,	Change

Noninterest Expense	2023	2022	Amount	%	2023	2022	Amount	%
Salaries and employee benefits	$ 14,220	$ 13,410	$ 810	6.0	$21,202	$20,403	$ 799	3.9
Net occupancy	2,222	1,952	270	13.8	3,315	3,077	238	7.7
Marketing and advertising	1,069	957	112	11.7	1,600	1,391	209	15.0
Legal and professional	1,005	999	6	0.6	1,593	1,580	13	0.8
Data processing	2,178	2,398	(220)	(9.2)	3,478	3,544	(66)	(1.9)
Pennsylvania bank shares tax	397	478	(81)	(16.9)	571	813	(242)	(29.8)
FDIC insurance	380	353	27	7.6	610	550	60	10.9
ATM/debit card processing	601	706	(105)	(14.9)	920	1,065	(145)	(13.6)
Telecommunications	197	199	(2)	(1.0)	300	313	(13)	(4.2)
Nonservice pension	(59)	138	(197)	(142.8)	(88)	207	(295)	(142.5)
Lease termination	495	—	495	NA	495	—	495	NA
Other	1,962	1,706	256	15.0	2,868	2,553	315	12.3
Total noninterest expense	$ 24,667	$ 23,296	$ 1,371	5.9	$36,864	$35,496	$1,368	3.9

Provision for Income Taxes

For the first half nine months of 2023, the Corporation recorded a Federal income tax expense of $790 thousand $1.6 million compared to $1.0 million $1.9 million for the same period in 2022. The effective tax rate for the first half nine months of 2023 was 11.2% 13.5% and reflects the benefit of a $280 thousand tax credit recorded during the first half nine months of 2023. Without the tax credit, the effective rate would have been 15.2% 15.9% compared to 13.3% 14.5% for the first half nine months of 2022. The federal statutory tax rate is 21% for 2023 and 2022.

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Financial Condition

Cash and Cash Equivalents:

Cash and cash equivalents totaled $64.8 million $74.0 million at June 30, 2023 September 30, 2023, a decrease an increase of $100 thousand $9.1 million from the prior year-end balance of $64.9 million. Short-term interest-earning deposits are held primarily at the Federal Reserve ($46.9 53.4 million).

Investment Securities:

AFS Securities: The At September 30, 2023, the AFS securities portfolio has decreased $51.6 million on had an amortized cost basis since of $525.5 million, a decrease of $22.8 million from the prior year-end, 2022. The portfolio is comprised primarily of mortgage and asset-backed securities issued by U.S. Agencies and municipal securities at approximately 32% and 31% of the portfolio had a fair value respectively. of $458.3 million, a decrease of $28.6 million from the prior year-end. The weighted average life Bank sold $41.2 million of securities taking advantage of higher market interest rates while restructuring the portfolio was 5.5 years and the effective duration is 4.30%.

AFS portfolio. The AFS securities portfolio had a net unrealized loss of $57.3 million $67.3 million at June 30, 2023 September 30, 2023 compared to a net unrealized loss of $61.5 million at the prior year-end. This change was primarily due to an increase in long-term interest rates over the period despite the Bank realizing $1.1 million of losses during the year due to restructuring of the portfolio and a decrease in long-term market interest rates. portfolio. The AFS portfolio averaged $454.4 million $457.2 million with a tax-equivalized yield of 3.29% 3.64% for the three months ended June 30, 2023 September 30, 2023. This compares to an average of $511.5 million $514.0 million and a tax-equivalized yield of 2.22% 2.62% for the same period in 2022. Impairment in The weighted average life of the investment AFS portfolio measured by gross unrealized losses, was $57.3 million, compared to $61.5 million at December 31, 2022 is 5.1 years and the effective duration is 4.57%.

The municipal bond AFS portfolio had the largest gross unrealized loss of $25.6 million held $83.7 million, 45% or 16% of the total gross unrealized loss. portfolio, of securities issued by the U.S. Treasury and another $147.1 million, or 28% of the total portfolio, of mortgage and asset-backed securities issued by a U.S. Government Agency or a government sponsored entity and securitized by pools of residential mortgages and other loan assets.

Municipal bond holdings in the AFS portfolio were $161.7 million, or 31% of the total portfolio. The municipal bond portfolio is holdings are well diversified geographically (154 issuers) and is are comprised primarily of general obligation bonds (68%). Many municipal bonds have credit enhancements in the form of private bond insurance or other credit support. The largest geographic municipal bond exposure is exposures are in the states of Texas (15%), California (13%), Pennsylvania (12%), and Michigan (10%). The average rating of the municipal portfolio holdings from Moody's is AA. No municipal bonds securities in the portfolio are rated below investment grade.

The corporate bond holdings in the AFS portfolio is were $26.3 million, or 5% of the total portfolio, comprised predominantly of 46 fixed rate community bank issued subordinated notes with totaling $22.1 million. All of the subordinated

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notes are unrated. The Bank monitors the credit of the issuers of the subordinated notes on a fair value quarterly basis. The remaining corporate bond holdings consist of $19.0 million five trust preferred securities and gross unrealized losses of $3.2 million. The majority of these securities are not investment grade rated.

The non-agency mortgage and asset-backed securities portfolio had a gross unrealized loss was $106.8 million, or 20% of $4.9 million. the total portfolio, at September 30, 2023, an increase of $36.0 million from the prior year-end. The majority of these securities, with a fair value of $44.7 million $84.7 million, are investment grade rated while the remaining $23.0 million $22.1 million of fair value securities in this portfolio are unrated. Many of these the securities in this portfolio have credit enhancement enhancements in the form of subordination and overcollateralization.

At June 30, 2023, Impairment in the AFS securities portfolio, measured by gross unrealized losses, were $67.3 million at September 30, 2023 compared to $61.5 million at December 31, 2022. The Bank believes it will be able to collect all interest and principal due on impaired securities and the decline in fair value below amortized cost is due to changing interest rates and not due to credit related factors; therefore, the Bank has no allowance for credit loss for these investments. The Bank does not have the intent to sell and does not believe it will more likely than not be required to sell, any of these securities prior to a recovery of their fair value to amortized cost.

Restricted Stock at Cost: The Bank held $694 thousand $2.3 million of restricted stock at June 30, 2023 September 30, 2023. Except for $30 thousand, this investment represents stock in FHLB Pittsburgh. The Bank is required to hold this stock to be a member of FHLB and it is carried at cost of $100 per share. The level of FHLB stock held is determined by FHLB and is comprised of a minimum membership amount plus a variable activity amount. FHLB stock is evaluated for impairment primarily based on an assessment of the ultimate recoverability of its cost. As a government sponsored entity, FHLB has the ability to raise funding through the U.S. Treasury that can be used to support its operations. There is not a public market for FHLB stock and the benefits of FHLB membership (e.g., liquidity and low-cost funding) add value to the stock beyond purely financial measures. Management intends to remain a member of the FHLB and believes that it will be able to fully recover the cost basis of this investment.

See Note 4 of the accompanying financial statements for additional information on Investment Securities.

Loans:

Residential real estate: This category is comprised of consumer purpose loans secured by residential real estate and to a lesser extent, commercial purpose loans secured by residential real estate. The consumer purpose category represents traditional residential mortgage loans and home equity products (primarily junior liens and lines of credit). Commercial purpose loans in this category represent loans made for various business needs but are secured with residential real estate. In addition to the real estate collateral, it is possible that additional security is provided by personal guarantees or UCC filings. These loans are underwritten as commercial loans and are not originated to be sold.

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Total residential real estate loans increased by $23.9 million $40.9 million over year-end 2022. For the first six nine months of 2023, the Bank originated $8.3 million $10.7 million of mortgages held for sale and sold $8.6 million $10.2 million through third party brokerage agreements. The Bank does not originate or hold any loans that would be considered sub-prime or Alt-A and does not generally originate mortgages outside of its primary market area.

Residential real estate construction: This category contains loans for the vertical construction of 1-4 family residential properties. The largest component of this category represents loans to residential real estate developers ($10.2 11.3 million), while loans for individuals to construct personal residences totaled $7.9 million $9.8 million at June 30, 2023 September 30, 2023. The Bank's exposure to residential construction loans is concentrated primarily in south central Pennsylvania. Real estate construction loans, including residential real estate and land development loans, occasionally provide an interest reserve in order to assist the developer during the development stage when minimal cash flow is generated. All real estate construction loans are underwritten in the same manner, regardless of the use of an interest reserve.

Commercial real estate (CRE): This category includes commercial, industrial, farm and agricultural loans and land development loans, where real estate serves as the primary collateral for the loans. Total commercial real estate loans increased to $638.1 million $671.2 million from $566.7 million at the end of 2022. The largest sectors (by collateral) in the commercial real estate category are: apartment buildings ($105.7 million), hotels and motels ($82.4 112.2 million), office buildings ($80.7 82.9 million), hotels & motels ($81.6 million), shopping centers ($56.6 69.3 million), and development land ($50.0 54.6 million). Within the office building portfolio, approximately 27% 27.4% of total office building exposure is to owner occupied properties. The majority of the Bank's hotel exposure is located along the Interstate 81 (I-81) corridor through south-central Pennsylvania. The portfolio is comprised of properties operating under 12 flagged brands and 3 independent operators.

Also included in CRE are real estate construction loans totaling $92.0 million $120.0 million. At June 30, 2023 September 30, 2023, the Bank had $38.0 million $52.3 million in real estate construction loans funded with an interest reserve and capitalized $609 thousand $1.2 million of interest in 2023 from these reserves on active projects for commercial construction. Real estate construction loans are monitored on a regular basis by either an independent third-party inspector or the assigned loan officer depending on loan amount or complexity

of the project. This monitoring process includes at a minimum, the submission of invoices and American Institute of Architects (AIA) documents (depending on the complexity of the project) detailing costs incurred by the borrower, on-site inspections, and a signature by the assigned loan officer for disbursement of funds.

Commercial: This category includes commercial, industrial, farm, agricultural, and municipal loans. Commercial loans increased $5.0 million $13.5 million to $240.6 million $249.1 million at June 30, 2023 September 30, 2023, compared to $235.6 million at the end of 2022. At June 30, 2023 September 30, 2023, the balance of PPP loans was $78 $68 thousand, down from $179 thousand at year-end. At June 30, 2023 September 30, 2023, the Bank had approximately $119.0 million $117.1 million in tax-free loans. The largest sectors (by industry) in the commercial category are: utilities ($43.2 million), public administration ($42.6 45.3 million), utilities ($41.3 million), real estate rental and leasing ($24.8 25.9 million), manufacturing ($16.9 23.2 million) and retail trade ($16.7 19.1 million).

Participations: The Bank may supplement its own commercial loan production by purchasing loan participations. These participations are primarily located in south-central Pennsylvania. At June 30, 2023 September 30, 2023, the outstanding commercial participations were $83.8 million $86.2 million, or 8.8% 8.6%, of commercial purpose loans and 7.3% 7.1% of total gross loans compared to $70.6 million at December 31, 2022, or 8.0%, of commercial purpose loans and 6.7% of total gross loans. The Bank's total exposure (including outstanding balances and unfunded commitments) to purchased participations is $110.5 million $122.4 million, compared to $90.0 million at December 31, 2022. The commercial loan participations are comprised of $21.7 million $23.0 million of Commercial loans and $62.1 million $63.2 million of CRE loans, reported in the respective loan class.

Consumer loans: This category had a balance of $6.3 million $6.4 million at June 30, 2023 September 30, 2023, compared to $6.2 million at prior year-end and is comprised primarily of installment loans and personal lines of credit.

The following table presents a summary of loans outstanding, by class as of:

(Dollars in thousands)	**June 30, 2023**	December 31, 2022	Change Amount	Change %	**September 30, 2023**	December 31, 2022	Change Amount	Change %
Residential Real Estate 1-4 Family								
Consumer first liens	$ **106,546**	$ 82,795	$ 23,751	28.7	$ **124,289**	$ 82,795	$ 41,494	50.1
Commercial first lien	**63,218**	61,702	1,516	2.5	**62,942**	61,702	1,240	2.0
Total first liens	**169,764**	144,497	25,267	17.5	**187,231**	144,497	42,734	29.6

Consumer junior liens and lines of credit	**68,463**	69,561	(1,098)	(1.6)	**68,141**	69,561	(1,420)	(2.0)
Commercial junior liens and lines of credit	**3,888**	4,127	(239)	(5.8)	**3,685**	4,127	(442)	(10.7)
Total junior liens and lines of credit	**72,351**	73,688	(1,337)	(1.8)	**71,826**	73,688	(1,862)	(2.5)
Total residential real estate 1-4 family	**242,115**	218,185	23,930	11.0	**259,057**	218,185	40,872	18.7
Residential real estate - construction								
Consumer	**7,868**	13,908	(6,040)	(43.4)	**11,264**	13,908	(2,644)	(19.0)
Commercial	**10,165**	10,485	(320)	(3.1)	**9,820**	10,485	(665)	(6.3)
Total residential real estate construction	**18,033**	24,393	(6,360)	(26.1)	**21,084**	24,393	(3,309)	(13.6)
Commercial real estate	**638,132**	566,662	71,470	12.6	**671,182**	566,662	104,520	18.4
Commercial	**240,555**	235,602	4,953	2.1	**249,119**	235,602	13,517	5.7
Total commercial	**878,687**	802,264	76,423	9.5	**920,301**	802,264	118,037	14.7
Consumer	**6,327**	6,199	128	2.1	**6,408**	6,199	209	3.4
	1,145,162	1,051,041	94,121	9.0	**1,206,850**	1,051,041	155,809	14.8
Less: Allowance for credit losses	**(14,615)**	(14,175)	(440)	3.1	**(15,528)**	(14,175)	(1,353)	9.5
Net Loans	**$ 1,130,547**	$ 1,036,866	$ 93,681	9.0	**$1,191,322**	$1,036,866	$154,456	14.9

Loan Quality:

Management monitors loan performance on a monthly basis and performs a quarterly evaluation of the adequacy of the Allowance for Credit Loss for loans (ACL). The Bank begins enhanced monitoring of all loans rated 6–OAEM or worse and obtains a new appraisal or asset valuation for any loans placed on nonaccrual and rated 7 - Substandard or worse. Management, at its discretion, may determine that additional adjustments to the appraisal or valuation are required. Valuation adjustments will be made as necessary based on factors, including, but not limited to: the economy, deferred maintenance, industry, type of property/equipment, age of the appraisal, etc. and the knowledge Management has about a particular situation. In addition, the cost to sell or liquidate the collateral is also estimated and deducted from the valuation in order to determine the net realizable value to the Bank. When determining the ACL, certain factors involved in the evaluation are inherently subjective and require material estimates that may be susceptible to significant change, including the amounts and timing of future cash flows. Management monitors the adequacy of the ACL on an ongoing basis and reports its adequacy quarterly to the Board Enterprise Risk Management Committee of the Board of Directors. Management believes the ACL at June 30, 2023 September 30, 2023 is adequate.

Watch list loans exhibit financial weaknesses that increase the potential risk of default or loss to the Bank. However, inclusion on the watch list, does not by itself, mean a loss is certain. The watch list totaled $10.0 million $10.4 million at June 30, 2023 September 30, 2023 compared to $11.6 million at December 31, 2022. The watch list includes both performing and nonperforming loans. Included in the watchlist total are $102 $213 thousand of nonaccrual loans. The credit composition of the watch list (loans rated 6, 7, or 8), by primary collateral is shown in Note 6 of the accompanying financial statements.

Delinquent loans are a result of borrowers' cash flow and/or alternative sources of cash being insufficient to repay loans. The Bank's likelihood of collateral liquidation to repay the loans becomes more probable the further behind a borrower falls, particularly when loans reach 90 days or more past due. Management monitors the performance status of loans by the use of an aging report. The aging report can provide an early indicator of loans that may become severely delinquent and possibly result in a loss to the Bank. See Note 6 in the accompanying financial statements for a table that presents the aging of payments in the loan portfolio.

Nonaccruing loans generally represent Management's determination that the borrower will be unable to repay the loan in accordance with its contractual terms and that collateral liquidation may or may not fully repay both interest and principal. It is the Bank's policy to evaluate the probable collectability of principal and interest due under terms of loan contracts for

all loans 90-days or more past due, nonaccrual loans, or impaired loans. Further, it is the Bank's policy to discontinue accruing interest on loans that are not adequately secured and in the process of collection. Upon determination of nonaccrual status, the Bank subtracts any current year accrued and unpaid interest from its income, and any prior year accrued and unpaid interest from the allowance for loan losses. Management continually monitors the status of nonperforming loans, the value of any collateral and potential of risk of loss. Nonaccrual loans are rated no better than 7-Substandard.

The Bank's Loan Management Committee reviews these loans and risk ratings on a quarterly basis in order to proactively identify and manage problem loans. In addition, a committee meets monthly to discuss possible workout strategies for all credits rated 7-Substandard or worse. Management also tracks other commercial loan risk measurements including high loan to value loans, concentrations, participations and policy exceptions and reports these to the Board Enterprise Risk Management Committee of the Board of Directors. The Bank also uses an external loan review consultant to assist with internal loan review with a goal of reviewing up to 80% of commercial loans each year. The FDIC defines certain supervisory loan-to-value lending limits. The Bank's internal loan–to-value limits are all equal to or have a lower loan-to-value limit than the supervisory limits. However, in certain instances, the Bank may make a loan that exceeds the supervisory loan-to-value limit. At June 30, 2023 September 30, 2023, the Bank had loans of $14.3 million (7.4% $14.2 million (7.6% of total risk-based capital) that exceeded the supervisory limit, compared to 7.2% at year-end 2022.

Loan quality, improved, as measured by nonaccrual loans, with had a balance of $102 $213 thousand at June 30, 2023 September 30, 2023 compared to $120 thousand at December 31, 2022 and the nonperforming loan to total loans ratio remained the same was 0.02% at September 30, 2023 compared to 0.01% at June 30, 2023 and December 31, 2022. Loans past due 90-days or more, but still accruing, totaled $94 $14 thousand at June 30, 2023 September 30, 2023.

In addition to monitoring nonaccrual loans, the Bank also closely monitors loans to borrowers experiencing financial difficulty when, based on current information and events, it is probable that the Bank will be unable to collect all interest and principal payments due according to the originally contracted terms of the loan agreement.

Modifications to borrowers experiencing financial difficulty may include interest rate reductions, principal or interest forgiveness, forbearances, term extensions, and other actions intended to minimize economic loss and to avoid foreclosure or repossession of collateral.

Allowance for Credit Losses:

Allowance for Credit Losses – Loans

The ACL for loans is established through provisions for credit losses charged against income. Loans deemed to be uncollectible are charged against the ACL, and subsequent recoveries, if any, are credited to the ACL.

The ACL for loans is an estimate of the losses expected to be realized over the life of the loan portfolio. The ACL is determined for two distinct categories of loans: 1) loans evaluated individually for expected credit losses (specific reserve), and 2) loans evaluated collectively for expected credit losses (pooled reserve). Management's periodic evaluation of the adequacy of the ACL for loans is based on the Bank's past loan loss experience, known and inherent risks in the portfolio, adverse situations that may affect the borrower's ability to repay, the estimated value of any underlying collateral, composition of the loan portfolio, current economic conditions, diversification of the loan portfolio, delinquency statistics, results of internal loan reviews, borrowers' actual or perceived financial and managerial strengths, and other relevant factors. This evaluation is inherently subjective, as it requires material assumptions and estimates that may be susceptible to significant change, including the amounts and timing of future cash flows expected to be received on loans evaluated individually.

Loans evaluated individually for credit losses are primarily commercial purpose loans that do not share similar characteristics with those loans evaluated in the pool. These loans may exhibit performance characteristics where it is probable that the Bank will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. All commercial purpose loans greater than $250 thousand and rated Substandard (7), Doubtful (8) or on nonaccrual status may be considered for individual evaluation. Impairment is measured on a loan-by-loan basis by one of the following methods: the fair value of the collateral if the loan is collateral dependent, the present value of expected future cash flows discounted at the loan's effective interest rate or the loan's obtainable market price. Commercial purpose loans with a balance less than $250 thousand, and consumer purpose loans are not evaluated individually for a specific reserve but are included in the pooled reserve calculation. Loans that are evaluated for a specific reserve, but not needing a specific reserve are not included in the pooled reserve calculation.

The Corporation has elected to exclude accrued interest receivable from the measurement of the ACL. When a loan is placed on nonaccrual status, any outstanding accrued interest is reversed against income.

The pooled reserve represents the ACL for pools of homogenous loans, not evaluated individually. The pooled reserve is calculated using a quantitative and qualitative component for the loan pools.

The following inputs are used to calculate the quantitative component for the loan pool:

- Segregating loans into homogeneous pools by the FRB Call Code which is primarily a collateral-based and secondarily a purpose-based segmentation.
- The average remaining life of each pool is calculated using the weighted average remaining maturity method (WARM). The WARM method produces an estimated remaining balance by pool, by year, until maturity.
- Using third party data, the Bank determines a reasonable and supportable economic forecast that it believes is likely to exist for the next 4 four quarters.
- A historical credit loss rate is calculated for each pool, using the average historical loss, by FRB Call Code, for a peer group of Pennsylvania community banks over the last eight quarters. The historical loss rate is calculated over a historical period the Bank believes best represents a period that will be similar to the next 4 four quarters.
- The historical peer credit loss rate is applied to each WARM bucket though the initial 4 four quarter forecast period.
- At the end of the forecast period, the credit loss rate applied to each WARM bucket reverts to the peer group historical loss rate for the respective pool.
- Collectively these estimated losses represent the quantitative component of the pooled reserve.

The qualitative component for the pool utilizes a risk matrix comprised of eight risk factors and assigns a risk level to each factor. The risk factors give consideration to changes in: lending policy, procedures and practice; economic conditions; nature and volume of loans; experience of lending team; volume of past due loans; quality of the loan review system; concentrations of credit; and other external factors. The risk factors are weighted to reflect Management's estimate of how the factor affects potential losses. The risk levels within each factor are measured in basis points and range from minimal risk (0 basis points) to very high risk (20 basis points); and collectively range from 0 to 160 basis points. The qualitative risk level is are determined independently for commercial loans, residential mortgage loans and consumer loans.

The ACL for pooled loans is the sum of the quantitative and qualitative loss estimates.

Allowance for Credit Losses – Unfunded Commitments

The ACL for unfunded commitments is recorded in other liabilities on the consolidated balance sheet. The ACL represents management's estimate of expected losses from unfunded commitments and is determined by estimating future usage of the commitments, based on historical usage. The estimated loss is calculated in a manner similar to that used for the ACL for loans, previously described. The ACL is increased or decreased through the provision for credit losses.

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The following table shows the allocation of the allowance for credit losses and other loan performance ratios, by class, as of June 30, 2023 September 30, 2023 and December 31, 2022:

(Dollars in thousands)	Residential Real Estate 1-4 Family							
2023	**First Liens**	**Junior Liens & Lines of Credit**	**Construction**	**Commercial Real Estate**	**Commercial**	**Consumer**	**Unallocated**	**Total**
Loans at June 30, 2023	$ 169,764	$ 72,351	$ 18,033	$ 638,132	$ 240,555	$ 6,327	$ —	$ 1,145,162
Average Loans through June 30, 2023	157,841	72,926	21,456	586,218	238,820	6,165	—	1,083,426
Nonaccrual Loans at June 30, 2023	102	—	—	—	—	—	—	102
Allowance for Credit Loss at June 30, 2023	1,720	683	177	9,083	2,854	98	—	14,615
YTD Net (Charge-offs)/Recoveries at June 30, 2023	2	—	42	—	(8)	(51)	—	(15)
Loans/Total Gross Loans at June 30, 2023	15%	6%	2%	56%	21%	1%	—	100%
Nonaccrual Loans/Total Gross Loans at June 30, 2023	0.06%	0.00%	0.00%	0.00%	0.00%	0.00%	—	0.01%
Allowance for Credit Loss/Gross Loans at June 30, 2023	1.01%	0.94%	0.98%	1.42%	1.19%	1.55%	—	1.28%
Net (Charge-offs) Recoveries/Average Loans at June 30, 2023*	0.01%	0.00%	0.78%	0.00%	-0.01%	-3.31%	—	0.00%
Allowance for Credit Loss/Nonaccrual Loans at June 30, 2023								14328.43%

(Dollars in thousands)	Residential Real Estate 1-4 Family			
		Junior Liens &		**Commercial**

2023	First Liens	Lines of Credit	Construction	Real Estate	Commercial	Consumer	Unallocated	Total
Loans at September 30, 2023	$ 187,231	$ 71,826	$ 21,084	$ 671,182	$ 249,119	$ 6,408	$ —	$ 1,206,850
Average Loans through September 30, 2023	165,206	72,769	20,648	607,870	240,742	6,240	—	1,113,475
Nonaccrual Loans at September 30, 2023	98	—	—	—	115	—	—	213
Allowance for Credit Loss at September 30, 2023	1,201	418	242	10,207	3,370	90	—	15,528
YTD Net (Charge-offs)/Recoveries at September 30, 2023	2	—	46	—	5	(21)	—	32
Loans/Total Gross Loans at September 30, 2023	16%	6%	2%	56%	21%	1%	—	100%
Nonaccrual Loans/Total Gross Loans at September 30, 2023	0.05%	0.00%	0.00%	0.00%	0.05%	0.00%	—	0.02%
Allowance for Credit Loss/Gross Loans at September 30, 2023	0.64%	0.58%	1.15%	1.52%	1.35%	1.40%	—	1.29%
Net (Charge-offs) Recoveries/Average Loans at September 30, 2023*	0.00%	0.00%	0.22%	0.00%	0.00%	-0.34%	—	0.00%
Allowance for Credit Loss/Nonaccrual Loans at September 30, 2023								7290.14%

2022								
Loans at December 31, 2022	$ 144,497	$ 73,688	$ 24,393	$ 566,662	$ 235,602	$ 6,199	$ —	$ 1,051,041
Average Loans for 2022	139,577	73,200	21,737	550,772	241,395	5,938	—	1,032,619
Nonaccrual Loans at December 31, 2022	120	—	—	—	—	—	—	120
Allowance for Loan Losses at December 31, 2022	459	234	343	7,493	4,846	133	667	14,175
Net Recoveries/(Charge-offs) for 2022	28	2	—	(1,450)	(45)	(76)	—	(1,541)
Loans/Total Gross Loans at December 31, 2022	14%	7%	2%	54%	22%	1%	—	100%
Nonaccrual Loans/Total Gross Loans at December 31, 2022	0.08%	0.00%	0.00%	0.00%	0.00%	0.00%	—	0.01%
Allowance for Loan Loss/Gross Loans at December 31, 2022	0.32%	0.32%	1.41%	1.32%	2.06%	2.15%	—	1.35%
Net Recoveries(Charge-offs)/Average Loans for 2022	0.02%	0.00%	0.00%	-0.26%	-0.02%	-1.28%	—	-0.15%
Allowance for Loan Loss/Nonaccrual Loans at December 31, 2022								11812.50%

*Annualized

Deposits:

Total deposits decreased $38.3 million increased $16.0 million during the first six nine months of 2023 to $1.513 billion $1.567 billion. Interest-bearing checking decreased by $51.5 million $30.6 million primarily in state/municipal deposits and savings decreased by $11.3 million $18.6 million, while the Bank's Money Management increased $4.0 million $16.3 million. Time deposits increased $32.4 million $52.9 million as customers shifted to higher rate products. The Bank also added $8.6 million of brokered CDs, during the first half nine months of 2023.

As of June 30, 2023 September 30, 2023, the Bank had deposits of $215.6 million $233.5 million placed in the IntraFi Network deposit program ($127.8 142.1 million in interest-bearing checking and $87.8 million $91.4 million in money management) and $6.4 million $6.5 million in reciprocal time deposits in the CDARS program included in time deposits. These programs allow the Bank to offer full FDIC coverage to large depositors, but with the convenience to the customer of only having to deal with one bank. The Bank solicits these deposits from within its market and it believes they present no greater risk than any other local deposit. Only reciprocal deposits that exceed 20% of liabilities are considered brokered deposits. At June 30, 2023 September 30, 2023, the Bank's reciprocal deposits were 13.7% 14.0% of total liabilities compared to 12.7% at year-end 2022.

The Bank estimates that approximately 91% of its deposits are FDIC insured or collateralized as of June 30, 2023 September 30, 2023.

The following table presents a summary of deposits for the periods ended:

	June 30,	December 31,	Change	**September 30,**	December 31,	Change

(Dollars in thousands)	2023	2022	Amount	%	2023	2022	Amount	%
Noninterest-bearing checking	$ **287,385**	$ 299,231	$ (11,846)	(4.0)	$ **295,181**	$ 299,231	$ (4,050)	(1.4)
Interest-bearing checking	**445,003**	496,533	(51,530)	(10.4)	**465,897**	496,533	(30,636)	(6.2)
Money management	**573,582**	569,585	3,997	0.7	**585,872**	569,585	16,287	2.9
Savings	**117,423**	128,709	(11,286)	(8.8)	**110,158**	128,709	(18,551)	(14.4)
Total interest-bearing checking and savings	**1,136,008**	1,194,827	(58,819)	(4.9)	**1,161,927**	1,194,827	(32,900)	(2.8)
Time deposits	**89,742**	57,390	32,352	56.4	**110,306**	57,390	52,916	92.2
Total deposits	$ **1,513,135**	$ 1,551,448	$ (38,313)	(2.5)	$ **1,567,414**	$ 1,551,448	$ 15,966	1.0
Overdrawn deposit accounts reclassified as loans	$ **158**	$ 103			$ **120**	$ 103		

Borrowings:

At June 30, 2023 September 30, 2023, the Bank had $70.0 million borrowed from the Federal Reserve's Bank Term Funding Program (BTFP) to temporarily support its liquidity position. This position and $40.0 million in short-term borrowing from the Federal Home Loan Bank of Pittsburgh (FHLB). The BTFP borrowing is comprised of $50.0 million with a rate of 4.38% due March 22, 2024, and $20.0 million with a rate of 4.71% due May 10, 2024. At June 30, 2023 September 30, 2023, the fair value of debt securities pledged for the BTFP was $69.7 million $79.8 million. The FHLB borrowings have a blended rate of 5.80% and are due during the third quarter of 2024.

On August 4, 2020, the Corporation completed the sale of a subordinated debt note offering. The Corporation sold $15.0 million of subordinated debt notes with a maturity date of September 1, 2030. These notes are noncallable for 5 years and carry a fixed interest rate of 5.00% per year for 5 years and then convert to floating rate of SOFR plus 4.93% per year for the remainder of the term. The notes can be redeemed at par beginning 5 years prior to maturity. The Corporation also sold $5.0 million of subordinated debt notes with a maturity date of September 1, 2035. These notes are noncallable for 10 years and carry a fixed interest rate of 5.25% per year for 10 years and then convert to floating rate of SOFR plus 4.92% per year for the remainder of the term. The notes can be redeemed at par beginning 5 years prior to maturity. The notes are structured to qualify as Tier 2 capital for the Corporation and any funds it invests in the Bank qualify as Tier 1 capital at the Bank. The Corporation paid an issuance fee of 2% of the total issue that will be amortized to maturity date of each issue on a pro-rata basis. The proceeds are intended to be used for general corporate purposes.

Shareholders' Equity:

Total shareholders' equity increased $5.6 million $572 thousand to $119.86 million $114.8 million as of June 30, 2023 September 30, 2023 from December 31, 2022. Retained earnings increased $3.6 million $6.0 million in 2023 and accumulated other comprehensive income (AOCI) increased $3.3 million decreased $4.5 million as the fair value of the investment portfolio increased decreased during 2023. The increase in retained earnings was from net earnings of $6.3 million $10.1 million partially offset by cash dividends of $2.8 million $4.2 million. The Corporation's Dividend Reinvestment Plan (DRIP) added $295 $306 thousand in new capital from optional cash contributions and $516 $781 thousand from the reinvestment of quarterly dividends. The Corporation's dividend payout ratio was 44.77% 41.45% for the first six nine months of 2023 compared to 43.22% 37.91% for the first six nine months of 2022.

As part of its quarterly dividend decision, the Corporation considers current and future income projections, dividend yield, payout ratio, and current and future capital ratios. For the second third quarter of 2023, the Corporation paid a $0.32 per share dividend, compared to $0.32 paid in the first second quarter of 2023. On July 13, 2023 October 19, 2023, the Board of Directors declared a $0.32 per share regular quarterly dividend for the third fourth quarter of 2023, which will be paid on August 23, 2023 November 22, 2023.

On December 15, 2022, the Board of Directors authorized the 2022 Repurchase Plan for the repurchase of up to 150,000 shares of the Corporation's $1.00 par value common stock at market prices in open market or privately negotiated transactions beginning December 22, 2022 and expiring on December 21, 2023. The Corporation repurchased 74,306 shares during the second quarter of 2023. A total of 85,906 shares have been repurchased under the current plan. The Corporation is monitoring the market and intends to repurchase shares when and if the opportunity arises in accordance with applicable law, regulations and plan authorizations.

Capital adequacy for the Bank is currently defined by regulatory agencies through the use of several minimum required ratios. The capital ratios to be considered "well capitalized" are: (1) Common Equity Tier 1 (CET1) of 6.5%, (2) Tier 1 Leverage of 5%, (3) Tier 1 Risk-Based Capital of 8%, and (4) Total Risk-Based Capital of 10%. In addition, a capital conservation buffer of 2.5% is applicable to all of the capital ratios except for the Tier 1 Leverage ratio. The capital conservation buffer is equal to the lowest value of the three applicable capital ratios less the regulatory minimum for each respective capital measurement. The Bank's capital conservation buffer at June 30, 2023 September 30, 2023 was 7.50% 6.28% compared to the regulatory buffer of 2.5%. Compliance with the capital conservation buffer is required in order to avoid limitations to

certain capital distributions and is in addition to the minimum required capital requirements. As of June 30, 2023 September 30, 2023, the Bank was "well capitalized."

In 2019, the Community Bank Leverage Ratio (CBLR) was approved by federal banking agencies as an optional capital measure available to Qualifying Community Banking Organizations (QCBO). If a bank qualifies as a QCBO and maintains a CBLR of 9% or greater, the bank would be considered "well-capitalized" for regulatory capital purposes and exempt from complying with the risk-based capital rule described above. The CBLR rule took effect January 1, 2020 and banks could opt-in through an election in the first quarter 2020 regulatory filing. The Bank met the criteria of a QCBO but did not opt-in to the CBLR.

The consolidated asset limit on small bank holding companies is $3.0 billion and a company with assets under that limit is not subject to the consolidated capital rules but may file reports that include capital amounts and ratios. The Corporation has elected to file those reports.

The following table summarizes the regulatory capital requirements and results as of June 30, 2023 September 30, 2023 and December 31, 2022 for the Corporation and the Bank:

			Regulatory Ratios				Regulatory Ratios	
(Dollars in thousands)	**June 30, 2023**	December 31, 2022	**Adequately Capitalized Minimum**	**Well Capitalized Minimum**	**September 30, 2023**	December 31, 2022	**Adequately Capitalized Minimum**	**Well Capitalized Minimum**
Common Equity Tier 1 Risk-based Capital Ratio (1)								
Franklin Financial Services Corporation	**13.88%**	14.22%	N/A	N/A	**12.43%**	14.22%	N/A	N/A
Farmers & Merchants Trust Company	**14.25%**	14.63%	4.50%	6.50%	**13.03%**	14.63%	4.50%	6.50%
Tier 1 Risk-based Capital Ratio (2)								
Franklin Financial Services Corporation	**13.88%**	14.22%	N/A	N/A	**12.43%**	14.22%	N/A	N/A
Farmers & Merchants Trust Company	**14.25%**	14.63%	6.00%	8.00%	**13.03%**	14.63%	6.00%	8.00%
Total Risk-based Capital Ratio (3)								
Franklin Financial Services Corporation	**16.84%**	17.21%	N/A	N/A	**15.16%**	17.21%	N/A	N/A
Farmers & Merchants Trust Company	**15.50%**	15.88%	8.00%	10.00%	**14.28%**	15.88%	8.00%	10.00%
Tier 1 Leverage Ratio (4)								
Franklin Financial Services Corporation	**9.39%**	8.95%	N/A	N/A	**9.10%**	8.95%	N/A	N/A
Farmers & Merchants Trust Company	**9.64%**	9.21%	4.00%	5.00%	**9.53%**	9.21%	4.00%	5.00%

(1) Common equity Tier 1 capital / total risk-weighted assets

(2) Tier 1 capital / total risk-weighted assets

(3) Total risk-based capital / total risk-weighted assets

(4) Tier 1 capital / average quarterly assets

Economy

The Corporation's primary market area includes Franklin, Fulton, Cumberland, Huntingdon, and Dauphin Counties, Pennsylvania and Washington County, Maryland. This area is diverse in demographic and economic makeup. County populations range from a low of approximately 15,000 in Fulton County to over 260,000 280,000 in Cumberland Dauphin County. Unemployment in the Bank's market area ranged from 2.0% 1.9% in Washington County, MD to 3.8% 4.3% in Huntingdon County, as of the end of April July 2023. The market area has a diverse economic base and local industries include warehousing, truck & rail shipping centers, light and heavy manufacturers, healthcare, higher education institutions, farming and agriculture, and a varied service sector. The Corporation's primary market area provides easy access to the major metropolitan markets on the east coast via trucking and rail transportation. Because of this, warehousing and distribution companies continue to find the area attractive. The local economy is not overly dependent on any one industry or business and Management believes that the Bank's primary market area continues to be well suited for growth.

Impact of Inflation

The impact of inflation upon financial institutions such as the Corporation differs from its effect upon other commercial

enterprises. Unlike many companies, the assets and liabilities of the Corporation are financial in nature. As such, interest

rates and changes in interest rates may have a more significant effect on the Corporation's financial results than on other types of industries. Because of this, the Corporation watches the actions of the Federal Reserve Open Market Committee (FOMC) as it makes decisions about interest rate changes and how such changes affect market rates and the Corporation. Although inflation (and inflation expectations) may affect the interest rate environment, it is not possible to measure with any precision the effect of inflation on the Corporation.

Liquidity

The Corporation must meet the financial needs of the customers that it serves, while providing a satisfactory return on the shareholders' investment. In order to accomplish this, the Corporation must maintain sufficient liquidity in order to respond quickly to the changing level of funds required for both loan and deposit activity. The goal of liquidity management is to meet the ongoing cash flow requirements of depositors who want to withdraw funds and of borrowers who request loan disbursements. The Bank regularly reviews its liquidity position by measuring its projected net cash flows (in and out) at a 30 and 90-day interval. The Bank stresses the measurements by assuming a level of deposit out-flows that have not historically been realized. In addition to this forecast, other funding sources are reviewed as a method to provide emergency funding if necessary. The objective of this measurement is to identify the amount of cash that could be raised quickly without the need to liquidate assets. The Bank also stresses its liquidity position utilizing different longer-term scenarios. The varying degrees of stress create pressure on deposit flows in its local market, reduce access to wholesale funding and limit access of funds available through brokered deposit channels. In addition to stressing cash flow, specific liquidity risk indicators are monitored to help identify risk areas. This analysis helps identify and quantify the potential cash surplus/deficit over a variety of time horizons to ensure the Bank has adequate funding resources. Assumptions used for liquidity stress testing are subjective. Should an evolving liquidity situation or business cycle present new data, potential assumption changes will be considered. The Bank believes it can meet all anticipated liquidity demands.

Historically, the Corporation has satisfied its liquidity needs from earnings, repayment of loans and amortizing investment securities, maturing investment securities, loan` loan sales, deposit growth and its ability to access existing lines of credit. All investment securities are classified as available for sale; therefore, securities that are unencumbered ($216.5 179.5 million fair value) as collateral for borrowings are an additional source of readily available liquidity, either by selling the security or, more preferably, to provide collateral for additional borrowing. The Bank also has access to other wholesale funding via the brokered CD market.

The FHLB system has always been a major funding source for the Bank. There are no current indicators that lead the Bank to believe the FHLB would discontinue its lending function or restrict the Bank's ability to borrow. If either of these events would occur, it would have a negative effect on the Bank, and it is unlikely that the Bank could replace the level of FHLB funding in a short time. The Bank has established credit at the Federal Reserve Discount Window and at correspondent banks. At June 30, 2023 the Bank had an outstanding balance of $70.0 million from the Federal Reserve's Bank Term Funding Program to temporarily support its liquidity position.

The following table shows the Bank's available liquidity at June 30, 2023 September 30, 2023.

(Dollars in thousands)

Liquidity Source	Capacity	Outstanding	Available	Capacity	Outstanding	Available
Federal Home Loan Bank	$ 420,487	$ —	$ 420,487	$451,460	$ 40,000	$411,460
Federal Reserve Bank Discount Window	56,941	—	56,941	55,126	—	55,126
Fed Bank Term Funding Program	74,121	70,000	4,121	86,765	70,000	16,765
Correspondent Banks	56,000	—	56,000	56,000	—	56,000
Total	$ 607,549	$ 70,000	$ 537,549	$649,351	$ 110,000	$539,351

Off Balance Sheet Commitments

The Corporation’s financial statements do not reflect various commitments that are made in the normal course of business, which may involve some liquidity risk. These commitments consist mainly of unfunded loans and letters of credit made under the same standards as on-balance sheet instruments. Because these instruments have fixed maturity dates, and because many of them will expire without being drawn upon, they do not generally present any significant liquidity risk to the Corporation. At June 30, 2023 September 30, 2023, the ACL-unfunded commitments was $2.0 million compared to $1.5 million at December 31, 2022. The ACL-unfunded commitments is reported in Other Liabilities on the Consolidated Balance Sheet.

(Dollars in thousands)	**June 30, 2023**	December 31, 2022	**September 30, 2023**	December 31, 2022
Financial instruments whose contract amounts represent credit risk				
Commercial commitments to extend credit	**$ 356,488**	$ 275,867	**$ 318,116**	$ 275,867
Consumer commitments to extend credit (secured)	**95,459**	93,124	**101,059**	93,124
Consumer commitments to extend credit (unsecured)	**4,907**	5,247	**4,970**	5,247
	$ 456,854	$ 374,238	**$ 424,145**	$ 374,238
Standby letters of credit	**$ 28,264**	$ 30,734	**$ 28,341**	$ 30,734
ACL - Unfunded Commitments*	**$ 1,957**	$ 1,475	**$ 1,965**	$ 1,475

*Reported in Other Liabilities on the Consolidated Balance Sheet

The Corporation has entered into various contractual obligations to make future payments. These obligations include time deposits, long-term debt, operating leases, deferred compensation and pension payments. These amounts have not changed materially, except as reported, from those reported in the Corporation’s 2022 Annual Report on Form 10-K.

Management believes that any amounts actually drawn upon can be funded in the normal course of operations. The Corporation has no investment in or financial relationship with any unconsolidated entities that are reasonably likely to have a material effect on liquidity.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

There were no material changes in the Corporation’s exposure to market risk during the six nine months ended June 30, 2023 September 30, 2023. For more information on market risk refer to the Corporation’s 2022 Annual Report on Form 10-K.

Item 4. Controls and Procedures

Evaluation of Controls and Procedures

The Corporation carried out an evaluation, under the supervision and with the participation of the Corporation’s management, including the Corporation’s Chief Executive Officer and Chief Financial Officer, of the effectiveness of its disclosure controls and procedures, as defined in Exchange Act Rules 13a-15(e) and 15d-15(e). Based upon the evaluation, the Corporation’s Chief Executive Officer and Chief Financial Officer concluded that as of June 30, 2023 September 30, 2023, the Corporation’s disclosure controls and procedures are effective. Disclosure controls and procedures are controls and procedures that are designed to ensure that information required to be disclosed in the Corporation’s reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission’s rules and forms. There were no changes in the Corporation’s internal control over financial reporting during the quarterly period ended June 30, 2023 September 30, 2023, that have materially affected, or are reasonably likely to materially affect, the internal control over financial reporting.

The management of the Corporation is responsible for establishing and maintaining adequate internal control over financial reporting. The Corporation’s internal control system is designed 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.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Part II – OTHER INFORMATION

Item 1. Legal Proceedings

The nature of the Corporation's business generates a certain amount of litigation in the ordinary course of business.

In management's opinion, there are no other legal proceedings pending to which the Corporation is a party or to which its property is subject which, if determined adversely to the Corporation, would be material to the Corporation's financial condition or results of operations. No material proceedings are pending or are known to be threatened or contemplated against us by any governmental authorities.

Item 1A. Risk Factors

There were no material changes in the Corporation's risk factors during the three months ended June 30, 2023 September 30, 2023 except as described below. For more information, refer to the Corporation's 2022 Annual Report on Form 10-K.

Recent Negative Developments Affecting the Banking Industry, Including Recent Bank Failures or Concerns Regarding Liquidity, Have Eroded Customer Confidence in the Banking System and May Have a Material Adverse Effect on the Corporation.

During March and April 2023, three significant bank failures occurred (Silicon Valley Bank, Signature Bank, and First Republic Bank). This was and continues to be accompanied by financial instability at various additional banks. These bank failures and bank instabilities have created and may continue to create market and other risks, for all financial institutions and banks, including the Corporation. These risks include, but are not limited to:

1. Market risk and loss of confidence in the financial services sector, and/or specific banks;
2. Deterioration of securities and loan portfolios;
3. Deposit volatility and reductions with higher volumes and occurring over shorter periods of time;
4. Increased liquidity demand and utilization of sources of liquidity; and
5. Interest rate volatility and abrupt, sudden and greater than usual rate changes.

These factors individually, or in any combination, could materially and adversely affect:

1. Financial condition;
2. Operations and results thereof; and
3. Stock price.

In addition, the previously mentioned bank failures and instabilities may result in an increase of FDIC deposit insurance premiums and/or result in special FDIC deposit insurance assessments, which also may adversely affect the Corporation's financial condition, operations, results thereof or stock price.

The Corporation cannot predict the impact, timing or duration of such events.

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

On December 15, 2022, the Board of Directors authorized the 2022 Repurchase Plan for the repurchase of up to 150,000 shares of the Corporation's $1.00 par value common stock at market prices in open market or privately negotiated transactions beginning December 22, 2022 and expiring on December 21, 2023. The following table presents the activity under this plan No shares were repurchased during the second third quarter of 2023.

Period	Number of Shares Purchased as Part of Publicly Announced Program	Weighted Average Price Paid per Share	Dollar Amount of Shares Purchased as Part of Publicly Announced Program	Maximum Number of Shares Yet To Be Purchased Under Program
April 2023	21,367	$ 29.75	$ 635,626	117,033
May 2023	17,348	$ 26.15	453,642	99,685

June 2023	35,591	$	28.30	988,534	64,094
	74,306			$ 2,077,802	

Item 3. Defaults by the Company on its Senior Securities

None

Item 4. Mine Safety Disclosures

Not Applicable

Item 5. Other Information

None

Item 6. Exhibits

Exhibits

3.1	Amended and Restated Articles of Incorporation of the Corporation (Filed as Exhibit 3.1 to Quarterly Report on Form 10-Q for the quarter ended June 30, 2020 September 30, 2020 and incorporated herein by reference).
3.2	Bylaws of the Corporation. (Filed on Form 8-K, as Exhibit 99 with the commission on September 2, 2022 and incorporated herein by reference).
31.1	Rule 13a – 14(a)/15d-14(a) Certifications – Principal Executive Officer
31.2	Rule 13a – 14(a)/15d-14(a) Certifications – Principal Financial Officer
32.1	Section 1350 Certifications – Principal Executive Officer
32.2	Section 1350 Certifications – Principal Financial Officer
101	Interactive Data File (XBRL)
104	Cover Page Interactive Data File (the cover page XBRL tags are imbedded in the XBRL document)

FRANKLIN FINANCIAL SERVICES CORPORATION

and SUBSIDIARIES

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.

Franklin Financial Services Corporation

August 10, November 14, 2023	/s/ Timothy G. Henry
	Timothy G. Henry

	Chief Executive Officer and President (Principal Executive Officer**)**
August 10, November 14, 2023	/s/ Mark R. Hollar
	Mark R. Hollar Treasurer and Chief Financial Officer (Principal Financial and Accounting Officer)

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Exhibit 31.1Rule 13a-14(a)/15d-14(a) CertificationsI, Timothy G. Henry, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Franklin Financial Services 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 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:

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: August 10, 2023 November 14, 2023/s/ Timothy G. HenryTimothy G. HenryPresident and Chief Executive Officer

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Exhibit 31.2Rule 13a-14(a)/15d-14(a) CertificationsI, Mark R. Hollar, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Franklin Financial Services 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 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:

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: August 10, 2023 November 14, 2023/s/ Mark R. HollarMark R. HollarTreasurer and Chief Financial Officer

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Exhibit 32.1Certification Pursuant to 18 U.S.C. Section 1350,As Adopted Pursuant to Section 906 of the Sarbanes–Oxley Act of 2002In connection with the Quarterly Report of Franklin Financial Services Corporation (the "Corporation") on Form 10-Q, for the period ending June 30, 2023 September 30, 2023, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Timothy G. Henry, Chief Executive Officer of the Corporation, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes–Oxley Act of 2002 that:

(1) The report fully complies with the requirements of Section 13(a) or 15(d) of the Securities and Exchange Act of 1934; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Company.

/s/ Timothy G. Henry

Timothy G. Henry

President and Chief Executive Officer

August 10, November 14, 2023

Exhibit 32.2Certification Pursuant to 18 U.S.C. Sections 1350,As Adopted Pursuant to Section 906 of the Sarbanes–Oxley Act of 2002In connection with the Quarterly Report of Franklin Financial Services Corporation (the "Corporation") on Form 10-Q for the period ending June 30, 2023 September 30, 2023 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Mark R. Hollar, Chief Financial Officer of the Corporation, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes–Oxley Act of 2002 that:

(1) The report fully complies with the requirements of Section 13(a) or 15(d) of the Securities and Exchange Act of 1934; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Company.

/s/ Mark R. Hollar

Mark R. Hollar

Chief Financial Officer

August 10, November 14, 2023

DISCLAIMER