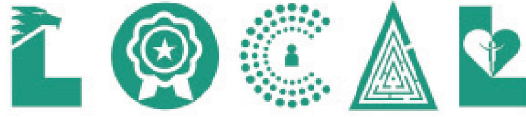
Annual Report

Growing a LOCAL Legacy



Bank of Clarke started off 2023 with a bang in the form of a rebrand, introducing a new logo and removing "County" from our name. While we are committed to our traditional footprint, to remain the independent community bank you know and trust, we also needed a brand that reflects the vibrant and growing organization that we are.

Over the summer, Bank of Clarke became certified as A Great Place to Work®, which recognizes companies who create an outstanding employee experience. This rounds out the many "best of" nods we got from the major publications in our footprint.

As a further show of our ongoing community support, we partnered with the Virginia Bankers Association to host our summer internship program. This opportunity reached out to local college students to help provide and show them possible career choices that we offer as a financial institution.

In addition, the Bank of Clarke Foundation donated over $260K to local organizations in 2023, including the Shenandoah Valley Discovery Museum, the Clarke County Education Foundation, the Loudoun Symphony and over 180 more. And, through our "Give with BoC" campaign, we raised over $42K for local organizations.

We thank our loyal customers for all their support and our staff that continuously serve our community. We look forward to serving you as your trusted financial partner along with the challenges and successes 2024 will be sure to bring.

Dear Eagle Financial Services, Inc. Shareholders:

Despite ongoing challenges in the banking sector, in 2023, Bank of Clarke delivered many successes for Eagle Financial Services, Inc. For the year, our commercial and residential lending team delivered net loan growth of $138.8 million, an 11% increase over 2022, coupled with record mortgage and Small Business Administration (SBA) loan income. In addition, our Trust and Wealth Management division crossed the $500 million threshold in Assets Under Management (AUM) in 2023 and contributed over $1.8 million in after-tax revenue to the company. We strategically sold off our marine financing division, LV Finance. However, even though the Bank posted a record 52% increase in interest and dividend income, overall net income decreased, primarily because of the significantly increased interest expense the entire industry faced.

The year started off with a new brand and a new name, Bank of Clarke. To ensure inclusivity of all communities in our current footprint -- from our original service area in Clarke and Frederick Counties to Loudoun and Fauquier Counties and our loan production offices in Tyson's Corner and Frederick, MD -- the decision was made to eliminate the word "County." We also took this opportunity to change our logo and other branding to reflect the dynamic financial institution we are.

As in previous years, the Bank was awarded many accolades. We were named Best Bank from LoudounNow and Best Bank/Credit Union from the Winchester Star. We also received numerous first-time acknowledgements: The Fauquier Times Reader's Choice Award for Best Bank (after only 18 months in that market), Top VA Employers for Interns from the Virginia Banking Association, and aTop 200 Community Bank from American Banker. Importantly, we earned the prestigious Great Place to Work® certification.

Community banks are only as strong as the communities they serve and, as such, we have a long-standing tradition of giving back to the region's numerous worthy non-profits. In 2023, through the Bank's branch-based #GiveWithBoC initiative and the Bank of Clarke Foundation, we donated over $307,000 to charities throughout our footprint, a 22% increase over 2022. This does not include the many personal hours that were donated by our employees to support local organizations.

We continue to remain focused on our customers, community, and shareholders by combining the customer service of Main Street and the product set of Wall Street. Thanks to our remarkable staff for their tireless work in putting our customers at the center of everything we do, as we work to earn the moniker of being the trusted financial partners for all we serve in the Shenandoah Valley and Northern Virginia. The Company remains well-capitalized and diversified, with strong credit quality and a conservative lending foundation, and is well-poised to face the challenges that 2024 will continue to bring.

Results

The Bank saw success across multiple categories in 2023 despite a difficult economic environment. As of December 31, 2023, the Company had total assets of $1.83 billion, net loans of $1.45 billion, total deposits of $1.51 billion, and shareholders' equity of $108.4 million.

The Company's annual dividend was $1.20, an increase from $1.15 per share in 2022. This is the 40th year that the Bank has offered a dividend with continued increases every year.

Business Segments

Commercial and Retail

As in 2020 through 2022, our commercial lending group realized the highest growth rates in the history of the organization – a key factor in the institution's strong loan and deposit performance. Commercial and industrial loans were $107.8 million or 7.4% and $99.6

million or 7.6% of total loans as of December 31, 2023 and December 31, 2022, respectively. This represents an increase of $8.2 million or 8.2% for 2023. The Bank activity pursued deposits through marketing and sales efforts, adding $197 million in average balances. Continued improvements in technology allowed the Bank to grow the online channel, with a 5% increase in mobile banking users and a 289% increase in person-to-person payment users, with the mid-2023 launch of Zelle®. In addition, great strides were made in streamlining the personal loan, mortgage, and home equity account opening processes.

Trust and Investments

Bank of Clarke Wealth Management, the Bank's Trust and Financial Advisory division, experienced continued growth in 2023, with total assets under management climbing from $489 million at year end 2022 to $515 million in December 2023. Wealth Management contributed over $1.8 million in after-tax revenue, approximately four times its historical contribution. Fee income increased 18.7% versus 2022. We continued to refine procedures in this area and add appropriate staff, who can provide an expanded product set, including Private Banking and insurance.

Non-Interest Income

In addition to strong loan growth, the combination of efforts to expand fee income opportunities and to leverage existing technologies has led to significant year-over-year increases in non-interest income. Just as 2022 saw record levels with total non-interest income at $13.3 million, this trend continued in 2023, with non-interest income of $14.7 million.

The Year Ahead

What lies ahead in 2024? The Bank has the unique position of being in high-growth geographies. That, coupled with the past high performance, allows the bank to grow by market expansion and adding new services and technologies. To achieve our goals, we continue to focus on:

- **High Performance and Growth.** We will create value for our shareholders, customers, and employees while remaining a well-capitalized bank.
- **Employer of Choice.** We will be the employer of choice in the communities we serve.
- **Digital Capabilities.** We will provide a premier digital experience across all products and services, while never treating our customer as a "number."
- **Commercial and Small Business Bank of Choice.** We will be a market leader for commercial and small businesses in our footprint.

I would like to thank our shareholders for their confidence in the Company, its Board of Directors, the management team, and our employees. Your continued support of this organization ensures we are able to serve our communities, customers, and employees while providing shareholders with even stronger returns on their investments.

Brandon Lorey
President & CEO

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-K

(Mark One)

☒ **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended December 31, 2023

or

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

Commission File Number: 0-20146

EAGLE FINANCIAL SERVICES, INC.

(Exact name of registrant as specified in its charter)

Virginia	**54-1601306**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
2 East Main Street P.O. Box 391 Berryville, Virginia	**22611**
(Address of principal executive offices)	**(Zip Code)**

(540) 955-2510

(Registrant's telephone number, including area code)

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

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
None		

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

Common Stock, Par Value $2.50

(Title of class)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ☐ No ☒

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes ☐ No ☒

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

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

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

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

Indicate by check mark whether the registrant has filed a report on and attestation to its management's assessment of the effectiveness of its internal control over financial reporting under Section 404(b) of the Sarbanes-Oxley Act (15 U.S.C. 7262(b)) by the registered public accounting firm that prepared or issued its audit report. ☐

If securities are registered pursuant to Section 12(b) of the Act, indicate by check mark whether the financial statements of the registrant included in the filing reflect the correction of an error to previously issued financial statements. ☐

Indicate by check mark whether any of those error corrections are restatements that required a recovery analysis of incentive-based compensation received by any of the registrant's executive officers during the relevant recovery period pursuant to §240.10D-1(b). ☐

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

The aggregate market value of the voting common equity held by non-affiliates of the registrant at June 30, 2023 was $94,161,812.

The number of shares of the registrant's Common Stock ($2.50 par value) outstanding as of March 22, 2024 was 3,557,229.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's Proxy Statement for the 2024 Annual Meeting of Shareholders are incorporated by reference into Part III.

EAGLE FINANCIAL SERVICES, INC.
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PART I

Item 1. Business

General

Eagle Financial Services, Inc. is a bank holding company that was incorporated in 1991. The company is headquartered in Berryville, Virginia and conducts its operations through its subsidiary, Bank of Clarke (the "Bank"). The Bank changed its name from Bank of Clarke County to Bank of Clarke in 2022. The Bank is chartered under Virginia law. For purposes of this annual report on Form 10-K, the terms the "Company," "our," "us" and "we" refer to Eagle Financial Services, Inc. and our subsidiaries as a combined entity, unless this report otherwise indicates or the context otherwise requires.

The Bank has thirteen full-service branches, two loan production offices, and one drive-through only facility. The Bank's main office is located at 2 East Main Street in Berryville, Virginia. The Bank opened for business on April 1, 1881. The Bank has Virginia offices located in Clarke County, Frederick County, Fauquier County, Loudoun County and Fairfax County, as well as the Towns of Leesburg, Ashburn and Purcellville and the City of Winchester. The Bank has a Maryland office located in Frederick. This market area is located in the Shenandoah Valley of Virginia, Northern Virginia and Frederick, Maryland.

The Bank offers a wide range of retail and commercial banking services, including demand, savings and time deposits and consumer, mortgage and commercial loans. The Bank has thirteen ATM locations in its trade area and issues debit cards to deposit customers. These cards can be used to withdraw cash at most ATMs through the Bank's membership in both regional and national networks. These cards can also be used to make purchases at retailers who accept transactions through the same regional and national networks. The Bank offers telephone banking, internet banking, and mobile banking to its customers. Internet banking also offers online bill payment to consumer and commercial customers. The Bank offers other commercial deposit account services such as ACH origination and remote deposit capture.

The Bank of Clarke Wealth Management Division, a division of the Bank, provides both a full-service trust department and a separate brokerage area. The trust department features a full range of fiduciary expertise, including service as trustee of personal trusts, service as guardian or conservator by court appointment, fiduciary investment management, estate settlement, and agency for trustees. The brokerage area offers advisory services and a broad selection of investment products, including individual retirement accounts, mutual funds, tax-deferred annuities, 529 college savings plans, life insurance, long term care insurance, brokerage certificates of deposit, among other brokerage services. Securities and other property held by the Bank of Clarke Wealth Management Division in a fiduciary or agency capacity are not assets of the Bank and are not included in the accompanying consolidated financial statements. Non-deposit investment products are offered through a third party provider.

The Bank of Clarke is a member in Bankers Title Shenandoah, LLC, which sells title insurance and is an investor in Virginia Bankers Insurance Center, LLC, which serves as the broker for insurance sales through its member banks. Bank of Clarke is also an investor in low-income housing projects in Virginia and building rehabilitation projects in surrounding states. These investments generate tax credits for the Bank.

Employees

The Company, including the Bank, had 92 officers, 142 other full-time and 9 part-time employees (or 241 full-time equivalent employees) at December 31, 2023. None of the Company's employees are represented by a union or covered under a collective bargaining agreement. The Company considers relations with its employees to be excellent, receiving a *Great Place to Work® certified.* designation in the fourth quarter of 2023.

Securities and Exchange Commission Filings

The Company maintains an internet website at *www.bankofclarke.bank*. Shareholders of the Company and the public may access, free of charge, the Company's periodic and current reports (including annual reports on Form 10-K, quarterly reports on Form 10-Q and current reports on Form 8-K, and any amendments to those reports) filed with or furnished to the Securities and Exchange Commission (the "SEC"), through the "Investor Relations" section of the Company's website. The reports are made available on this website as soon as practicable following the filing of the reports with the SEC. In addition, certain committee charters and the Company's Code of Ethics are available on the Company's website. The information is free of charge and may be reviewed, downloaded and printed from the website at any time. The information on the Company's website is not a part of, and is not incorporated into, this Annual Report on Form 10-K.

Competition

There is significant competition for both loans and deposits within the Company's trade area. Competition for loans comes from other commercial banks, savings banks, credit unions, mortgage brokers, finance companies, financial technology firms, insurance companies, and other institutional lenders. Competition for deposits comes from other commercial banks, savings banks, credit unions, brokerage firms, and other financial institutions. Based on total deposits at June 30, 2023 as reported to the FDIC, the Bank has 9.27% of the total deposits in its market area. The Company's primary deposit market area includes Clarke County, Frederick County, Loudoun County, Fauquier County and the City of Winchester.

Supervision and Regulation

General. As a bank holding company, the Company is subject to regulation under the Bank Holding Company Act of 1956, as amended, and the examination and reporting requirements of the Board of Governors of the Federal Reserve System (the "Federal Reserve"). As a state-chartered commercial bank, the Bank is subject to regulation, supervision and examination by the Virginia State Corporation Commission's Bureau of Financial Institutions. It is also subject to regulation, supervision and examination by the Federal Reserve. Other federal and state laws, including various consumer and compliance laws, govern the activities of the Bank, the investments that it makes and the aggregate amount of loans that it may grant to one borrower.

The following sections summarize some of the significant federal and state laws applicable to the Company and its subsidiary. To the extent that statutory or regulatory provisions are described, the description is qualified in its entirety by reference to that particular statutory or regulatory provision.

The Bank Holding Company Act. Under the Bank Holding Company Act, the Company is subject to periodic examination by the Federal Reserve and is required to file periodic reports regarding its operations and any additional information that the Federal Reserve may require. Activities at the bank holding company level are limited to the following:

- banking, managing or controlling banks;
- furnishing services to or performing services for its subsidiaries; and
- engaging in other activities that the Federal Reserve has determined by regulation or order to be so closely related to banking as to be a proper incident to these activities.

Some of the activities that the Federal Reserve has determined by regulation to be closely related to the business of a banking include making or servicing loans and specific types of leases, performing specific data processing services and acting in some circumstances as a fiduciary or investment or financial adviser.

With some limited exceptions, the Bank Holding Company Act requires every bank holding company to obtain the prior approval of the Federal Reserve before:

- acquiring substantially all the assets of any bank;
- acquiring direct or indirect ownership or control of any voting shares of any bank if after such acquisition it would own or control more than 5% of the voting shares of such bank (unless it already owns or controls the majority of such shares); or
- merging or consolidating with another bank holding company.

In addition, and subject to some exceptions, the Bank Holding Company Act and the Change in Bank Control Act, together with their regulations, require Federal Reserve approval prior to any person or company acquiring 25% or more of any class of voting securities of the bank holding company. Prior notice to the Federal Reserve is required if a person acquires 10% or more, but less than 25%, of any class of voting securities of a bank or bank holding company and either the institution has registered securities under Section 12 of the Securities Exchange Act of 1934 or no other person owns a greater percentage of that class of voting securities immediately after the transaction.

In November 1999, Congress enacted the Gramm-Leach-Bliley Act ("GLBA"), which made substantial revisions to the statutory restrictions separating banking activities from other financial activities. Under the GLBA, bank holding companies that are well-capitalized and well-managed and meet other conditions can elect to become "financial holding companies." As financial holding companies, they and their subsidiaries are permitted to acquire or engage in previously impermissible activities such as insurance underwriting, securities underwriting and distribution, travel agency activities, insurance agency activities, merchant banking and other activities that the Federal Reserve determines to be financial in nature or complementary to these activities. Financial holding companies continue to be subject to the overall oversight and supervision of the Federal Reserve, but the GLBA applies the concept of functional regulation to the activities conducted by subsidiaries. For example, insurance activities would be subject to supervision and regulation by state insurance authorities. Although the Company has not elected to become a financial holding company in order to exercise the broader activity powers provided by the GLBA, the Company may elect do so in the future.

Payment of Dividends. The Company is organized under the Virginia Stock Corporation Act, which prohibits the payment of a dividend if, after giving it effect, the corporation would not be able to pay its debts as they become due in the usual course of business or if the corporation's total assets would be less than the sum of its total liabilities plus the amount that would be needed, if the corporation were to be dissolved, to satisfy the preferential rights upon dissolution of any preferred shareholders. In addition, the Federal Reserve has indicated that a bank holding company should generally pay dividends only if its current earnings are sufficient to fully fund the dividends, and the prospective rate of earnings retention appears consistent with the organization's capital needs, asset quality and overall financial condition.

The Company is a legal entity separate and distinct from its subsidiary. Its ability to distribute cash dividends will depend primarily on the ability of the Bank to pay dividends to it, and the Bank is subject to laws and regulations that limit the amount of dividends that it can pay. As a state member bank, the Bank is subject to certain restrictions imposed by the reserve and capital requirements of federal and Virginia banking statutes and regulations. Under Virginia law, a bank may not declare a dividend in excess of its undivided profits. Additionally, the Bank may not declare a dividend if the total amount of all dividends, including the proposed dividend, declared by it in any calendar year exceeds the total of its retained net income of that year to date, combined with its retained net income of the two preceding years, unless the dividend is approved by the Federal Reserve.

The Federal Reserve, the FDIC and the state of Virginia have the general authority to limit the dividends paid by insured banks if the payment is deemed an unsafe and unsound practice. These regulators have indicated that paying dividends that deplete a bank's capital base to an inadequate level would be an unsound and unsafe banking practice. The Bank may also not declare or pay a dividend without the approval of its board and two-thirds of its shareholders if the dividend would exceed its undivided profits, as reported to the Federal Reserve.

The Company does not expect that any of these laws, regulations or policies will materially affect the Bank's ability to pay dividends to the Company. During 2023, the Company paid total dividends of $4.2 million, including cash dividends that were reinvested in Company stock.

Insurance of Accounts, Assessments and Regulation by the FDIC. The Bank's deposits are insured up to applicable limits by the FDIC. In July 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") permanently raised the standard maximum deposit insurance amount to $250,000. The FDIC has implemented a risk-based assessment system in which assessment rates for insured institutions with under $10 billion in assets are calculated based on supervisory evaluations and certain other financial measures. The assessment base is an institution's average consolidated total assets less average tangible equity, and the initial base assessment rates are currently between 5 and 32 basis points depending on the institution's composite rating, and subject to potential adjustment based on certain long-term unsecured debt. Progressively lower assessment rate schedules will take effect once the FDIC's reserve ratio reaches 2.0% or greater, and again once the reserve ratio reaches 2.5% or greater.

Capital Requirements. The Federal Reserve and the other federal banking agencies have issued risk-based and leverage capital guidelines applicable to U.S. banking organizations. Those regulatory agencies may from time to time require that a banking organization maintain capital above the minimum levels because of its financial condition or actual or anticipated growth. Pursuant to the Federal Reserve's Small Bank Holding Company and Savings and Loan Holding Company Policy Statement, qualifying bank holding companies with total consolidated assets of less than $3 billion, such as the Company, are not subject to consolidated regulatory capital requirements.

Effective January 1, 2015, the Federal Reserve adopted capital rules intended to revise and strengthen its risk-based and leverage capital requirements and its method for calculating risk-weighted assets. The rules implemented the Basel III regulatory capital reforms from the Basel Committee on Banking Supervision and certain provisions of the Dodd-Frank Act.

Under these risk-based capital requirements of the Federal Reserve, the Bank is required to maintain a minimum ratio of total capital (which is defined as core capital and supplementary capital less certain specified deductions from total capital such as reciprocal holdings of depository institution capital instruments and equity investments) to risk-weighted assets of at least 8.0%. At least 6.0% of risk-weighted assets is required to be "Tier 1 capital," which consists principally of common and certain qualifying preferred shareholders' equity (including grandfathered trust preferred securities) as well as retained earnings, less certain intangibles and other adjustments. The "Tier 2 capital" consists of cumulative preferred stock, long-term perpetual preferred stock, a limited amount of subordinated and other qualifying debt (including certain hybrid capital instruments), and a limited amount of the allowance for loan losses, including reserves for off-balance sheet commitments. A common equity Tier 1 capital ratio of 4.5% of risk-weighted assets also was added with the rules effective January 1, 2015.

Each of the federal bank regulatory agencies also has established a minimum leverage capital ratio of Tier 1 capital to average adjusted assets ("Tier 1 leverage ratio"). The guidelines require a minimum Tier 1 leverage ratio of 3.0% for financial holding companies and banking organizations with the highest supervisory rating. All other banking organizations are required to maintain a minimum Tier 1 leverage ratio of 4.0% unless a different minimum was specified by an appropriate regulatory authority. In addition, for a depository institution to be considered "well capitalized" under the regulatory framework for prompt corrective action, its Tier 1 leverage ratio must be at least 5.0%. Banking organizations that have experienced internal growth or made acquisitions are expected to maintain strong capital positions substantially above the minimum supervisory levels without significant reliance on intangible assets. The Federal Reserve has not advised the Company or the Bank of any specific minimum leverage ratio applicable to either entity.

The capital requirements that became effective January 1, 2015 were phased in over a four-year period. As fully phased in effective January 1, 2019, the rules require the Bank to maintain (i) a minimum ratio of common equity Tier 1 to risk-weighted assets of at least 4.5%, plus a 2.5% "capital conservation buffer" (which is added to the 4.5% common equity Tier 1 ratio, effectively resulting in a minimum ratio of common equity Tier 1 to risk-weighted assets of at least 7.0%); (ii) a minimum ratio of Tier 1 capital to risk-weighted assets of at least 6.0%, plus the 2.5% capital conservation buffer (which is added to the 6.0% Tier 1 capital ratio, effectively resulting in a minimum Tier 1 capital ratio of 8.5%); (iii) a minimum ratio of total capital to risk-weighted assets of at least 8.0%, plus the 2.5% capital conservation buffer (which is added to the 8.0% total capital ratio, effectively resulting in a minimum total capital ratio of 10.5%); and (iv) a minimum leverage ratio of 4.0%, calculated as the ratio of Tier 1 capital to average assets.

The capital conservation buffer requirement was phased in beginning January 1, 2016, at 0.625% of risk-weighted assets, increasing by the same amount each year until fully implemented at 2.5% effective January 1, 2019. The capital conservation buffer is designed to absorb losses during periods of economic stress. Banking institutions with a ratio of common equity Tier 1 to risk-weighted assets above the minimum but below the conservation buffer will face constraints on dividends, equity repurchases, and compensation based on the amount of the shortfall.

The Federal Reserve's final rules also revised the "prompt corrective action" regulations pursuant to Section 38 of the FDIA by (i) introducing a common equity Tier 1 capital ratio requirement at each level (other than critically undercapitalized), with the required ratio being 6.5% for well-capitalized status; (ii) increasing the minimum Tier 1 capital ratio requirement for each category, with the minimum ratio for well-capitalized status being 8.0%; and (iii) eliminating the provision that provided that a bank with a composite supervisory rating of 1 may have a 3.0% Tier 1 leverage ratio and still be well-capitalized. These thresholds were effective for the Bank as of January 1, 2015. The minimum total capital to risk-weighted assets ratio (10.0%) and minimum leverage ratio (5.0%) for well-capitalized status were unchanged by the final rules.

As directed by the Economic Growth, Regulatory Relief and Consumer Protection Act (the "Economic Growth Act"), the federal banking regulators jointly issued a final rule in 2019 that permits qualifying banks that have less than $10 billion in total consolidated assets to elect to be subject to a 9% "community bank leverage ratio." A qualifying bank that has chosen the proposed framework is not required to calculate the existing risk-based and leverage capital requirements and would be considered to have met the capital ratio requirements to be "well capitalized" under prompt corrective action rules, provided it has a community bank leverage ratio greater than 9%.

Other Safety and Soundness Regulations. There are a number of obligations and restrictions imposed on bank holding companies and their depository institution subsidiaries by federal law and regulatory policy that are designed to reduce potential loss exposure to the depositors of such depository institutions and to the FDIC insurance funds in the event that the depository institution is insolvent or is in danger of becoming insolvent. For example, under the requirements of the Federal Reserve with respect to bank holding company operations, a bank holding company is required to serve as a source of financial strength to its subsidiary depository institutions and to commit resources to support such institutions in circumstances where it might not do so otherwise. In addition, the “cross-guarantee” provisions of federal law require insured depository institutions under common control to reimburse the FDIC for any loss suffered or reasonably anticipated by the FDIC as a result of the insolvency of commonly controlled insured depository institutions or for any assistance provided by the FDIC to commonly controlled insured depository institutions in danger of failure. The FDIC may decline to enforce the cross-guarantee provision if it determines that a waiver is in the best interests of the deposit insurance funds. The FDIC’s claim for reimbursement under the cross guarantee provisions is superior to claims of shareholders of the insured depository institution or its holding company but is subordinate to claims of depositors, secured creditors and nonaffiliated holders of subordinated debt of the commonly controlled insured depository institutions.

Federal Reserve System. In 1980, Congress enacted legislation that imposed reserve requirements on all depository institutions that maintain transaction accounts or nonpersonal time deposits. NOW accounts, money market deposit accounts and other types of accounts that permit payments or transfers to third parties fall within the definition of transaction accounts and are subject to these reserve requirements, as are any nonpersonal time deposits at an institution.

The reserve percentages are subject to adjustment by the Federal Reserve. Because required reserves must be maintained in the form of vault cash or in a non-interest-bearing account at, or on behalf of, a Federal Reserve Bank, the effect of the reserve requirement is to reduce the amount of the institution’s interest-earning assets.

However, in March 2020, in an unprecedented move, the Federal Reserve announced that the banking system had ample reserves, and, as reserve requirements no longer played a significant role in this regime, it reduced all reserve tranches to zero percent, thereby freeing banks from the reserve maintenance requirement. The action permits the Bank to loan or invest funds that were previously unavailable. The Federal Reserve has indicated that it expects to continue to operate in an ample reserves regime for the foreseeable future.

Transactions with Affiliates. Transactions between banks and their affiliates are governed by Sections 23A and 23B of the Federal Reserve Act. An affiliate of a bank is any bank or entity that controls, is controlled by or is under common control with such bank. Generally, Sections 23A and 23B (i) limit the extent to which the Bank or its subsidiaries may engage in “covered transactions” with any one affiliate to an amount equal to 10% of such institution’s capital stock and surplus, and maintain an aggregate limit on all such transactions with affiliates to an amount equal to 20% of such capital stock and surplus, and (ii) require that all such transactions be on terms substantially the same, or at least as favorable, to the association or subsidiary as those provided to a nonaffiliate. The term “covered transaction” includes the making of loans, purchase of assets, issuance of a guarantee and similar other types of transactions.

Transactions with Insiders. The Federal Reserve Act and related regulations impose specific restrictions on loans to directors, executive officers and principal shareholders of banks. Under Section 22(h) of the Federal Reserve Act, loans to a director, an executive officer and to a principal shareholder of a bank, and some affiliated entities of any of the foregoing, may not exceed, together with all other outstanding loans to such person and affiliated entities, the bank’s loan-to-one borrower limit. Loans in the aggregate to insiders and their related interests as a class may not exceed two times the bank’s unimpaired capital and unimpaired surplus until the bank’s total deposits equal or exceed $100,000,000, at which time the aggregate is limited to the bank’s unimpaired capital and unimpaired surplus. Section 22(h) also prohibits loans, above amounts prescribed by the appropriate federal banking agency, to directors, executive officers and principal shareholders of a bank or bank holding company, and their respective affiliates, unless such loan is approved in advance by a majority of the board of directors of the bank with any “interested” director not participating in the voting. The FDIC has prescribed the loan amount, which includes all other outstanding loans to such person, as to which such prior board of director approval is required, as being the greater of $25,000 or 5% of capital and surplus (up to $500,000). Section 22(h) requires that loans to directors, executive officers and principal shareholders be made on terms and underwriting standards substantially the same as offered in comparable transactions to other persons.

The Dodd-Frank Act also provides that banks may not “purchase an asset from, or sell an asset to” a bank insider (or their related interests) unless (i) the transaction is conducted on market terms between the parties, and (ii) if the proposed transaction represents more than 10 percent of the capital stock and surplus of the bank, it has been approved in advance by a majority of the bank’s non-interested directors.

Community Reinvestment Act. Under the Community Reinvestment Act and related regulations, depository institutions have an affirmative obligation to assist in meeting the credit needs of their market areas, including low and moderate-income areas, consistent with safe and sound banking practice. The Community Reinvestment Act directs each bank to maintain a public file containing specific information, including all written comments received from the public for the current year and each of the previous two calendar years that specifically relate to the bank's performance in helping to meet community credit needs. Depository institutions are periodically examined for compliance with the Community Reinvestment Act and are periodically assigned ratings in this regard. Banking regulators consider a depository institution's Community Reinvestment Act rating when reviewing applications to establish new branches, undertake new lines of business, and/or acquire part or all of another depository institution. An unsatisfactory rating can significantly delay or even prohibit regulatory approval of a proposed transaction by a bank holding company or its depository institution subsidiaries.

In October 2023, the Office of the Comptroller of the Currency ("OCC"), the Federal Reserve System Board and the FDIC finalized comprehensive revisions to their CRA regulations. The objectives in issuing the final rule include strengthening the achievement of the core purpose of the statute, adapting to changes in the banking industry, including the expanded role of mobile and online banking, tailoring performance standards to account for differences in bank size and business models and local conditions, confirming that CRA and fair lending responsibilities are mutually reinforcing, and promoting a consistent regulatory approach that applies to banks regulated by all three agencies. The final rule is expected to go into effect on April 1, 2024, but most provisions of the rule, including the new tests, the need to define retail lending assessment areas, and the data collection requirements, will become applicable on January 1, 2026. Reporting of the collected data will not be required until 2027. In addition to numerous technical revisions, the final rule introduces major changes to the CRA regulations in four key areas: (A) the delineation of assessment areas; (B) the overall evaluation framework and performance standards and metrics; (C) the definition of community development activities; and (D) data collection and reporting. The new evaluation framework is "tailored" based on the size of the bank.

Fair Lending; Consumer Laws. In addition to the Community Reinvestment Act, other federal and state laws regulate various lending and consumer aspects of the banking business. Governmental agencies, including the Department of Housing and Urban Development, the Federal Trade Commission and the Department of Justice, have become concerned that prospective borrowers experience discrimination in their efforts to obtain loans from depository and other lending institutions. These agencies have brought litigation against depository institutions alleging discrimination against borrowers. Many of these suits have been settled, in some cases for material sums, short of a full trial.

These governmental agencies have clarified what they consider to be lending discrimination and have specified various factors that they will use to determine the existence of lending discrimination under the Equal Credit Opportunity Act and the Fair Housing Act, including evidence that a lender discriminated on a prohibited basis, evidence that a lender treated applicants differently based on prohibited factors in the absence of evidence that the treatment was the result of prejudice or a conscious intention to discriminate, and evidence that a lender applied an otherwise neutral non-discriminatory policy uniformly to all applicants, but the practice had a discriminatory effect, unless the practice could be justified as a business necessity.

Banks and other depository institutions are also subject to numerous consumer-oriented laws and regulations. These laws, which include the Truth in Lending Act, the Truth in Savings Act, the Real Estate Settlement Procedures Act, the Electronic Funds Transfer Act, the Funds Availability Act, the Equal Credit Opportunity Act, and the Fair Housing Act, require compliance by depository institutions with various disclosure requirements and requirements regulating the availability of funds after deposit or the making of some loans to customers.

Privacy Regulations. The GLBA contains extensive customer privacy protection provisions. Under these provisions, a financial institution must provide to its customers, both at the inception of the customer relationship and on an annual basis, the institution's policies and procedures regarding the handling of customers' nonpublic personal financial information. The law provides that, except for specific limited exceptions, an institution may not provide such personal information to unaffiliated third parties unless the institution discloses to the customer that such information may be so provided and the customer is given the opportunity to opt out of such disclosure. An institution may not disclose to a non-affiliated third party, other than to a consumer reporting agency, customer account numbers or other similar account identifiers for marketing purposes. The GLBA also provides that the states may adopt customer privacy protections that are more strict than those contained in the act.

Regulation P provides an exception under which financial institutions that meet certain conditions are not required to provide annual privacy notices to customers. To qualify for this exception, a financial institution must not share nonpublic personal information about customers except as described in certain statutory exceptions. In addition, the rule requires that the financial institution must not have changed its policies and practices with regard to disclosing nonpublic personal information from those that the institution disclosed in the most recent privacy notice it sent. As part of its implementation, the CFPB also amended Regulation P to provide timing requirements for delivery of annual privacy notices in the event that a financial institution that qualified for this annual notice exception later changes its policies or practices in such a way that it no longer qualifies for the exception. The CFPB further removed the Regulation P provision that allowed for use of the alternative delivery method for annual privacy notices because the CFPB believes the alternative delivery method will no longer be used in light of the annual notice exception.

Anti-Money Laundering Laws and Regulations. The Bank is subject to several federal laws that are designed to combat money laundering, terrorist financing, and transactions with persons, companies or foreign governments designated by U.S. authorities ("AML laws"). This category of laws includes the Bank Secrecy Act of 1970, the Money Laundering Control Act of 1986, the USA PATRIOT Act of 2001, and the Anti-Money Laundering Act of 2020. The Anti-Money Laundering Act of 2020, the most sweeping anti-money laundering legislation in 20 years, requires various federal agencies to promulgate regulations implementing a number of its provisions.

The AML laws and their implementing regulations require insured depository institutions, broker-dealers, and certain other financial institutions to have policies, procedures, and controls to detect, prevent, and report money laundering and terrorist financing. The AML laws and their regulations also provide for information sharing, subject to conditions, between federal law enforcement agencies and financial institutions, as well as among financial institutions, for counter-terrorism purposes. Federal banking regulators are required, when reviewing bank holding company acquisition and bank merger applications, to take into account the effectiveness of the anti-money laundering activities of the applicants. To comply with these obligations, the Company has implemented appropriate internal practices, procedures, and controls.

Cybersecurity. The federal banking agencies have adopted guidelines for establishing information security standards and cybersecurity programs for implementing safeguards under the supervision of a financial institution's board of directors. These guidelines, along with related regulatory materials, increasingly focus on risk management and processes related to information technology and the use of third parties in the provision of financial products and services. The federal banking agencies expect financial institutions to establish lines of defense and ensure that their risk management processes also address the risk posed by compromised customer credentials, and also expect financial institutions to maintain sufficient business continuity planning processes to ensure rapid recovery, resumption and maintenance of the institution's operations after a cyber-attack. If the Bank fails to meet the expectations set forth in this regulatory guidance, it could be subject to various regulatory actions and any remediation efforts may require significant resources of the Bank. In addition, all federal and state bank regulatory agencies continue to increase focus on cybersecurity programs and risks as part of regular supervisory exams.

In November 2021, the federal banking agencies approved a final rule effective on April 1, 2022 that, among other things, requires banking organizations to notify their primary regulator within 36 hours of becoming aware of a "computer-security incident" that rises to the level of a "notification incident." The rule also requires bank service providers to notify their banking organization customers as soon as possible after becoming aware of similar incidents.

In 2023, the SEC issued a final rule that requires disclosure of material cybersecurity incidents, as well as cybersecurity risk management, strategy and governance. Under this rule, banking organizations that are SEC registrants must generally disclose information about a material cybersecurity incident within four business days of determining it is material with periodic updates as to the status of the incident in subsequent filings as necessary.

Sarbanes-Oxley Act of 2002. The Sarbanes-Oxley Act implemented a number of laws affecting corporate governance, accounting obligations and corporate reporting. The Sarbanes-Oxley Act is applicable to all companies with equity securities registered or that file reports under the Securities Exchange Act of 1934. In particular, the Sarbanes-Oxley Act established: (i) requirements for audit committees, including independence, expertise, and responsibilities; (ii) responsibilities regarding financial statements for the Chief Executive Officer and Chief Financial Officer of the reporting company; (iii) standards for auditors and regulation of audits; (iv) disclosure and reporting obligations for reporting companies and their directors and executive officers; and (v) civil and criminal penalties for violations of the securities laws. Because the Company's common stock is registered with the SEC, it is currently subject to these requirements.

Incentive Compensation. In June 2010, the Federal Reserve issued a final rule on incentive compensation policies intended to ensure that the incentive compensation policies of banking organizations do not undermine the safety and soundness of such organizations by encouraging excessive risk-taking. Banking organizations are instructed to review their incentive compensation policies to ensure that they do not encourage excessive risk-taking and implement corrective programs as needed. The Federal Reserve will review, as part of the regular, risk-focused examination process, the incentive compensation arrangements of banking organizations, such as the Bank, that are not "large, complex banking organizations." These reviews will be tailored to each organization based on the scope and complexity of the organization's activities and the prevalence of incentive compensation arrangements. The findings of the supervisory initiatives will be included in reports of examination. Deficiencies will be incorporated into the organization's supervisory ratings, which can affect the organization's ability to make acquisitions and take other actions.

Dodd-Frank Act. In July 2010, the Dodd-Frank Act was signed into law, incorporating numerous financial institution regulatory reforms. The Dodd-Frank Act implements far-reaching reforms of major elements of the financial landscape, particularly for larger financial institutions. Many of its provisions do not directly impact community-based institutions like the Bank. For instance, provisions that regulate derivative transactions and limit derivatives trading activity of federally-insured institutions, enhance supervision of "systemically significant" institutions, impose new regulatory authority over hedge funds, limit proprietary trading by banks, and phase-out the eligibility of trust preferred securities for Tier 1 capital are among the provisions that do not directly impact the Bank either because of exemptions for institutions below a certain asset size or because of the nature of the Bank's operations. Certain aspects of the Dodd-Frank Act remain subject to rulemaking and interpretation and will take effect over several years, and their impact on the Company or the financial industry is difficult to predict before such regulations or interpretations are adopted.

In May 2018, the Economic Growth Act was enacted to modify or remove certain regulatory financial reform rules and regulations, including some of those implemented under the Dodd-Frank Act. While the Economic Growth Act maintains most of the regulatory structure established by the Dodd-Frank Act, it amends certain aspects of the regulatory framework for small depository institutions with assets of less than $10 billion, such as the Bank, and for large banks with assets of more than $50 billion.

Among other matters, the Economic Growth Act expands the definition of qualified mortgages which may be held by a financial institution with total consolidated assets of less than $10 billion, exempts community banks from the Volcker Rule, and includes additional regulatory relief regarding regulatory examination cycles, call reports, mortgage disclosures and risk weights for certain high-risk commercial real estate loans.

*Future Legislation and Regulation***.** Congress may enact legislation from time to time that affects the regulation of the financial services industry, and state legislatures may enact legislation from time to time affecting the regulation of financial institutions chartered by or operating in those states. Federal and state regulatory agencies also periodically propose and adopt changes to their regulations or change the manner in which existing regulations are applied. The substance or impact of pending or future legislation or regulation, or the application thereof, cannot be predicted, although enactment of the proposed legislation could impact the regulatory structure under which the Company and the Bank operate and may significantly increase costs, impede the efficiency of internal business processes, require an increase in regulatory capital, require modifications to business strategy, and limit the ability to pursue business opportunities in an efficient manner. A change in statutes, regulations or regulatory policies applicable to the Company or the Bank could have a material, adverse effect on the business, financial condition and results of operations of the Company and the Bank. Future legislation, regulation, and government policy could affect the banking industry as a whole, including the business and results of operations of the Company and the Bank, in ways that are difficult to predict. The Company fully expects that the financial institution industry will remain heavily regulated in the near future and that additional laws or regulations may be adopted further regulating specific banking practices.

Wage and Hour Division, Department of Labor. On December 16, 2019, the Department of Labor issued a final rule, the rule updates a number of regulations on the calculation of overtime compensation both to provide clarity and to better reflect the 21st-century workplace. These changes will promote compliance with the FLSA, provide appropriate and updated guidance in an area of evolving law and practice, and encourage employers to provide additional and innovative benefits to workers without fear of costly litigation. This final rule was effective on January 15, 2020.

CARES Act. In response to the COVID-19 pandemic, President Trump signed into law the Coronavirus Aid, Relief, and Economic Security ("CARES") Act on March 27, 2020. Among other things, the CARES Act included the Small Business Administration's Paycheck Protection Program. Under the Paycheck Protection Program, funds were authorized for small business loans to pay payroll and group health costs, salaries and commissions, mortgage and rent payments, utilities, and interest on other debt. The loans were provided through participating financial institutions, including the Bank, that processed loan applications and serviced the loans.

Item 1A. Risk Factors

The Company is subject to many risks that could adversely affect its future financial condition and performance and, therefore, the market value of its securities. The risk factors applicable to the Company include, but are not limited to the following:

Credit Risks

The Company's concentration in loans secured by real estate may increase its credit losses, which would negatively affect our financial results.

At December 31, 2023, loans secured by real estate totaled $1.0 billion and represented 71.5% of the Company's loan portfolio, net of net deferred loan costs and premiums. If we experience adverse changes in the local real estate market or in the local or national economy, borrowers' ability to pay these loans may be impaired, which could impact the Company's financial performance. The Company attempts to limit its exposure to this risk by applying good underwriting practices at origination, evaluating the appraisals used to establish property values, and routinely monitoring the financial condition of borrowers. If the value of real estate serving as collateral for the loan portfolio were to continue to decline materially, a significant part of the loan portfolio could become under-collateralized. If the loans that are secured by real estate become troubled when real estate market conditions are declining or have declined, in the event of foreclosure, the Company may not be able to realize the amount of collateral that was anticipated at the time of originating the loan. In that event, the Company might have to increase the provision for loan losses, which could have a material adverse effect on its operating results and financial condition.

An inadequate allowance for credit losses would reduce our earnings.

Our earnings are significantly affected by our ability to properly originate, underwrite and service loans. We maintain an allowance for credit losses on loans based upon many factors, including the following:

- actual loan loss history;
- nature, terms, and volume of the loan portfolio;
- the amount and trends of problems loans and non-performing loans;
- the effect of changes in the local real estate market on collateral values;
- the legal and regulatory environment;
- lending policies and procedures;
- credit administrations and lending staff;
- concentrations of credit;
- the loan review function;
- the effect of current economic conditions on a borrower's ability to pay; and
- other factors deemed relevant by management.

These determinations are based upon estimates that are inherently subjective, and their accuracy depends on the outcome of future events; therefore, realized losses may differ from current estimates. Changes in economic, operating, and other conditions, including changes in interest rates, which are generally beyond our control, could increase actual loan losses significantly. As a result, actual losses could exceed our current allowance estimate. We cannot provide assurance that our allowance for credit losses is sufficient to cover actual loan losses should such losses differ significantly from the current estimates.

Technology Risks

The Company's operations may be adversely affected by cybersecurity risks.

In the ordinary course of business, the Company collects and stores sensitive data, including proprietary business information and personally identifiable information of its customers and employees in systems and on networks of the Company and its customers and third-party service providers. The secure processing, maintenance, and use of this information is critical to the Company's operations and business strategy. In addition, the Company relies heavily on communications and information systems to conduct its business. Any failure, interruption, or breach in security or operational integrity of these systems could result in failures or disruptions in the Company's customer relationship management, general ledger, deposit, loan, and other systems. The Company has invested in accepted technologies, and continually reviews processes and practices that are designed to protect its networks, computers, and data from damage or unauthorized access. To date, the Company has not experienced a significant compromise, significant data loss or any material financial losses related to cybersecurity attacks, but the Company's

systems and those of its customers and third-party service providers are under constant threat and it is possible that the Company could experience a significant event in the future. Risks and exposures related to cybersecurity attacks are expected to remain high for the foreseeable future due to the rapidly evolving nature and sophistication of these threats, as well as due to the expanding use of Internet banking, mobile banking and other technology-based products and services by the Company and its customers. The Company's computer systems and infrastructure may be vulnerable to attacks by hackers or breached due to employee error, malfeasance, or other disruptions. A breach of any kind could compromise systems and the information stored there could be accessed, damaged, or disclosed. A breach in security or other failure could result in legal claims, regulatory penalties, disruption in operations, increased expenses, loss of customers and business partners, and damage to the Company's reputation, which could adversely affect its business and financial condition. Furthermore, as cyber threats continue to evolve and increase, the Company may be required to expend significant additional financial and operational resources to modify or enhance its protective measures, or to investigate and remediate any identified information security vulnerabilities.

Failure to keep pace with technological change could adversely affect our business.

The financial services industry is continually undergoing rapid technological change with frequent introductions of new technology-driven products and services. The effective use of technology increases efficiency and enables financial institutions and other firms to better serve customers and to reduce costs. The pace of these technological changes has increased in the "Fintech" environment, in which industry changing products and services are often introduced and adopted, including innovative ways that customers can make payments, access products, and manage accounts. Our future success depends, in part, upon our ability to address the needs of our customers by using technology to provide products and services that will satisfy customer demands, as well as to create additional efficiencies in our operations. Many of our competitors have substantially greater resources to invest in technological improvements. We may not be able to effectively implement new technology-driven products and services, which could entail significant time, resources and additional risk to develop or adopt, or be successful in marketing these products and services to our customers. Failure to successfully keep pace with technological change affecting the financial services industry could have a material adverse impact on our business and, in turn, our financial condition and results of operations.

Liquidity and Interest Rate Risks

The Company's success depends upon its ability to manage interest rate risk.

The profitability of the Company depends significantly on its net interest income, which is the difference between the interest earned on loans, securities and other interest-earning assets, and the interest paid on deposits and borrowings. Changes in interest rates will affect the rates earned on securities and loans and rates paid on deposits and other borrowings. These factors include competition, federal economic, monetary and fiscal policies, and general economic conditions.

In addition, changes in interest rates may negatively affect both the returns on and market value of the Company's investment securities. During 2022 and early 2023, the FRB increased the federal funds rate 11 times and has held such rates steady since July 2023. Interest rate changes can reduce unrealized gains or increase unrealized losses in its portfolio and thereby negatively impact its accumulated other comprehensive income and equity levels. Further, such losses could be realized into earnings should liquidity and/or business strategy necessitate the sales of securities in a loss position. Additionally, actual investment income and cash flows from investment securities that carry prepayment risk, such as mortgage-backed securities and callable securities, may materially differ from those anticipated at the time of investment or subsequently as a result of changes in interest rates and market conditions. These occurrences could have a material adverse effect on the Company's net interest income or our results of operations.

The Company relies substantially on deposits obtained from customers in its target markets to provide liquidity and support growth.

The Company requires sufficient liquidity to fund asset growth, meet customer loan requests, customer deposit maturities and withdrawals, make payments on its debt obligations as they come due and other cash commitments. The Company's business strategy is based primarily on access to funding from local customer deposits. Deposit levels may be affected by a number of factors, including interest rates paid by competitors, general interest rate levels, returns available to customers on alternative investments, changes in the liquidity needs of our depositors and general economic conditions that affect savings levels and the amount of liquidity in the economy, including government stimulus efforts in response to economic crises. If market interest rates rise or our competitors raise the rates they pay on deposits, the Company's funding costs may increase, either because we raise our rates to avoid losing deposits or because we lose deposits and must rely on more expensive sources of funding. Either of these factors could reduce the Company's net interest margin and net interest income and could have a material adverse effect on the Company's business, financial condition, results of operations, liquidity and cash flows from operations.

Further, if local customer deposits are not sufficient to fund the Company's normal operations and growth, we may rely on secondary sources of liquidity, such as borrowings from the Federal Home Loan Bank of Atlanta ("FHLB"), and federal funds lines of credit with larger institutions; however, there can be no assurance that these arrangements will be available to us when needed on favorable terms, or at all, or that they will be sufficient to meet future liquidity needs. For example, the Company's ability to access borrowings from the FHLB will be dependent upon whether and the extent to which we can provide collateral to secure FHLB borrowings. In addition, the availability of these funding sources is highly dependent upon the perception of the liquidity and creditworthiness of the financial institution, and such perception can change quickly in response to market conditions or circumstances unique to a particular company. The Company also may need to raise funds through the issuance of shares of our debt or equity securities, or the sale of investment securities or loans, as additional sources of liquidity. If the Company is unable to access funding sufficient to support our business operations and growth strategies or are unable to access such funding on attractive terms, the Company may not be able to implement our business strategies or satisfy our obligations.

Market Risks

The Company's success depends upon its ability to compete effectively in the banking industry.

The Company's banking subsidiary faces competition from banks and other financial institutions, including savings and loan associations, savings banks, finance companies and credit unions for deposits, loans and other financial services in our market area. Certain divisions within the banking subsidiary face competition from wealth management and investment brokerage firms. A number of these banks and other financial institutions are significantly larger and have substantially greater access to capital and other resources, as well as larger lending limits and branch systems, and offer a wider array of banking services. In addition, the Company faces competition from market place lenders and other financial technology firms, which may provide competitive services quickly and in innovative ways and may have fewer regulatory constraints and lower cost structures. This competition may reduce or limit our margins and our market share and may adversely affect our results of operations and financial condition.

The Company could be adversely affected by economic conditions in its market area.

The Company's branches are located in the counties of Clarke, Frederick, Fauquier, and Loudoun, the towns of Purcellville, Leesburg and Ashburn, and the City of Winchester. The Company also operates loan production offices in the counties of Fairfax (Virginia) as well as Frederick (Maryland). Because our lending is concentrated in these markets, we will be affected by the general economic conditions in these areas. Changes in the economy may influence the growth rate of our loans and deposits, the quality of the loan portfolio and loan and deposit pricing. Although the domestic and global economies have largely recovered from the COVID-19 pandemic, certain consequences of the pandemic continue to impact the macroeconomic environment and may persist for some time. For example, the COVID-19 pandemic could have long-lasting impacts certain industries due to changes in consumer behavior and business practices, including remote work and business travel. Further, the growth in economic activity and in the demand for goods and services, coupled with labor shortages, supply chain disruptions and other factors, has contributed to rising inflationary pressures, the Federal Reserve's responsive interest rate hikes, and the risk of recession. A decline in general economic conditions caused by inflation, recession, unemployment or other factors beyond our control would impact the demand for banking products and services generally, which could negatively affect our financial condition and performance.

The soundness of other financial institutions could adversely affect us.

Our ability to engage in routine funding transactions could be adversely affected by the actions and commercial soundness of other financial institutions. Financial services institutions are interrelated as a result of trading, clearing, counterparty or other relationships. We have exposure to many different industries and counterparties, and we routinely execute transactions with counterparties in the financial industry. As a result, defaults by, or even rumors or questions about, one or more financial services institutions, or the financial services industry generally, have led to market-wide liquidity problems and could lead to losses or defaults by us or by other institutions. Many of these transactions expose us to credit risk in the event of default of our counterparty or client. In addition, our credit risk may be exacerbated when the collateral held by us cannot be realized upon or is liquidated at prices not sufficient to recover the full amount of the financial instrument exposure due us. There is no assurance that any such losses would not materially and adversely affect our results of operations.

In addition, financial challenges at other banking institutions could lead to depositor concerns that spread within the banking industry. In March 2023, Silicon Valley Bank and Signature Bank experienced large deposit outflows coupled with insufficient liquidity to meet withdrawal demands, resulting in the institutions being placed into FDIC receiverships. In the aftermath, there was substantial market disruption and concern that diminished depositor confidence could spread across the banking industry, leading to deposit outflows that could destabilize other institutions. While public confidence in the banking

system has stabilized, deposit outflows caused by reputational concerns or events affecting the banking industry generally could adversely affect the Company’s liquidity, financial condition, and results of operations.

Operational Risks

Our exposure to operational risk may adversely affect our business.

We are exposed to many types of operational risk, including reputational risk, legal and compliance risk, the risk of fraud or theft by employees or outsiders, unauthorized transactions by employees or operational errors, including clerical or record-keeping errors or those resulting from faulty or disabled computer or telecommunications systems.

Reputational risk, or the risk to our earnings and capital from negative public opinion, could result from our actual alleged conduct in any number of activities, including lending practices, corporate governance, regulatory compliance or the occurrence of any of the events or instances mentioned below, or from actions taken by government regulators or community organizations in response to that conduct. Negative public opinion could also result from adverse news or publicity that impairs the reputation of the financial services industry generally.

Further, if any of our financial, accounting, or other data processing systems fail or have other significant shortcomings, we could be adversely affected. We depend on internal systems and outsourced technology to support these data storage and processing operations. Our inability to use or access these information systems at critical points in time could unfavorably impact the timeliness and efficiency of our business operations. We could be adversely affected if one of our employees causes a significant operational break-down or failure, either as a result of human error or where an individual purposefully sabotages or fraudulently manipulates our operations or systems. We are also at risk of the impact of natural disasters, terrorism and international hostilities on our systems or for the effects of outages or other failures involving power or communications systems operated by others.

If any of the foregoing risks materialize, it could have a material adverse affect on our business, financial condition and results of operations.

The Company may not be able to successfully manage its growth or implement its growth strategy, which may adversely affect results of operations and financial condition.

A key component of the Company’s business strategy is to continue to grow and expand. The Company’s ability to grow and expand depends upon its ability to open new branch locations, attract new deposits to the existing and new branch locations, and identify attractive loan and investment opportunities. The Company may not be able to implement its growth strategy if it is unable to identify attractive markets or branch locations. Once identified, successfully managing growth will depend on integrating the new branch locations while maintaining adequate capital, cost controls and asset quality. As this growth strategy is implemented, the Company will incur construction costs and increased personnel, occupancy and other operating expenses. Because these costs are incurred before new deposits and loans are generated, adding new branch locations will initially decrease earnings, despite efficient execution of this strategy. In addition, the Company could experience difficulties expanding into new markets or product lines. The Company’s lack of history and familiarity with those markets, clients and lines of business may lead to unexpected challenges or difficulties that inhibit its success and adversely affect the Company’s results of operations.

Severe weather, natural disasters, acts of war or terrorism, geopolitical instability, public health issues, and other external events could significantly impact the Company's business.

Severe weather, natural disasters, acts of war or terrorism, geopolitical instability, public health issues, and other adverse external events could have a significant impact on the Company's ability to conduct business. In addition, such events could affect the stability of the Company’s deposit base, cause economic or market uncertainty, negatively impact consumer confidence, impair the ability of borrowers to repay outstanding loans, impair the value of collateral securing loans, cause significant property damage, result in loss of revenue, and/or cause the Company to incur additional expenses. The Company is also at risk of the impact of natural disasters, terrorism, and international hostilities on its systems and from the effects of cyberattacks, outages or other failures involving power or communications systems operated by others, which may give rise to disruption of service to customers and to financial loss or liability. The occurrence of any such events in the future and the economic impact from such events could have a material adverse effect on the Company's business, which, in turn, could have a material adverse effect on its financial condition and results of operations.

The Company relies heavily on its senior management team and the unexpected loss of key officers could adversely affect operations.

The Company believes that its growth and success depends heavily upon the skills of its senior management team. The Company also depends on the experience of its subsidiary's officers and on their relationships with the customers they serve. The loss of one or more of these officers could disrupt the Company's operations and impair its ability to implement its business strategy, which could adversely affect the Company's financial condition and performance.

Legal, Regulatory and Compliance Risks

Government measures to regulate the financial industry, including the Dodd-Frank Act, subject us to increased regulation and could adversely affect us.

As a financial institution, we are heavily regulated at the state and federal levels. These laws and regulations are generally intended to benefit consumers, borrowers and depositors, but not investors. Our success depends on our ability to maintain compliance with existing and new laws and regulations. We face, and expect to continue to face, increased public and legislative scrutiny as well as stricter and more comprehensive regulation of our financial services practices. The Dodd-Frank Act includes significant changes in the financial regulatory landscape and has increased our operations and compliance costs in the short-term. Future legislation, regulation and government policy, which are beyond our control, may change rapidly and unpredictably and could affect the banking industry as a whole, including our business and results of operations, in ways that are difficult to predict. We expect that financial institutions will remain heavily regulated in the near future and that additional laws or regulations may be adopted further regulating specific banking practices. As a result of the provisions in the Dodd-Frank Act and other current or future laws and regulations applicable to the Bank, we could experience additional costs, as well as limitations on the products and services we offer and on our ability to efficiently pursue business opportunities, which may adversely affect our businesses, financial condition or results of operations.

The Bank is subject to stringent capital and liquidity requirements as a result of the Basel III regulatory capital reforms and the Dodd-Frank Act.

The Bank is subject to capital adequacy guidelines and other regulatory requirements specifying minimum amounts and types of capital which it must maintain. From time to time, regulators implement changes to these regulatory capital adequacy guidelines. Under the Dodd-Frank Act, the federal banking agencies have established stricter capital requirements and leverage limits for banks and bank holding companies that are based on the Basel III regulatory capital reforms. The Basel III Capital Rules require banking organizations to maintain significantly more capital and adopted more demanding regulatory capital risk weightings and calculations. While the recently passed Economic Growth Act requires that federal banking regulators establish a simplified leverage capital framework for smaller banks, these more stringent capital requirements could, among other things, limit banking operations and activities, and growth of loan portfolios, in order to focus on retention of earnings to improve capital levels. The Bank believes that it maintains sufficient levels of Tier 1 and Common Equity Tier 1 capital to comply with the Basel III Final rules. However, if the Bank fails to meet these minimum capital guidelines and/or other regulatory requirements, the Bank could be subject to regulatory restrictions, including limitations on paying dividends to the holding company for shareholder dividends and share repurchases and paying discretionary bonuses, or experience other adverse consequences that could cause its financial condition to be materially and adversely affected.

Changes in accounting standards could impact reported earnings and capital.

The authorities that promulgate accounting standards, including the Financial Accounting Standards Board (the "FASB"), the SEC, and other regulatory authorities, periodically change the financial accounting and reporting standards that govern the preparation of the Company's consolidated financial statements. These changes are difficult to predict and can materially impact how the Company records and reports its financial condition and results of operations. In some cases, the Company could be required to apply a new or revised standard retroactively, resulting in the restatement of financial statements for prior periods. Such changes could also impact the capital levels of the Bank, or require the Company to incur additional personnel or technology costs. Most notably, new guidance on the calculation of credit reserves using current expected credit losses, referred to as CECL, was finalized in June 2016. The standard was effective for the Company beginning January 1, 2023. To implement the new standard, the Company has and will incur costs related to data collection and documentation, technology and training. Upon implementation in 2023, the Company recognized a one-time cumulative effect adjustment to reduce retained earnings and increase the allowance for credit losses as well as the reserve for unfunded commitments as a result of adopting the CECL standard as further described in Note 1 to the Consolidated Financial Statements. If the Company is required to materially increase the level of the allowance for credit losses or incurs additional expenses to determine the appropriate level of the allowance for credit losses, such changes could adversely affect the Company's capital levels, financial condition and results of operations.

Increasing scrutiny and evolving expectations from customers, regulators, investors, and other stakeholders with respect to environmental, social and governance (ESG) practices may impose additional costs on the Company or expose it to new or additional risks.

Companies are facing increasing scrutiny from customers, regulators, investors, and other stakeholders related to ESG practices and disclosure. Investor advocacy groups, investment funds, and influential investors are also increasingly focused on these practices, especially as they relate to climate risk, hiring practices, the diversity of the work force, and racial and social justice issues. Increased ESG related compliance costs could result in increases to the Company's overall operational costs. Failure to adapt to or comply with regulatory requirements or investor or stakeholder expectations and standards could negatively impact the Company's reputation, ability to do business with certain partners, and the Company's stock price. New government regulations could also result in new or more stringent forms of ESG oversight and expanding mandatory and voluntary reporting, diligence, and disclosure.

Climate change and related legislative and regulatory initiatives may result in operational changes and expenditures that could significantly impact the Company's business.

The current and anticipated effects of climate change are creating an increasing level of concern for the state of the global environment. As a result, political and social attention to the issue of climate change has increased. Federal and state legislatures and regulatory agencies have continued to propose and advance numerous legislative and regulatory initiatives seeking to mitigate the effects of climate change. The federal banking agencies have emphasized that climate-related risks are faced by banking organizations of all types and sizes and are in the process of enhancing supervisory expectations regarding banks' risk management practices. In December 2021, the OCC published proposed principles for climate risk management by banking organizations with more than $100 billion in assets. The OCC also has appointed its first ever Climate Change Risk Officer and established an internal climate risk implementation committee in order to assist with these initiatives and to support the agency's efforts to enhance its supervision of climate change risk management. Similar and even more expansive initiatives are expected, including potentially increasing supervisory expectations with respect to banks' risk management practices, accounting for the effects of climate change in stress testing scenarios and systemic risk assessments, revising expectations for credit portfolio concentrations based on climate-related factors and encouraging investment by banks in climate-related initiatives and lending to communities disproportionately impacted by the effects of climate change. To the extent that these initiatives lead to the promulgation of new regulations or supervisory guidance applicable to the Company, the Company would likely experience increased compliance costs and other compliance-related risks.

In March 2024, the SEC issued new climate-related disclosure rules, which when effective, will require new climate-related disclosures in SEC filings and audited financial statements, including certain climate-related metrics and greenhouse gas emissions data, information about climate-related targets and goals, transition plans, if any, and attestation requirements. While the final rule was scaled-down from the original proposal and includes a phase-in period, these rules could impose increased costs.

The lack of empirical data surrounding the credit and other financial risks posed by climate change render it impossible to predict how specifically climate change may impact the Company's financial condition and results of operations; however, the physical effects of climate change may also directly impact the Company. Specifically, unpredictable and more frequent weather disasters may adversely impact the value of real property securing the loans in the Bank's loan portfolio. Additionally, if insurance obtained by borrowers is insufficient to cover any losses sustained to the collateral, or if insurance coverage is otherwise unavailable to borrowers, the collateral securing loans may be negatively impacted by climate change, which could impact the Company's financial condition and results of operations. Further, the effects of climate change may negatively impact regional and local economic activity, which could lead to an adverse effect on customers and impact the communities in which the Company operates. Overall, climate change, its effects and the resulting, unknown impact could have a material adverse effect on the Company's financial condition and results of operations.

Risks Relating to Our Securities

There can be no assurances concerning continuing dividend payments.

Our common stockholders are only entitled to receive the dividends declared by our Board of Directors. Although we have historically paid quarterly dividends on our common stock, there can be no assurances that we will be able to continue to pay regular quarterly dividends or an annual stock dividend or that any dividends we do declare will be in any particular amount. The primary source of money to pay our cash dividends comes from dividends paid to the Company by the Bank. The Bank's ability to pay dividends to the Company is subject to, among other things, its earnings, financial condition and applicable

regulations, which in some instances limit the amount that may be paid as dividends. In addition, the Company and the Bank are required to maintain a capital conservation buffer of 2.5% of Common Equity Tier 1 Capital on top of minimum risk-weighted asset ratios to pay dividends without additional restrictions.

There is a limited trading market for our common shares, and you may not be able to resell your shares at or above the price you paid for them.

Although our common shares are listed for trading under the symbol "EFSI," the trading in our common shares has substantially less liquidity than many other publicly traded companies. A public trading market having the desired characteristics of depth, liquidity and orderliness depends on the presence in the market of willing buyers and sellers of our common shares at any given time. This presence depends on the individual decisions of investors and general economic and market conditions over which we have no control. We cannot assure you that volume of trading in our common shares will increase in the future.

The stock market can be volatile, and fluctuations in our operating results and other factors could cause our stock price to decline.

The stock market has experienced, and may continue to experience, fluctuations that significantly impact the market prices of securities issued by many companies. Market fluctuations could adversely affect our stock price. These fluctuations have often been unrelated or disproportionate to the operating performance of particular companies. These broad market fluctuations, as well as general economic, systemic, political and market conditions, such as recessions, loss of investor confidence, interest rate changes, tariffs, government shutdowns, or international currency fluctuations, may negatively affect the market price of our common stock. Moreover, our operating results may fluctuate and vary from period to period due to the risk factors set forth herein. As a result, period-to-period comparisons should not be relied upon as an indication of future performance. Our stock price could fluctuate significantly in response to our quarterly or annual results, annual projections, and the impact of these risk factors on our operating results or financial position.

Item 1B. Unresolved Staff Comments

None.

Item 1C. Cybersecurity

Risk Management and Strategy

Cybersecurity risks are constantly evolving and becoming increasingly pervasive across all industries. To mitigate these risks and protect sensitive customer data, financial transactions, and our information systems, the Company has implemented a comprehensive Information Security Program ("Program") which is a component of its overarching enterprise risk management program. The Program is achieved through a collaborative effort involving operations, technology, compliance, risk, and senior management. Cybersecurity is a critical component of this program, given the increasing reliance on technology and potential cyber threats.

Key components of the risk management program include:

- A risk assessment process that identifies and prioritizes material risks; defines and evaluates the effectiveness of controls to mitigate the risks; and reports results to executive management and the Board of Directors.
- Third-party managed detection and response service, which monitors the security of our information systems around-the-clock, including intrusion detection and alerting.
- A patch management system that safeguards our environment by keeping software up-to-date and resilient against threats.
- Internal and external penetration testing that is conducted and reviewed either by independent third parties or qualified employees.
- A third-party risk management program that is designed to ensure our vendors meet our cybersecurity requirements.
- A training and awareness program that educates employees about cybersecurity risks and how to protect themselves from cyberattacks.
- An incident response plan that outlines the steps the Company will take to respond to a cybersecurity incident, which is tested at least annually.

Governance and Oversight

The Board of Directors, including its Risk Subcommittee provides oversight of Company cybersecurity risks. The Board of Directors receives periodic reports on cybersecurity threats, awareness training, and key risk indicators related to cybersecurity. Additionally, the Company's Audit Committee provides oversight as it relates to annual audits related to information technology and cybersecurity. Management promptly reviews results of these audits to initiate necessary remediation, which are then reviewed by the Audit Committee.

The Board of Directors has designated the Security Committee and Incident Response Team with responsibilities related to information security and cybersecurity.

The Security Committee is a management committee with representation from operations, technology, compliance, risk, and senior management. The Security Committee monitors, reviews, and makes necessary changes to the Information Security Program. This Committee provides accountability for policies and procedures and reviews incidents that may affect information security.

The Incident Response Team has overall authority and responsibility for preparing and responding to incidents and consists of various sub-teams including representation from operations, technology, risk, compliance, human resources, and marketing. While key personnel have identified roles, this team ensures appropriate reports, statuses, and decisions are presented to the Executive Management and the Board of Directors.

The Company's Chief Technology Officer ("CTO") oversees the Company's information technology programs and investments. The Company's CTO has over 30 years of information technology experience. The Company's Compliance and Security Officer, who oversees the Company's information security programs, has over 10 years of experience and reports to the Chief Operating Officer. The Compliance and Security Officer is designated as the program coordinator responsible for coordinating and overseeing the Information Security Program.

Material Effects of Cybersecurity Threats

While cybersecurity risks have the potential to materially affect the Company's business, financial condition, and results of operations, the Company does not believe that risks from cybersecurity threats or attacks, including because of any previous cybersecurity incidents, have materially affected the Company, including its business strategy, results of operations or financial condition. However, the sophistication of cyber threats continues to increase, and the Company's cybersecurity risk management and strategy may be insufficient or may not be successful in protecting against all cyber incidents. Accordingly, no matter how well designed or implemented the Company's controls are, it will not be able to anticipate all cyber security breaches, and it may not be able to implement effective preventive measures against such security breaches in a timely manner.

For more information on how cybersecurity risk may materially affect the Company's business strategy, results of operations or financial condition, refer to Item 1A, Risk Factors of this Form 10-K.

Item 2. Properties

The Company owns or leases buildings which are used in normal business operations. The Company's corporate headquarters, and that of Bank of Clarke, is located at 2 East Main Street, Berryville, Virginia, 22611. At December 31, 2023, Bank of Clarke operated thirteen full-service branches, one loan production office, and one drive-through only facility in the Virginia communities of Berryville, Winchester, Boyce, Stephens City, Purcellville, Warrenton, Leesburg, Ashburn and Fairfax. The Bank also operated one loan production office in the Maryland community of Frederick. See Note 1 "Nature of Banking Activities and Significant Accounting Policies" and Note 6 "Bank Premises and Equipment, Net" and Note 13 "Leases" in the "Notes to the Consolidated Financial Statements" of this Form 10-K for information with respect to the amounts at which bank premises and equipment are carried and commitments under long-term leases.

All of the Company's properties are well maintained, are in good operating condition and are adequate for the Company's present and anticipated future needs.

Item 3. Legal Proceedings

There are no material pending legal proceedings to which the Company is a party or of which the property of the Company is subject.

Item 4. Mine Safety Disclosures

None.

PART II

Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

The Company's common stock is quoted on the OTC Markets Group's OTCQX Market under the symbol "EFSI." The OTC Markets Group provides information about the common stock to professional market makers who match sellers with buyers. Securities brokers can obtain information from the OTC Markets Group when working with clients. When a client decides to initiate a transaction, the broker will contact one of the stock's market makers. Any over-the-counter market quotations in the Company's common stock reflect inter-dealer prices, without retail mark-up, mark-down or commission and may not necessarily represent actual transactions.

As of March 22, 2024, the Company had approximately 868 shareholders of record.

The Company has historically paid dividends on a quarterly basis. The final determination of the timing, amount and payment of dividends on the Common Stock is at the discretion of the Company's Board of Directors. Some of the factors affecting the payment of dividends on the Company's common stock are operating results, financial condition, capital adequacy, regulatory requirements and shareholders returns.

Issuer Purchases of Equity Securities for the Quarter Ended December 31, 2023

On June 21, 2023, the Corporation renewed the stock repurchase program to repurchase up to 150,000 shares of its common stock prior to June 30, 2024. During 2023, the Company purchased 8,531 shares of its Common Stock under its stock repurchase program at an average price of $35.34.

The following table details the Company's purchases of its common stock during the fourth quarter pursuant to the stock repurchase program discussed above.

	Total Number of Shares Purchased	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plan	Maximum Number of Shares that may Yet Be Purchased Under the Plan
October 1 - October 31, 2023	—	$ —	—	145,059
November 1 - November 30, 2023	—	—	—	145,059
December 1 - December 31, 2023	—	—	—	145,059
	—	$ —	—	145,059

Item 6. Reserved

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operation

The purpose of this discussion is to focus on the important factors affecting the financial condition, results of operations, liquidity and capital resources of Eagle Financial Services, Inc. (the "Company"). This discussion should be read in conjunction with the Company's Consolidated Financial Statements and the Notes to the Consolidated Financial Statements presented in Item 8, Financial Statements and Supplementary Data, of this Form 10-K.

GENERAL

The Company is a bank holding company which owns 100% of the stock of Bank of Clarke (the "Bank"). Accordingly, the results of operations for the Company are dependent upon the operations of the Bank. The Bank conducts a commercial banking business which consists of attracting deposits from the general public and investing those funds in commercial, consumer and real estate loans and corporate, municipal and U.S. government agency securities. The Bank also operates a wealth management division, which provides both a full-service trust department and a separate brokerage area. The Bank's deposits are insured by the Federal Deposit Insurance Corporation to the extent permitted by law. At December 31, 2023, the Company had total assets of $1.83 billion, net loans of $1.45 billion, total deposits of $1.51 billion and shareholders' equity of $108.4 million. The Company's net income was $9.4 million for the year ended December 31, 2023.

The following table presents selected financial data, which was derived from the Company's audited financial statements for the periods indicated.

	As of or for the Years Ended December 31,				
	2023	2022	2021	2020	2019
	(dollars in thousands, except per share amounts)				
Income Statement Data:					
Interest and dividend income	$ 83,128	$ 54,686	$ 42,676	$ 38,908	$ 35,454
Interest expense	32,837	5,473	1,677	3,281	4,239
Net interest income	$ 50,291	$ 49,213	$ 40,999	$ 35,627	$ 31,215
Provision for credit losses	1,649	1,830	1,483	1,457	629
Net interest income after provision for credit losses	$ 48,642	$ 47,383	$ 39,516	$ 34,170	$ 30,586
Noninterest income	14,745	13,345	11,320	8,579	7,759
Net revenue	$ 63,387	$ 60,728	$ 50,836	$ 42,749	$ 38,345
Noninterest expenses	52,754	43,057	38,049	29,441	26,776
Income before income taxes	$ 10,633	$ 17,671	$ 12,787	$ 13,308	$ 11,569
Applicable income taxes	1,276	3,150	1,766	2,136	1,810
Net Income	$ 9,357	$ 14,521	$ 11,021	$ 11,172	$ 9,759
Performance Ratios:					
Return on average assets	0.54%	1.02%	0.90%	1.11%	1.18%
Return on average equity	9.05%	14.06%	10.28%	11.03%	10.60%
Shareholders' equity to assets	5.94%	6.29%	8.46%	9.30%	10.98%
Dividend payout ratio	45.11%	27.58%	34.38%	31.80%	35.21%
Non-performing loans to total loans	0.40%	0.19%	0.28%	0.57%	0.34%
Non-performing assets to total assets	0.34%	0.16%	0.21%	0.47%	0.27%
Share and Per Share Data:					
Net income, basic	$ 2.66	$ 4.17	$ 3.20	$ 3.27	$ 2.84
Net income, diluted	2.66	4.17	3.20	3.27	2.84
Cash dividends declared	1.20	1.15	1.10	1.04	1.00
Book value	30.78	29.15	31.93	30.86	28.08
Market price	30.00	35.95	34.65	29.50	31.05
Average shares outstanding, basic	3,523,547	3,482,368	3,440,080	3,417,543	3,438,410
Average shares outstanding, diluted	3,523,547	3,482,368	3,440,080	3,417,543	3,438,410
Balance Sheet Data:					
Total securities	$ 147,011	$ 158,389	$ 193,370	$ 166,222	$ 166,200
Total loans	1,462,686	1,323,783	985,720	836,334	644,760
Total assets	1,825,597	1,616,717	1,303,038	1,130,152	877,320
Total deposits	1,506,322	1,264,075	1,177,235	1,013,087	771,544
Shareholders' equity	108,379	101,729	110,280	105,074	96,326

MANAGEMENT'S STRATEGY

The Company strives to be an outstanding financial institution in its market by building solid sustainable relationships with: (1) its customers, by providing highly personalized customer service, a network of conveniently placed branches and ATMs, a competitive variety of products/services and courteous, professional employees, (2) its employees, by providing generous benefits, a positive work environment, advancement opportunities and incentives to exceed expectations, (3) its communities, by participating in local concerns, providing monetary support, supporting employee volunteerism and providing employment opportunities, and (4) its shareholders, by providing sound profits and returns, sustainable growth, regular dividends and committing to our local, independent status.

OPERATING STRATEGY

The Bank is a locally owned and managed financial institution. This allows the Bank to be flexible and responsive in the products and services it offers. The Bank grows primarily by lending funds to local residents and businesses at a competitive price that reflects the inherent risk of lending. The Bank attempts to fund these loans through deposits gathered from local residents and businesses. The Bank prices its deposits by comparing alternative sources of funds and selecting the lowest cost available. When deposits are not adequate to fund asset growth, the Bank relies on borrowings, both short and long term. The Bank's primary source of borrowed funds is the Federal Home Loan Bank of Atlanta which offers numerous terms and rate structures to the Bank.

As interest rates change, the Bank attempts to maintain its net interest margin. This is accomplished by changing the price, terms, and mix of its financial assets and liabilities. The Bank also earns fees on services provided through the Bank of Clarke Wealth Management Division, which is the Bank's investment management division that offers both trust services and investment sales, mortgage originations and deposit operations. The Bank also incurs noninterest expenses associated with compensating employees, maintaining and acquiring fixed assets, and purchasing goods and services necessary to support its daily operations.

The Bank has a marketing department which seeks to develop new business. This is accomplished through an ongoing calling program whereby account officers contact existing and potential customers to discuss the products and services offered. The Bank conducts advertising through television commercials, radio ads, newspaper ads, printed materials, electronic materials, billboards, emails, and social media posts.

LENDING POLICIES

Administration and supervision over the lending process is provided by the Bank's Credit Administration Department. The principal risk associated with the Bank's loan portfolio is the creditworthiness of its borrowers. In an effort to manage this risk, the Bank's policy gives loan amount approval limits to individual loan officers based on their position and level of experience. Credit risk is increased or decreased, depending on the type of loan and prevailing economic conditions. In consideration of the different types of loans in the portfolio, the risk associated with real estate mortgage loans, commercial loans and consumer loans varies based on employment levels, consumer confidence, fluctuations in the value of real estate and other conditions that affect the ability of borrowers to repay debt.

The Company has written policies and procedures to help manage credit risk. The Company utilizes a loan review process that includes formulation of portfolio management strategy, guidelines for underwriting standards and risk assessment, procedures for ongoing identification and management of credit deterioration, and regular portfolio reviews to establish loss exposure and to ascertain compliance with the Company's policies.

The Bank uses a tiered approach to approve credit requests consisting of individual lending authorities, joint approval of Co-Approval officers (Executive, Regional Credit Officer, Small Business Credit Officer), and a director loan committee. Lending limits for individuals are set by the Board of Directors and are determined by loan purpose, collateral type, and internal risk rating of the borrower. The highest individual authority (Executive) is assigned to the Bank's President/ Chief Executive Officer, Chief Banking Officer and Chief Credit Officer (approval authority only). Two Executive officers may combine their authority to approve loan requests to borrowers with credit exposure up to $10.0 million on a secured basis and $6.0 million unsecured. Three Executive officers may combine to approve loan requests to borrowers with credit exposure up to $15.0 million on a secured basis and $9.0 million unsecured. Consumer Central Lenders can co-approve consumer, home equity lines of credit and home equity loan requests up to their stated authorities. Officers in Categories A through F have lesser authorities and with approval of an Executive officer may extend loans to borrowers with exposure of $5.0 million on a secured basis and $3.0 million unsecured. Officers in Categories A through F can also utilize the co-approval of the Regional and Small Business Credit Officers to extend loans with exposures up to $2.5 million and $1.5 million respectively on a secured basis, and up to $1 million and $750 thousand respectively on an unsecured basis. Loans exceeding $15.0 million and up to the Bank's legal lending limit can be approved by the Director Loan Committee consisting of four directors (three directors

constituting a quorum). The Director's Loan Committee also reviews and approves changes to the Bank's Loan Policy as presented by management. The following sections discuss the major loan categories within the total loan portfolio:

One-to-Four-Family Residential Real Estate Lending

Residential lending activity may be generated by the Bank's loan officer solicitations, referrals by real estate professionals, and existing or new bank customers. Loan applications are taken by a Bank loan officer. As part of the application process, information is gathered concerning income, employment and credit history of the applicant. The valuation of residential collateral is provided by independent fee appraisers who have been approved by the Bank's Directors Loan Committee. In connection with residential real estate loans, the Bank requires title insurance, hazard insurance and, if applicable, flood insurance. In addition to traditional residential mortgage loans secured by a first or junior lien on the property, the Bank offers home equity lines of credit.

Commercial Real Estate Lending

Commercial real estate loans are secured by various types of commercial real estate in the Bank's market area, including multi-family residential buildings, commercial buildings and offices, small shopping centers and churches. Commercial real estate loan originations are obtained through broker referrals, direct solicitation of developers and continued business from customers. In its underwriting of commercial real estate, the Bank's loan to original appraised value ratio is generally 80% or less. Commercial real estate lending entails significant additional risk as compared with residential mortgage lending. Commercial real estate loans typically involve larger loan balances concentrated with single borrowers or groups of related borrowers. Additionally, the repayment of loans secured by income producing properties is typically dependent on the successful operation of a business or a real estate project and thus may be subject, to a greater extent, to adverse conditions in the real estate market or the economy, in general. The Bank's commercial real estate loan underwriting criteria require an examination of debt service coverage ratios, the borrower's creditworthiness, prior credit history and reputation, and the Bank typically requires personal guarantees or endorsements of the borrowers' principal owners.

Construction and Land Development Lending

The Bank makes local construction loans and land acquisition and development loans. The construction loans are secured by residential houses under construction and the underlying land for which the loan was obtained. The average life of most construction loans is less than one year and the Bank offers both fixed and variable rate interest structures. The interest rate structure offered to customers depends on the total amount of these loans outstanding and the impact of the interest rate structure on the Bank's overall interest rate risk. There are two characteristics of construction lending which impact its overall risk as compared to residential mortgage lending. First, there is more concentration risk due to the extension of a large loan balance through several lines of credit to a single developer or contractor. Second, there is more collateral risk due to the fact that loan funds are provided to the borrower based upon the estimated value of the collateral after completion. This could cause an inaccurate estimate of the amount needed to complete construction or an excessive loan-to-value ratio. To mitigate the risks associated with construction lending, the Bank generally limits loan amounts to 80% of the estimated appraised value of the finished property. The Bank also obtains a first lien on the property as security for its construction loans and typically requires personal guarantees from the borrower's principal owners. Finally, the Bank performs inspections of the construction projects to ensure that the percentage of construction completed correlates with the amount of draws on the construction line of credit.

Commercial and Industrial Lending

Commercial business loans generally have more risk than residential mortgage loans but have higher yields. To manage these risks, the Bank generally obtains appropriate collateral and personal guarantees from the borrower's principal owners and monitors the financial condition of its business borrowers. Residential mortgage loans generally are made on the basis of the borrower's ability to make repayment from employment and other income and are secured by real estate whose value tends to be readily ascertainable. In contrast, commercial business loans typically are made on the basis of the borrower's ability to make repayment from cash flow from its business and are secured by business assets, such as, accounts receivable, equipment and inventory. As a result, the availability of funds for the repayment of commercial business loans is substantially dependent on the success of the business itself. Furthermore, the collateral for commercial business loans may depreciate over time and generally cannot be appraised with as much precision as residential real estate. Refer to the Marine Lending section below for discussion of additional commercial and industrial lending.

Consumer Lending

The Bank offers various secured and unsecured consumer loans, which include personal installment loans, personal lines of credit, automobile loans, and credit card loans. The Bank generally originates its consumer loans within its geographic market area and these loans are largely made to customers with whom the Bank has an existing relationship. Consumer loans

generally entail greater risk than residential mortgage loans, particularly in the case of consumer loans which are unsecured or secured by rapidly depreciable assets such as automobiles. In such cases, any repossessed collateral on a defaulted consumer loan may not provide an adequate source of repayment of the outstanding loan balance as a result of the greater likelihood of damage, loss or depreciation. Consumer loan collections are dependent on the borrower's continuing financial stability, and thus are more likely to be adversely affected by job loss, divorce, illness or personal bankruptcy. Furthermore, the application of various federal and state laws, including federal and state bankruptcy and insolvency laws, may limit the amount which can be recovered on such loans.

The underwriting standards employed by the Bank for consumer loans include a determination of the applicant's payment history on other debts and an assessment of ability to meet existing obligations and payments on the proposed loan. The stability of the applicant's monthly income may be determined by verification of gross monthly income from primary employment, and from any verifiable secondary income. Although creditworthiness of the applicant is the primary consideration, the underwriting process also includes an analysis of the value of the security in relation to the proposed loan amount.

Marine Lending

Through August 22, 2023, the Bank's marine lending unit included originated retail loans, classified as commercial and industrial loans or consumer loans, depending on the borrower, and dealer floor plan loans, classified as commercial and industrial loans. The Company's relationships were limited to well established dealers of global premium brand manufacturers with the top three manufacturer customers in business between 30 and 100 years. Retail loans were generally limited to premium manufacturers with established relationships with the Company which have a vested interest in the secondary market pricing of their respective brand due to the limited inventory available for resale. Consequently, while not contractually committed, manufacturers will often support secondary resale values which can have the effect of reducing losses from non-performing retail marine loans. Retail borrowers generally have very high credit scores, substantial down payments, substantial net worth, personal liquidity, and excess cash flow. See additional discussion under the heading "Business Segments" as well as Note 27 to the Consolidated Financial Statements presented in Item 8, Financial Statements and Supplementary Data, of this Form 10-K.

CRITICAL ACCOUNTING POLICIES

The financial statements of the Company are prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP"). The financial information contained within these statements is, to a significant extent, based on measurements of the financial effects of transactions and events that have already occurred. A variety of factors could affect the ultimate value that is obtained when earning income, recognizing an expense, recovering an asset or relieving a liability. In addition, GAAP itself may change from one previously acceptable method to another method. Although the economics of the transactions would be the same, the timing of events that would impact the transactions could change.

Allowance for Credit Losses on Loans

The Company establishes the allowance for credit losses through charges to earnings in the form of a provision for credit losses. Loan losses are charged against the allowance for credit losses for the difference between the carrying value of the loan and the estimated net realizable value or fair value of the collateral, if collateral dependent, when management believes that the collectability of the principal is unlikely. Subsequent recoveries, if any, are credited to the allowance. The allowance represents management's current estimate of expected credit losses over the contractual term of loans held for investment, and is recorded at an amount that, in management's judgment, reduces the recorded investment in loans to the net amount expected to be collected. Management's judgment in determining the level of the allowance is based on evaluations of historical loan losses, current conditions and reasonable and supportable forecasts relevant to the collectability of loans. The measurement of the allowance for credit losses is based in part on forecasts of unemployment, inflation, as well as the consumer price index, and may also consider other factors, which we believe to be indicative of risk factors related to collectability. Management also assesses the risk of credit losses arising from changes in economic conditions; the nature and volume of the loan portfolio; the volume and severity of delinquencies and adversely classified loan balances; lending policy and procedures; credit administration and lending staff; loan review; concentrations of credit and the value of underlying collateral in determining the recorded balance of the allowance for credit losses. This evaluation is inherently subjective because it requires estimates that are susceptible to significant revision as more information becomes available. In evaluating the level of the allowance, we consider a range of possible assumptions and outcomes related to the various factors identified above. Note 1 to the Consolidated Financial Statements presented in Item 8, Financial Statements and Supplementary Data, of the 2023 Form 10-K, provides additional information concerning the determination of the allowance for credit losses on loans.

FORWARD LOOKING STATEMENTS

The Company makes forward looking statements in this report that are subject to risks and uncertainties. These forward looking statements include statements regarding our profitability, liquidity, allowance for loan losses, interest rate sensitivity, market risk, growth strategy, and financial and other goals. The words “believes,” “expects,” “may,” “will,” “should,” “projects,” “contemplates,” “anticipates,” “forecasts,” “intends,” or other similar words or terms are intended to identify forward looking statements. These forward looking statements are subject to significant uncertainties because they are based upon or are affected by factors including:

- difficult market conditions in our industry;
- effects of soundness of other financial institutions;
- potential impact on us of existing and future legislation and regulations;
- the ability to successfully manage growth or implement growth strategies if the Bank is unable to identify attractive markets, locations or opportunities to expand in the future, expand into new markets, or successfully implement new product lines;
- competition with other banks and financial institutions, and companies outside of the banking industry, including those companies that have substantially greater access to capital and other resources;
- the successful management of interest rate risk;
- risks inherent in making loans such as repayment risks and fluctuating collateral values;
- changes in general economic and business conditions in the market area;
- reliance on the management team, including the ability to attract and retain key personnel;
- changes in interest rates and interest rate policies;
- maintaining capital levels adequate to support growth;
- maintaining cost controls and asset qualities as new branches are opened or acquired;
- demand, development and acceptance of new products and services;
- deposit flows;
- problems with technology utilized by the Bank;
- changing trends in customer profiles and behavior;
- geopolitical conditions, including acts or threats of terrorism, international hostilities, or actions taken by the U.S. or other governments in response to acts or threats of terrorism and/or military conflicts, which could impact business and economic conditions in the U.S. and abroad;
- the Company’s potential exposure to fraud, negligence, computer theft, and cyber-crime
- changes in accounting policies and banking and other laws and regulations; and
- other factors described in Item 1A., “Risk Factors,” above.

Because of these uncertainties, actual future results may be materially different from the results indicated by these forward looking statements. In addition, past results of operations do not necessarily indicate future results.

RESULTS OF OPERATIONS

Net Income

Net income for 2023 was $9.4 million, a decrease of $5.2 million or 35.56% from 2022's net income of $14.5 million. Basic and diluted earnings per share were $2.66 and $4.17 for 2023 and 2022, respectively.

Return on average assets ("ROA") measures how efficiently the Company uses its assets to produce net income. Some issues reflected within this efficiency include the Company's asset mix, funding sources, pricing, fee generation, and cost control. The ROA of the Company, on an annualized basis, was 0.54% and 1.02% for 2023 and 2022, respectively.

Return on average equity ("ROE") measures the utilization of shareholders' equity in generating net income. This measurement is affected by the same factors as ROA with consideration to how much of the Company's assets are funded by the shareholders. The ROE for the Company was 9.05% and 14.06% for 2023 and 2022, respectively.

Net Interest Income

Net interest income, the difference between total interest income and total interest expense, is the Company's primary source of earnings. Net interest income was $50.3 million for 2023 and $49.2 million for 2022, which represents an increase of $1.1 million or 2.19%. Net interest income is derived from the volume of earning assets and the rates earned on those assets as compared to the cost of funds. Total interest income was $83.1 million for 2023 and $54.7 million for 2022, which represents an increase of $28.4 million or 52.01% for 2023. Total interest expense was $32.8 million for 2023 and $5.5 million for 2022, which represents an increase of $27.4 million or 499.98% in 2023. The increase in total interest income, total interest expense and net interest income during 2023 was driven by the growth in interest-earning assets, interest-bearing liabilities and the rising interest rate environment. Refer to the table titled "Volume and Rate Analysis" for further detail.

The table titled "Average Balances, Income and Expenses, Yields and Rates" displays the composition of interest earnings assets and interest bearing liabilities and their respective yields and rates for the years ended December 31, 2023 and 2022.

The net interest margin was 2.96% for 2023 and 3.68% for 2022. The net interest margin is calculated by dividing tax-equivalent net interest income by total average earnings assets. Tax-equivalent net interest income is calculated by adding the tax benefit on certain securities and loans, whose interest is tax-exempt, to total interest income then subtracting total interest expense. The tax rate used to calculate the tax benefit was the federal statutory rate of 21%. The table titled "Tax-Equivalent Net Interest Income" reconciles net interest income to tax-equivalent net interest income, which is not a measurement under GAAP, for the years ended December 31, 2023 and 2022.

Net interest income and net interest margin may experience some decline due to additional deposit pricing pressure as interest rates continue to increase or remain at the current level and increased competition for new deposits is experienced. These combined also could result in the Company having to borrow wholesale funding to fund asset growth which is more expensive than deposits.

Average Balances, Income and Expenses, Yields and Rates
(dollars in thousands)

	Years Ended					
	December 31, 2023			December 31, 2022		
	Average Balance	Interest Income/ Expense	Average Rate	Average Balance	Interest Income/ Expense	Average Rate
Assets:						
Securities:						
Taxable	$ 150,187	$ 3,663	2.44 %	$ 172,501	$ 3,401	1.97 %
Tax-Exempt (1)	507	21	4.13 %	8,305	280	3.37 %
Total Securities	$ 150,694	$ 3,684	2.45 %	$ 180,806	$ 3,681	2.04 %
Loans: (2)						
Taxable	1,418,916	75,127	5.29 %	1,121,429	50,509	4.50 %
Non-accrual	3,458	—	—%	2,350	—	—%
Tax-Exempt (1)	10,106	497	4.91 %	5,671	218	3.85 %
Total Loans	$ 1,432,480	$ 75,624	5.28 %	$ 1,129,450	$ 50,727	4.49 %
Federal funds sold and interest-bearing deposits in other banks	118,789	3,928	3.31 %	32,562	382	1.17 %
Total earning assets	$ 1,701,963	$ 83,236	4.89 %	$ 1,342,818	$ 54,790	4.08 %
Allowance for loan losses	(14,176)			(9,852)		
Total non-earning assets	59,388			93,289		
Total assets	$ 1,747,175			$ 1,426,255		
Liabilities and Shareholders' Equity:						
Interest-bearing deposits:						
NOW accounts	$ 244,277	$ 5,238	2.14 %	$ 173,843	$ 663	0.38 %
Money market accounts	257,496	4,491	1.74 %	270,725	1,155	0.43 %
Savings accounts	151,556	185	0.12 %	179,709	130	0.07 %
Time deposits:						
$250,000 and more	116,077	4,756	4.10 %	62,757	560	0.89 %
Less than $250,000	219,809	8,960	4.08 %	62,907	433	0.69 %
Total interest-bearing deposits	$ 989,215	$ 23,630	2.39 %	$ 749,941	$ 2,941	0.39 %
Federal funds purchased	2,801	70	2.50 %	7,882	170	2.16 %
Federal Home Loan Bank advances	162,548	7,720	4.75 %	39,589	1,295	3.27 %
Subordinated debt	29,408	1,417	4.82 %	22,193	1,067	4.81 %
Total interest-bearing liabilities	$ 1,183,972	$ 32,837	2.77 %	$ 819,605	$ 5,473	0.67 %
Noninterest-bearing liabilities:						
Demand deposits	442,539			485,061		
Other Liabilities	17,328			18,293		
Total liabilities	$ 1,643,839			$ 1,322,959		
Shareholders' equity	103,336			103,296		
Total liabilities and shareholders' equity	$ 1,747,175			$ 1,426,255		
Net interest income		$ 50,399			$ 49,317	
Net interest spread			2.12 %			3.42 %
Interest expense as a percent of average earning assets			1.93 %			0.41 %
Net interest margin			2.96 %			3.68 %

(1) Income and yields are reported on a tax-equivalent basis using the federal tax rate of 21%.
(2) Interest and yields on loans include the amortization/accretion of origination costs/fees as well as any purchase premiums or discounts.

Tax-Equivalent Net Interest Income
(dollars in thousands)

	Twelve Months Ended December 31,	
	2023	2022
	(in thousands)	
GAAP Financial Measurements:		
Interest Income - Loans	$ 75,520	$ 50,682
Interest Income - Securities and Other Interest-Earnings Assets	7,608	4,004
Interest Expense - Deposits	23,630	2,941
Interest Expense - Other Borrowings	9,207	2,532
Total Net Interest Income	$ 50,291	$ 49,213
Non-GAAP Financial Measurements:		
Add: Tax Benefit on Tax-Exempt Interest Income - Loans (1)	$ 104	$ 45
Add: Tax Benefit on Tax-Exempt Interest Income - Securities (1)	4	59
Total Tax Benefit on Tax-Exempt Interest Income	$ 108	$ 104
Tax-Equivalent Net Interest Income	$ 50,399	$ 49,317

(1) Tax benefit was calculated using the federal statutory tax rate of 21%.

The tax-equivalent yield on earning assets increased 81 basis points from 2022 to 2023. The tax-equivalent yield on securities increased 41 basis points from 2022 to 2023. The tax-equivalent yield on loans increased 79 basis points from 2022 to 2023. The increase in the tax-equivalent yield on earning assets resulted mostly from the increase in the tax-equivalent yield on loans. The increase in the tax-equivalent yield on loans as compared to the corresponding period in the prior year was due to a combination of increase of volume of loans and the rising interest rate environment.

The average rate on interest-bearing liabilities increased 210 basis points from 2022 to 2023. The average rate on total interest-bearing deposits increased 200 basis points from 2022 to 2023. The Federal Reserve's interest rate increases beginning early 2022 and continuing into 2023 heightened interest rates paid on deposit accounts. In general, deposit pricing is done in response to monetary policy actions and yield curve changes. Local competition for funds also affects the cost of time deposits, which are primarily comprised of certificates of deposit. The Company prefers to rely most heavily on non-maturity deposits when possible, which include NOW accounts, money market accounts, and savings accounts. The average balance of non-maturity interest-bearing deposits increased $29.1 million or 4.65% from $624.3 million during 2022 to $653.3 million in 2023. The Company also actively pursued time deposits during 2023 adding $210.2 million, or 28.03%, in average balances, primarily in amounts less than $250,000. These time deposits were obtained through pricing and, to a lesser extent, entering into a $30.0 million brokered account during the first quarter. The cost of total time deposits increased to 4.08% during 2023 from 0.79% during 2022. The cost of interest-bearing liabilities was also higher during 2023 due increased usage of FHLB advances, which had a 148 basis point, or 45.3%, increase in cost combined with a $123.0 million increase in average balance.

The table titled “Volume and Rate Analysis” provides information about the effect of changes in financial assets and liabilities and changes in rates on net interest income.

Tax-equivalent net interest income increased $1.1 million during 2023. The net increase in tax-equivalent net interest income during 2023 is comprised of an increase due to volume of $6.7 million and a decrease due to rate of $5.6 million. The increase in tax-equivalent net interest income during 2023 was largely affected by the increased volume of taxable loans, as well as increases in rates earned from interest-earning assets. This increase was mostly offset by the increased volume in borrowing and time deposits and increases in rates paid on interest bearing liabilities.

Volume and Rate Analysis (Tax-Equivalent Basis)
(dollars in thousands)

	2023 vs 2022 Increase (Decrease) Due to Changes in:		
	Volume	**Rate**	**Total**
Earning Assets:			
Securities:			
Taxable	$ (310)	$ 572	$ 262
Tax-exempt	(342)	83	(259)
Loans:			
Taxable	14,814	9,804	24,618
Tax-exempt	205	74	279
Federal funds sold and interest-bearing deposits in other banks	2,097	1,449	3,546
Total earning assets	$ 16,464	$ 11,982	$ 28,446
Interest-Bearing Liabilities:			
NOW accounts	$ 368	$ 4,207	$ 4,575
Money market accounts	(54)	3,390	3,336
Savings accounts	(15)	70	55
Time deposits:			
$250,000 and more	800	3,396	4,196
Less than $250,000	2,871	5,656	8,527
Total interest-bearing deposits	$ 3,970	$ 16,719	$ 20,689
Federal funds purchased	(132)	32	$ (100)
Federal Home Loan Bank advances	5,608	817	6,425
Subordinated debt	348	2	350
Total interest-bearing liabilities	$ 9,794	$ 17,570	$ 27,364
Change in net interest income	$ 6,670	$ (5,588)	$ 1,082

Provision for Credit Losses

The provision for credit losses is based upon management's estimate of the amount required to maintain an adequate allowance for credit losses as discussed within the Critical Accounting Policies section above and Note 1 to the Consolidated Financial Statements presented in Item 8, Financial Statements and Supplementary Data. The provision for credit losses was $1.6 million for 2023 and $1.8 million for 2022. The amount of provision for credit losses on loans is affected by several factors including the growth rate of loans, net charge-offs (recoveries), and the estimated amount of expected losses within the loan portfolio.The amount of provision for credit losses during each period reflects the results of the Company's analysis used to determine the adequacy of the allowance for credit losses. The provision for credit losses in 2023 reflects loan growth during the year, largely in the residential and commercial real estate portfolios. Net charge-offs during 2023 totaled $443 thousand. The provision for loan losses in 2022 reflects loan growth in the portfolio partially offset by net recoveries of $601 thousand during 2022. The Company is committed to maintaining an allowance that it believes will adequately absorb the current expected losses in the loan portfolio. This commitment is more fully discussed in the "Asset Quality" section.

Noninterest Income

Total noninterest income was $14.7 million and $13.3 million during 2023 and 2022, respectively. This represents an increase of $1.4 million or 10.49% for 2023. Management reviews the activities which generate noninterest income on an ongoing basis.

The following table provides the components of noninterest income for the twelve months ended December 31, 2023 and 2022, which are included within the respective Consolidated Statements of Income headings. The following paragraphs provide information about activities which are included within the respective Consolidated Statements of Income headings. Variances that the Company believes require explanation are discussed below the table.

	December 31,			
(dollars in thousands)	**2023**	**2022**	**$ Change**	**% Change**
Wealth management fees	$ 4,926	$ 4,149	$ 777	18.73 %
Service charges on deposit accounts	1,810	1,618	192	11.87 %
Other service charges and fees	4,413	3,943	470	11.92 %
Gain on the sale of marine finance assets	435	—	435	NM
Gain (loss) on the sale and disposal of bank premises and equipment	14	(11)	25	(227.27)%
(Loss) on sale of securities	—	(737)	737	(100.00)%
Gain on sale of loans	1,428	1,875	(447)	(23.84)%
Bank owned life insurance income	713	626	87	13.90 %
Other operating income	1,006	1,882	(876)	(46.55)%
Total noninterest income	$ 14,745	$ 13,345	$ 1,400	10.49 %

NM - Not Meaningful

Wealth management fees increased from 2022 to 2023. Wealth management fee income is comprised of income from fiduciary activities as well as commissions from the sale of non-deposit investment products. The amount of income from wealth management fees is determined by the number of active accounts and total assets under management. New business efforts in addition to fee increases and one-time fees for estates and other services have contributed to the year over year increase in revenue.

Services charges on deposit accounts increased when comparing the year ended December 31, 2023 to 2022. This increase is mainly due to increases in overdraft charges. Overdraft charges can fluctuate based on changes in customer activity and number of accounts.

Other service charges and fees increased during the twelve months ended December 31, 2023 compared to the same period in 2022. This increase can be attributed to increased ATM fee income. ATM fee income can fluctuate based on ATM usage by non-customers.

Gain on the sale of marine finance assets was $435 thousand for the year ended December 31, 2023. On August 23, 2023, the Company completed the sale of certain marine finance division assets. Refer to additional discussion of marine lending under the heading "Lending Policies" in Item 7 above and in Notes 1 and 27 to the Consolidated Financial Statements.

The Company recorded a net loss of $737 thousand on its sale $15.4 million in available for sale securities during 2022. There were no sales of available for sale securities during the year ended December 31, 2023.

During 2023, the Company sold $32.1 million in mortgage loans on the secondary market, $51.7 million of loans from the commercial and consumer loan portfolios and $8.0 million in Small Business Association ("SBA") loans. During 2022, the Company sold $12.2 million in mortgage loans on the secondary market, $155.0 million of loans from the commercial and consumer loan portfolios and $2.8 million in SBA loans. These loan sales resulted in gains of $1.4 million and $1.9 million during the years ended December 31, 2023 and 2022, respectively.

Bank owned life insurance ("BOLI") fee income increased during 2023 when compared to 2022 as a result of an investment of $5 million into BOLI by the Company during the fourth quarter of 2023.

Other operating income decreased during 2023. The fluctuation from 2022 to 2023 is mostly attributed to cash distributions received from investments in Small Business Investment Companies during 2022 that were not received during 2023 and loan swap fee income. The decrease in loan swap fee income was attributable to less loan swap fee income recognized during 2023 compared to 2022. Loan swap agreements with initial notional balances of $20.9 million and $21.2 million were entered into during the years ended December 31, 2023 and 2022, respectively. In 2022, the Bank also earned a fee for its participation in a loan swap agreement with an outside lead bank.

Noninterest Expenses

Total noninterest expenses were $52.8 million and $43.1 million during 2023 and 2022, respectively. This represents an increase of $9.7 million or 22.52% during 2023.

The following table provides the components of noninterest expense for the twelve months ended December 31, 2023 and 2022, which are included within the respective Consolidated Statements of Income headings. The following paragraphs provide information about activities which are included within the respective Consolidated Statements of Income headings. Variances that the Company believes require explanation are discussed below the table.

	December 31,			
(dollars in thousands)	**2023**	**2022**	**$ Change**	**% Change**
Salaries and employee benefits	$ 30,306	$ 25,730	$ 4,576	17.78 %
Occupancy expenses	2,202	2,068	134	6.48 %
Equipment expenses	1,299	1,121	178	15.88 %
Advertising and marketing expenses	1,157	770	387	50.26 %
Stationery and supplies	191	199	(8)	(4.02)%
ATM network fees	1,563	1,313	250	19.04 %
Other real estate owned expense	5	34	(29)	(85.29)%
(Gain) on other real estate owned	(7)	—	(7)	NM
FDIC assessment	1,585	614	971	158.14 %
Computer software expense	1,360	960	400	41.67 %
Bank franchise tax	1,255	886	369	41.65 %
Professional fees	2,540	2,019	521	25.80 %
Data processing fees	1,935	1,779	156	8.77 %
Other operating expenses	7,363	5,564	1,799	32.33 %
Total noninterest expenses	$ 52,754	$ 43,057	$ 9,697	22.52 %

NM - Not Meaningful

The Company's growth has had an impact on noninterest expenses. Total assets have grown by $208.9 million or 12.9% from December 31, 2022 to December 31, 2023. This growth has required investments to be made in the Company's infrastructure, causing increases in salaries and employee benefits, occupancy expenses, equipment expenses, advertising and marketing expenses, computer software expense, and other operating expenses. In addition, increases in asset size and capital levels have impacted both the FDIC assessment and bank franchise tax amounts.

Salaries and employee benefits expense increased during 2023. Annual pay increases, staffing changes, increasing insurance costs and enhanced employee incentive plans have attributed to these increases. The Company had 241 full-time equivalent employees (FTEs) at both December 31, 2022 and December 31, 2023. As part of the sale of the marine finance assets during the third quarter, the Company reduced its workforce associated with the marine lending division as it expects to cease accepting new marine lending business. While additional expenses were incurred at the time of the sale, the workforce reduction will have a positive impact on salaries and employee benefits expense going forward.

Advertising and marketing expenses increased during 2023 reflecting the Company's continued marketing and branding campaigns, including its recognition of receiving a *Great Place to Work® certified.* designation. In addition expenses in 2023 were higher due to the rebranding that occurred in early 2023.

ATM network fees increased during the year ended December 31, 2023 compared to the year ended December 31, 2022. This is mainly due to fluctuations in customer usage.

FDIC assessment and bank franchise taxes both increased in 2023 reflecting growth in the Company. The increase in FDIC assessment was also due to a two basis point increase in the assessment rate charged by the FDIC, which was applied to all financial institutions.

Computer software expense increased during 2023 over 2022, largely due to investments in software platforms to improve operating efficiencies and customer experience with bank products and services.

Professional fees increased during 2023. There are several factors that contributed to the increase of professional fees during 2023. Expenses related to the ESOP termination and the new stock incentive plan caused increases to legal expense, while the outsourcing of a portion of the internal audit function related to FDICIA testing caused increases to audit expenses.

Other operating expenses increased during 2023. This increase is due primarily to a change in control agreement related to the workforce reduction described above and increased loan related expenses due to a higher loan origination volume. Also reflected in the year-over-year increase were a greater amount of charitable contributions and costs for education, training and travel.

The efficiency ratio of the Company was 81.55% and 67.90% for 2023 and 2022, respectively. The efficiency ratio is calculated by dividing total noninterest expenses by the sum of tax-equivalent net interest income and total noninterest income, excluding gains and losses on investment portfolio sales and other gains/losses from OREO, repossessed assets, sale or disposals of bank assets, etc. The tax rate utilized is 21%. The Company calculates and reviews this ratio as a means of evaluating operational efficiency. A reconciliation of tax-equivalent net interest income, which is not a measurement under GAAP, to net interest income is presented within the *Net Interest Income* section above.

The calculation of the efficiency ratio for the twelve months ended December 31, 2023 and 2022 was as follows:

	December 31,	
	2023	**2022**
	(in thousands)	
Summary of Operating Results:		
Noninterest expenses	$ 52,754	$ 43,057
Less: (Gain) on other real estate owned	(7)	—
Adjusted noninterest expenses	$ 52,761	$ 43,057
Net interest income	$ 50,291	$ 49,213
Noninterest income	$ 14,745	$ 13,345
Less: (Loss) on sales of securities	—	(737)
Less: Gain on the sale of marine finance assets	435	—
Less: Gain (loss) on the sale and disposal of premises and equipment	14	(11)
Adjusted noninterest income	$ 14,296	$ 14,093
Tax equivalent adjustment (1)	108	104
Total net interest income and noninterest income, adjusted	$ 64,695	$ 63,410
Efficiency ratio	81.55 %	67.90 %

(1) Includes tax-equivalent adjustments on loans and securities using the federal statutory tax rate of 21%.

Income Taxes

Income tax expense was $1.3 million and $3.2 million for the years ended December 31, 2023 and 2022, respectively. These amounts correspond to an effective tax rate of 12.00% and 17.83% for 2023 and 2022, respectively. The effective tax rate is below the statutory rate of 21%, due primarily to tax credits on qualified affordable housing project investments as discussed in Note 25 to the Consolidated Financial Statements as well as qualified rehabilitation credits. During 2023, one of the Company's rehabilitation tax credit investments was finalized and the total amount of credits to be received was determined and certified. The effective tax rate is also impacted by tax-exempt income on investment securities and loans. Note 9 to the Consolidated Financial Statements provides a reconciliation between income tax expense computed using the federal statutory income tax rate and the Company's actual income tax expense during 2023 and 2022.

Business Segments

The Company has three reportable operating segments: community banking, marine lending and wealth management. Revenue from community banking operations consist primarily of net interest income related to investments in non-marine loans and securities and outstanding deposits and borrowings, fees earned on deposit accounts and debit card interchange activity. Revenue from marine lending operations consist primarily of net interest income related to commercial and consumer marine loans and gains on sales of loans. The wealth management division's net revenues are comprised primarily of income from offering wealth management services and insurance products through third-party service providers.

On August 23, 2023, the Company completed a sale of specific assets from its marine lending segment. As part of the sale, the Company sold its interest in marine vessel floor plan loans totaling $52.8 million, its rights to service loans that had been sold to secondary market investors prior to the date of sale (valued at $595 thousand on balance sheet prior to sale), and other assets that were not individually significant. The Company received total consideration, net of selling expenses, of $53.5 million and recognized a gain of $435 thousand. The assets sold as well as their related revenues and contribution to earnings did not constitute a significant portion of the Company's assets or operating results for the year ended December 31, 2023. As part of the sale, the Company reduced its workforce associated with the marine lending division, as it expects to cease accepting new marine lending business. Subsequent to the sale of these assets, the Company retained ownership of approximately $260.5 million of marine vessel retail loans which continue to constitute a significant portion of the Company's assets, revenues, and earnings. At present, the Company expects to hold the retained outstanding loans until they are ultimately repaid.

Financial information for the parent company is included in the "All Other" category. The parent company's operating results are comprised primarily of interest expense associated with subordinated debt. Refer to Notes 1 and 27 of the Consolidated Financial Statements included in Item 8 of this Annual Report on Form 10-K for additional information.

The following table provides income and asset information as of and for the twelve months ended December 31, 2023 and 2022, which are included within the Consolidated Balance Sheets and Consolidated Statements of Income. Variances that the Company believes require explanation are discussed below the table.

	Twelve Months Ended December 31, 2023 (in thousands)					
	Community Banking	Marine Lending	Wealth Management	All Other	Eliminations	Consolidated
Interest Income	$ 67,990	$ 15,138	$ —	$ —	$ —	$ 83,128
Interest Expense	25,850	5,570	—	1,417	—	32,837
Net Interest Income (Expense)	42,140	9,568	—	(1,417)	—	50,291
Gain on sales of loans	1,117	311	—	—	—	1,428
Other noninterest income	7,313	1,078	4,926	—	—	13,317
Net Revenue	50,570	10,957	4,926	(1,417)	—	65,036
Provision for credit losses	2,051	(402)	—	—	—	1,649
Noninterest expense	44,479	5,106	2,646	523	—	52,754
Income before taxes	4,040	6,253	2,280	(1,940)	—	10,633
Income tax expense (benefit)	(103)	1,313	479	(413)	—	1,276
Net Income	$ 4,143	$ 4,940	$ 1,801	$ (1,527)	$ —	$ 9,357
Other data:						
Capital expenditures	$ 1,035	$ 36	$ —	$ —	$ —	$ 1,071
Depreciation and amortization	1,573	224	126	67	—	1,990

	Twelve Months Ended December 31, 2022 (in thousands)					
	Community Banking	Marine Lending	Wealth Management	All Other	Eliminations	Consolidated
Interest Income	$ 47,554	$ 7,132	$ —	$ —	$ —	$ 54,686
Interest Expense	4,026	380	—	1,067	—	5,473
Net Interest Income (Expense)	43,528	6,752	—	(1,067)	—	49,213
Gain on sales of loans	478	1,397	—	—	—	1,875
Other noninterest income	7,222	99	4,149	—	—	11,470
Net Revenue	51,228	8,248	4,149	(1,067)	—	62,558
Provision for credit losses	1,059	771	—	—	—	1,830
Noninterest expense	36,401	3,695	2,590	371	—	43,057
Income before taxes	13,768	3,782	1,559	(1,438)	—	17,671
Income tax expense (benefit)	2,343	794	328	(315)	—	3,150
Net Income	$ 11,425	$ 2,988	$ 1,231	$ (1,123)	$ —	$ 14,521
Other data:						
Capital expenditures	$ 829	$ 9	$ —	$ —	$ —	$ 838
Depreciation and amortization	1,499	236	124	51	—	1,910

	Community Banking	Marine Lending	Wealth Management	All Other	Eliminations	Consolidated
Total assets at December 31, 2023	$ 1,562,600	$ 261,011	$ 1,080	$ 906	$ —	$ 1,825,597
Total assets at December 31, 2022	1,377,461	237,595	1,206	455	—	1,616,717

The decrease in community banking segment net income for the year ended December 31, 2023 compared to the year ended December 31, 2022 was due to impact of the rising interest rate environment as the cost of interest-bearing liabilities outpaced income earned on interest-earning assets along with an increase in noninterest expenses. Interest expense increased by $21.8 million, or 542.1%, compared to an increase in interest income of $20.4 million, or 43.0%. The year-over-year decrease was also impacted by the increase in noninterest expense, partially offset by an increase in noninterest income and a decrease in income tax expense. The increase in noninterest expense is largely due to the Bank's growth and an increase in the allocated cost of funding. This growth has required investments to be made in the Bank's infrastructure, causing increases in salaries and employee benefits, occupancy expenses, equipment expenses, advertising and marketing expenses, computer software expenses, and other operating expenses. In addition, increases in asset size and capital levels have impacted both the FDIC assessment and bank franchise tax amounts.

The increase in marine lending segment net income for the year ended December 31, 2023 compared to the year ended December 31, 2022 was primarily due to higher interest income resulting from loan growth, as well as the effects of rising interest rates on asset yields. The average balance of marine loans increased $108.1 million, or 65.18% during 2023. The increase in interest income was partially offset by higher interest expense and salaries and employee benefits expense.

FINANCIAL CONDITION

Assets, Liabilities and Shareholders' Equity

The Company's total assets were $1.83 billion at December 31, 2023, an increase of $208.9 million or 12.92% from $1.62 billion at December 31, 2022. Securities decreased $11.7 million or 7.85% between 2022 and 2023. Loans, net of the allowance for credit losses, increased by $135.6 million or 10.33% from 2022 to 2023. Total liabilities were $1.72 billion at December 31, 2023, compared to $1.51 billion at December 31, 2022. Total shareholders' equity at year end 2023 and 2022 was $108.4 million and $101.7 million, respectively.

Securities

Total securities, excluding restricted stock, were $137.4 million and $149.2 million for the years ended December 31, 2023 and December 31, 2022, respectively. The Company did not purchase any securities during 2023. The Company had $14.5 million in maturities, calls, and principal repayments on securities during 2023. This amount includes $728 thousand or 5.03% in obligations of U.S. government corporations and agencies, $12.9 million or 89.17% in mortgage-backed securities, and $840 thousand or 5.80% in obligations of states and political subdivisions. Note 2 to the Consolidated Financial Statements provides additional details about the Company's securities portfolio as of December 31, 2023 and 2022.

The ability to dispose of available for sale securities prior to maturity provides management more options to react to future rate changes and provides more liquidity, when needed, to meet short-term obligations. The Company had net unrealized losses on available for sale securities of $22.8 million and $25.9 million at December 31, 2023 and 2022, respectively. Unrealized gains or losses on available for sale securities are reported within shareholders' equity, net of the related deferred tax effect, as accumulated other comprehensive income (loss).

The table titled "Maturity Distribution and Yields of Securities" shows the maturity period and average yield for the different types of securities in the portfolio at December 31, 2023. The weighted average yield is calculated based on the relative amortized costs of the securities. Although mortgage-backed securities have definitive maturities, they provide monthly principal curtailments which can be reinvested at a prevailing rate and for a different term.

Maturity Distribution and Yields of Securities

	December 31, 2023				
	Due in one year or less	**Due after 1 through 5 years**	**Due after 5 through 10 years**	**Due after 10 years**	**Total**
Securities available for sale:					
Obligations of U.S. government corporations and agencies	—%	2.15 %	2.65 %	—%	2.60 %
Mortgage-backed securities	—%	—%	1.10 %	1.74 %	1.73 %
Obligations of states and political subdivisions, taxable	3.57 %	2.93 %	3.01 %	—%	3.10 %
Subordinated debt	—%	—%	4.28 %	—%	—%
Total taxable	3.57 %	2.69 %	2.55 %	1.74 %	1.92 %
Obligations of states and political subdivisions, tax-exempt (1)	—%	—%	4.01 %	—%	—%
Total	3.57 %	2.69 %	2.59 %	1.74 %	1.92 %

(1) Yields on tax-exempt securities have been computed on a tax-equivalent basis using a federal tax rate of 21%.

Loan Portfolio

The Company's primary use of funds is supporting lending activities from which it derives the greatest amount of interest income. Gross loans net of net deferred costs and premiums were $1.46 billion and $1.32 billion at December 31, 2023 and 2022, respectively. This represents an increase of $138.8 million or 10.55% for 2023. The ratio of net loans to deposits decreased during the year from 104.72% to 97.10% at December 31, 2022 and December 31, 2023, respectively.

Loans secured by real estate were $1.04 billion, or 71.51%, and $928.3 million, or 70.52%, of total loans at December 31, 2023 and 2022, respectively. This represents an increase of $112.3 million or 12.10% for 2023. Consumer installment loans were $42.4 million, or 2.92%, and $44.8 million, or 3.41%, of total loans at December 31, 2023 and 2022, respectively. This represents an decrease of $2.4 million or 5.40% for 2023. Commercial and industrial loans were $107.8 million, or 7.41%, and $99.6 million, or 7.57%, of total loans at December 31, 2023 and 2022, respectively. This represents an increase of $8.2 million, or 8.21%, for 2023. Marine loans were $251.2 million, or 17.26%, and $230.9 million, or 17.54%, of total loans at December 31, 2023 and 2022, respectively. All other loans were $13.1 million and $12.7 million at December 31, 2023 and 2022, respectively. This represents an increase of $427 thousand or 3.36%.

During the year ended December 31, 2023, loan growth was mainly concentrated in residential and commercial real estate loans, due largely to the continued expansion of the Bank's current market area. Marine loan growth was also strong during the first half of 2023. On August 23, 2023, the Company completed a sale of specific assets from its marine lending segment. As part of the sale, the Company sold its interest in marine vessel floor plan loans totaling $52.8 million and reduced its workforce associated with the marine lending division as it expects to cease accepting new marine lending business. Subsequent to the sale of these assets, the Company retained ownership of marine vessel retail loans, which had a balance of $251.2 million as of December 31, 2023. At present, the Company expects to hold the retained outstanding loans until they are ultimately repaid.

The table titled "Maturity Schedule of Selected Loans" shows the different loan categories and the period during which they mature. For loans maturing in more than one year, the table also shows a breakdown between fixed rate loans and floating rate loans. The table indicates that $567.1 million or 38.97% of the loan portfolio matures within five years. The floating rate loans maturing after five years are primarily comprised of loans secured by 1-4 family residential properties.

Maturity Schedule of Selected Loans
(dollars in thousands)

	December 31, 2023				
	Within 1 Year	After 1 Year Within 5 Years	After 5 Years Within 15 years	After 15 Years	Total
Loans secured by real estate:					
Construction & Farmland	$ 23,834	$ 26,032	$ 25,485	$ 8,794	$ 84,145
Secured by 1-4 family residential properties	16,726	81,821	87,854	169,715	356,116
Commercial & Multifamily	16,052	302,762	271,816	9,705	600,335
Commercial and industrial loans	38,576	41,537	26,339	1,376	107,828
Marine	—	873	69,906	180,389	251,168
Consumer installment loans	550	13,753	1,792	26,324	42,419
All other loans	1,741	2,854	6,521	2,032	13,148
	$ 97,479	$ 469,632	$ 489,713	$ 398,335	$ 1,455,159
For maturities over one year:					
Floating rate loans		$ 68,862	$ 120,064	$ 123,481	$ 312,407
Fixed rate loans		400,770	369,649	274,854	1,045,273
		$ 469,632	$ 489,713	$ 398,335	$ 1,357,680

Asset Quality

The Company has policies and procedures designed to control credit risk and to maintain the quality of its loan portfolio. These include underwriting standards for new originations and ongoing monitoring and reporting of asset quality and adequacy of the allowance for credit losses. There were $6.1 million in total non-performing assets, which consist of nonaccrual loans, loans 90 days or more past due and still accruing, other real estate owned, and repossessed assets at December 31, 2023. This is an increase of $3.5 million when compared to the December 31, 2022 balance of $2.6 million. This increase resulted mostly from an increase in nonaccrual loans.

Nonaccrual loans were $5.6 million at December 31, 2023 and $2.2 million at the end of 2022. The gross amount of interest income that would have been recognized on nonaccrual loans was $140 thousand for 2023 and $93 thousand for 2022. None of this interest income was included in net income for 2023 or 2022. A total of 13 loans totaling $4.1 million were placed on nonaccrual during 2023. Two relationships totaling $3.4 million or 83.25% of loans placed on nonaccrual were added due to delinquent payments, however, these loans required no allowance for credit losses based on management's evaluation of the underlying collateral values. The remaining loans added to nonaccrual status during 2023 ranged from $8 thousand to $367 thousand with the average outstanding balance being $115 thousand. In addition, two loans totaling $294 thousand were removed from nonaccrual status during 2023. Both loans were removed from nonaccrual status due to charge off. Management evaluates the financial condition of these borrowers and the value of any collateral on these loans. The results of these evaluations are used to estimate the amount of losses which may be realized on the disposition of these nonaccrual loans. Nonaccrual loans that were individually evaluated for impairment at December 31, 2023 totaled $5.6 million, none of which required a specific allocation to be assigned.

Other real estate owned and repossessed assets increased from $108 thousand at December 31, 2022 to $304 thousand at December 31, 2023. One asset, a marine vessel, was repossessed during 2023 and placed into repossessed assets and the one property that was foreclosed on during 2022 was sold during 2023. The difference between the amount of other real estate owned and the settlement proceeds is recognized as a gain or loss on the sale of other real estate owned. A net gain of $7 thousand was recognized on the sale of other real estate owned during the twelve months ended December 31, 2023.

Nonperforming and Other Assets

Nonperforming assets consist of nonaccrual loans, loans past due 90 days and accruing interest, other real estate owned (foreclosed properties), and repossessed assets. The table titled "Nonperforming Assets and Credit Ratios" shows the amount of nonperforming assets and loans past due 90 days and accruing interest outstanding for the past two years. The table also shows the ratios for the allowance for credit losses on loans as a percentage of nonperforming assets and nonperforming assets as a percentage of loans outstanding and other real estate owned.

Loans are placed on non-accrual status when collection of principal and interest is doubtful, generally when a loan becomes 90 days past due. There are three negative implications for earnings when a loan is placed on non-accrual status. First, all interest accrued but unpaid at the date that the loan is placed on non-accrual status is either deducted from interest income or written off as a loss. Second, accruals of interest are discontinued until it becomes certain that both principal and interest can be repaid. Finally, there may be actual losses that require additional provisions for credit losses to be charged against earnings.

For real estate loans, upon foreclosure, the properties are recorded at the fair value of the property based on current appraisals and other current market trends, less selling costs. If a write down of the OREO property is necessary at the time of foreclosure, the amount is charged-off against the allowance for credit losses on loans. A review of the recorded property value is performed in conjunction with normal loan reviews, and if market conditions indicate that the recorded value exceeds the fair value, additional write downs of the property value are charged directly to operations. Gains on properties acquired through foreclosure where the fair value less costs to sell exceeds the related loan balance and there have been no prior charge-offs are recorded to current earnings.

In addition, the Company may, under certain circumstances, modify loans. Modifications made to a loan are considered when a borrower is experiencing financial difficulty and the modification constitutes a concession to the borrower that is not in line with market rates and/or terms. Modified terms are dependent upon the financial position and needs of the individual borrower. Generally, the modifications granted are extensions of terms, deferrals of payments for an extended period or interest rate reductions. There were two loan modifications to borrowers experiencing financial difficulty totaling $355 thousand during the year ended December 31, 2023.

Nonperforming Assets and Credit Ratios
(dollars in thousands)

	December 31,	
	2023	**2022**
Nonaccrual loans	$ 5,645	$ 2,162
Loans past due 90 days and accruing interest	181	318
Other real estate owned and repossessed assets	304	108
Total nonperforming assets	$ 6,130	$ 2,588
Allowance for credit losses on loans	$ 14,493	$ 11,218
Gross loans	$ 1,462,686	$ 1,323,783
Allowance for credit losses on loans to nonperforming assets	236 %	433 %
Allowance for credit losses on loans to total loans	0.99 %	0.85 %
Allowance for credit losses on loans to nonaccrual loans	257 %	519 %
Nonaccrual loans to total loans	0.40 %	0.19 %
Non-performing assets to period end loans, other real estate owned and repossessed assets	0.42 %	0.20 %

Other potential problem loans are defined as performing loans that possess certain risks that management has identified that could result in the loans not being repaid in accordance with their terms. Accordingly, these loans are risk rated at a level of substandard or lower. At December 31, 2023, other potential problem loans totaled $2.4 million.

Allowance for Credit Losses on Loans

The allowance for credit losses on loans represents management's current estimate of expected credit losses over the contractual term of loans held for investment, and is recorded at an amount that, in management's judgment, reduces the recorded investment in loans to the net amount expected to be collected. Management's judgment in determining the level of the allowance is based on evaluations of historical loan losses, current conditions and reasonable and supportable forecasts relevant to the collectability of loans. This evaluation is inherently subjective because it requires estimates that are susceptible to significant revision as more information becomes available. Additional information on the purpose and the methods for measuring the allowance for credit losses on loans are discussed in the Critical Accounting Policies section above.

Charged-off loans were $741 thousand and $659 thousand for 2023 and 2022, respectively. Recoveries were $298 thousand and $1.3 million for 2023 and 2022, respectively. Net charge-offs were $443 thousand for 2023. Net recoveries were $601 thousand for 2022. The year over year decline in net recoveries reflected strong recoveries in residential real estate during 2022, which were not also experienced in 2023. The allowance for credit losses as a percentage of loans was 0.99% and 0.85% at the end of 2023 and 2022, respectively. The increase in the allowance percentage year over year was attributable in large part to the adoption of ASC 326, which added $2.1 million to the allowance, as well as growth in the loan portfolio and an increase in nonaccrual loans. The ratio of net charge-offs/(recoveries) to average loans was 0.03% for 2023 and (0.05%) for 2022.

The provision for credit losses for the years ended December 31, 2023 and 2022 was $1.6 million and $1.8 million, respectively. The provision for credit losses in 2023 and 2022 reflected mainly loan growth in the portfolio.

The table titled "Allocation of Allowance for Credit Losses on Loans" shows the amount of the allowance for credit losses which is allocated to the indicated loan categories, along with that category's percentage of total loans, at December 31, 2023 and 2022. The amount of allowance for credit losses allocated to each loan category is based on the amount of delinquent loans in that loan category, the status of nonperforming assets in that loan category, the historical losses for that loan category, the evaluation of qualitative factors impacting the portfolio and the financial condition of certain borrowers whose financial conditional is monitored on a periodic basis. Management believes that the allowance for credit losses is adequate to absorb the current expected losses in the loan portfolio.

Analysis of Allowance for Credit Losses
(dollars in thousands)

	Years Ended December 31,					
	2023			2022		
	Net charge-offs (recoveries)	Average loans outstanding (1)	Net charge-offs (recoveries) to average loans outstanding	Net charge-offs (recoveries)	Average loans outstanding (1)	Net charge-offs (recoveries) to average loans outstanding
Construction and Farmland	$ (8)	$ 89,340	(0.01)%	$ (9)	$ 83,928	(0.01)%
Residential Real Estate	(18)	329,185	(0.01)%	(879)	271,203	(0.32)%
Commercial Real Estate	—	597,275	—%	(197)	492,623	(0.04)%
Commercial	269	95,159	0.28%	191	72,682	0.26%
Marine	126	273,831	0.05%	—	165,777	—%
Consumer	73	34,214	0.21%	35	31,899	0.11%
All Other Loans	1	13,476	0.01%	258	11,338	2.28%
Total	$ 443	$ 1,432,480	0.03%	$ (601)	$ 1,129,450	(0.05)%

(1) Averages as disclosed are based on the outstanding balances of the loans in each segment. These averages do not include net deferred costs and premiums

Allocation of Allowance for Credit Losses on Loans
(dollars in thousands)

	December 31, 2023		December 31, 2022	
	Allowance for Credit Losses	Percent of Loans in Category to Total Loans	Allowance for Credit Losses	Percent of Loans in Category to Total Loans
Construction and Farmland	$ 772	5.8 %	$ 2,714	6.8 %
Residential Real Estate	4,725	24.5 %	1,735	22.1 %
Commercial Real Estate	6,224	41.2 %	2,221	41.6 %
Commercial	1,027	7.4 %	2,222	7.6 %
Marine	1,153	17.3 %	1,555	17.5 %
Consumer	198	2.9 %	299	3.4 %
All Other Loans	394	0.9 %	472	1.0 %
Total	$ 14,493	100%	$ 11,218	100%

Deposits

Total deposits were $1.51 billion and $1.26 billion at December 31, 2023 and 2022, respectively, which represents an increase of $242.2 million or 19.16% during 2023. The table titled “Average Deposits and Rates Paid” shows the average deposit balances and average rates paid for 2023 and 2022.

Average Deposits and Rates Paid
(dollars in thousands)

	Years Ended December 31,			
	2023		2022	
	Amount	Rate	Amount	Rate
Noninterest-bearing	$ 442,539		$ 485,061	
Interest-bearing:				
NOW accounts	244,277	2.14 %	173,843	0.38 %
Money market accounts	257,496	1.74 %	270,725	0.43 %
Regular savings accounts	151,556	0.12 %	179,709	0.07 %
Time deposits:				
$250,000 and more	116,077	4.10 %	62,757	0.89 %
Less than $250,000	219,809	4.08 %	62,907	0.69 %
Total interest-bearing	$ 989,215	2.39 %	$ 749,941	0.39 %
Total deposits	$ 1,431,754		$ 1,235,002	

Noninterest-bearing demand deposits, which are comprised of checking accounts, decreased $42.1 million or 8.80% from $478.8 million at December 31, 2022 to $436.6 million at December 31, 2023. Interest-bearing deposits, which include NOW accounts, money market accounts, regular savings accounts and time deposits, increased $284.4 million or 36.21% from $785.3 million at December 31, 2022 to $1.07 billion at December 31, 2023. Total money market account balances decreased $1.7 million or 0.62% from $265.3 million at December 31, 2022 to $263.6 million at December 31, 2023 and regular savings accounts decreased $33.5 million or 19.39% from $173.0 million at December 31, 2022 to $139.5 million at December 31, 2023. Reciprocal deposit accounts balances (included in total money market account and NOW account balances) increased from $59.5 million to $115.7 million at December 31, 2022 and December 31, 2023, respectively. The reciprocal deposits balance at December 31, 2023 and December 31, 2022 consists of money market and NOW accounts obtained through the ICS network. The growth in deposits was mainly organic growth as we continue to expand and grow into newer market areas. Time deposits increased $255.4 million or 161.74% from $157.9 million at December 31, 2022 to $413.3 million at December 31, 2023, reflecting the Company’s pricing strategy and a $30.0 million brokered account entered into during the first quarter of 2023. Total estimated uninsured deposits at December 31, 2023 and December 31, 2022 were $389.3 million and $322.5 million, respectively.

The Company attempts to fund asset growth with deposit accounts and focus upon core deposit growth as its primary source of funding. Core deposits consist of checking accounts, NOW accounts, money market accounts, regular savings accounts, and time deposits of less than $250,000. Core deposits totaled $1.31 billion or 86.67% and $1.19 billion or 93.88% of total deposits at December 31, 2023 and 2022, respectively.

The table titled “Maturities of Certificates of Deposit and Other Time Deposits of $250,000 and Greater” shows the amount of certificates of deposit of $250,000 and more maturing within the time periods indicated at December 31, 2023. The total amount maturing within one year is $155.5 million or 99.76% of the total amount outstanding.

Maturities of Certificates of Deposit and Other Time Deposits of $250,000 and Greater
(dollars in thousands)

	Within Three Months	Three to Six Months	Six to Twelve Months	Over One Year	Total	Percent of Total Deposits
December 31, 2023	$ 40,372	$ 44,333	$ 70,761	$ 380	$ 155,846	10.35 %

The table titled “Certificates of Deposit and Other Time Deposits Otherwise Uninsured" shows the balances of certificates of deposit that were in excess of the FDIC insurance limit at December 31, 2023. The total amount maturing within one year is $106.1 million or 99.88% of the total amount outstanding.

Certificates of Deposit and Other Time Deposits Otherwise Uninsured
(dollars in thousands)

	Within Three Months	Three to Six Months	Six to Twelve Months	Over One Year	Total	Percent of Total Deposits
December 31, 2023	$ 27,686	$ 33,392	$ 44,972	$ 130	$ 106,180	7.05 %

CAPITAL RESOURCES

Total shareholders’ equity on December 31, 2023 was $108.4 million, reflecting a percentage of total assets of 5.94% as compared to $101.7 million and 6.29% at December 31, 2022. Our common stock’s book value per share increased $1.63 or 5.60% to $30.78 per share at December 31, 2023 from $29.15 per share at December 31, 2022. During 2023, the Company paid $1.20 per share in dividends as compared to $1.15 per share for 2022. The Company has a Dividend Investment Plan that allows participating shareholders to reinvest the dividends in Company stock. During 2023, the Company purchased 8,531 shares of its Common Stock under its stock repurchase program at an average price of $35.34. During 2022, the Company purchased 4,442 shares of its Common Stock under its stock repurchase program at an average price of $34.79. At December 31, 2023, and 2022, Management believes the Bank met all capital adequacy requirements to which it was subject. Additionally, at December 31, 2023, the most recent notification from the Federal Reserve categorized the Bank as well-capitalized under the regulatory framework for prompt corrective action. There are no conditions or events since the notification that management believes have changed the Bank’s category.

Federal regulatory risk-based capital guidelines require percentages to be applied to various assets, including off-balance sheet assets, based on their perceived risk in order to calculate risk-weighted assets. Tier 1 capital consists of total shareholders’ equity plus qualifying trust preferred securities outstanding less net unrealized gains and losses on available for sale securities, goodwill and other intangible assets. Total capital is comprised of Tier 1 capital plus the allowable portion of the allowance for loan losses and any excess trust preferred securities that do not qualify as Tier 1 capital.

Effective January 1, 2015, the Federal Reserve issued final risk-based capital rules to align with the Basel III regulatory capital framework and meet certain requirements of the Dodd-Frank Act. The final rules require the Bank to comply with the following minimum capital ratios: (i) a common equity Tier 1 capital ratio of 4.5% of risk-weighted assets; (ii) a Tier 1 capital ratio of 6.0% of risk-weighted assets; (iii) a total capital ratio of 8.0% of risk-weighted assets; and (iv) a leverage ratio of 4.0% of total assets. In addition, a capital conservation buffer requirement of 2.5% was effective January 1, 2019. The capital conservation buffer is designed to absorb losses during periods of economic stress. Banking institutions with any ratio (excluding the leverage ratio) above the minimum but below the conservation buffer will face constraints on dividends, equity repurchases, and compensation based on the amount of the shortfall. The capital conservation buffer rule requires the Bank to maintain (i) a minimum ratio of common equity Tier 1 to risk-weighted assets of at least 4.5%, plus a 2.5% "capital conservation buffer" (which is added to the 4.5% common equity Tier 1 ratio, effectively resulting in a minimum ratio of common equity Tier 1 to risk-weighted assets of at least 7.0%), (ii) a minimum ratio of Tier 1 capital to risk-weighted assets of at least 6.0%, plus the 2.5% capital conservation buffer (which is added to the 6.0% Tier 1 capital ratio, effectively resulting in a minimum Tier 1 capital ratio of 8.5%), (iii) a minimum ratio of total capital to risk-weighted assets of at least 8.0%, plus the 2.5% capital conservation buffer (which is added to the 8.0% total capital ratio, effectively resulting in a minimum total capital ratio of 10.5%), and (iv) a minimum leverage ratio of 4.0%, calculated as the ratio of Tier 1 capital to average assets.

In 2019, the federal banking agencies jointly issued a final rule that provides for an optional, simplified measure of capital adequacy, the Community Bank Leverage Ratio framework (CBLR), for qualifying community banking organizations, consistent with Section 201 of the Economic Growth, Regulatory Relief, and Consumer Protection Act. The final rule became effective on January 1, 2020. The CBLR removes the requirement for qualifying banking organizations to calculate and report risk-based capital but rather only requires a Tier 1 to average assets (leverage) ratio. Qualifying banking organizations that elect to use the CBLR and that maintain a leverage ratio of greater than the required minimum will be considered to have satisfied the generally applicable risk-based and leverage capital requirements in the agencies' capital rules and, if applicable, will be considered to have met the well-capitalized ratio requirements for purposes of section 38 of the Federal Deposit Insurance Act. Under the regulatory capital rules, an institution electing to use the CBLR must maintain a minimum leverage ratio of 9%. Qualifying institutions are allowed a two-quarter grace period to correct a ratio that falls below the required amount, provided the institution maintains a ratio of more than 8%. At December 31, 2022, the Bank was a qualifying institution and elected to utilize the CBLR to measure capital adequacy. As such, the related amounts and ratios for December 31, 2022, are presented below using the CLBR. The Bank entered the CLBR two-quarter grace period on June 30, 2023, having fallen below the minimum ratio of 9%, and at December 31, 2023 its leverage ratio was 8.48%. Therefore, the amounts and ratios at December 31, 2023 are presented using the risk-based capital framework and not the CLBR.

Pursuant to the Federal Reserve's Small Bank Holding Company and Savings and Loan Holding Company Policy Statement, qualifying bank holding companies with total consolidated assets of less than $3 billion, such as the Company, are not subject to consolidated regulatory capital requirements.

Analysis of Bank Capital
(dollars in thousands)

	December 31, 2023	December 31, 2022
Tier 1 Capital:		
Common stock	$ 1,682	$ 1,682
Capital surplus	9,773	29,773
Retained earnings	144,151	111,759
Nonmortgage servicing assets	(153)	(684)
Total Tier 1 capital	$ 155,453	$ 142,530
Common equity tier 1 capital	$ 155,453	$ 142,530
Tier 2 Capital:		
Allowable portion of allowance for credit losses and reserve for off-balance sheet commitments	$ 13,472	
Total Tier 2 capital	$ 13,472	
Total risk-based capital	$ 168,925	
Risk weighted assets	$ 1,513,802	
Capital Ratios:		
Common equity Tier 1 capital ratio	10.27 %	n/a
Tier 1 risk-based capital ratio	10.27 %	n/a
Total risk-based capital ratio	11.16 %	n/a
Tier 1 leverage ratio	8.48 %	9.15 %

Note 15 to the Consolidated Financial Statements provides additional discussion and analysis of regulatory capital requirements.

LIQUIDITY

Liquidity management involves meeting the present and future financial obligations of the Company with the sale or maturity of assets or with the occurrence of additional liabilities. Liquidity needs are met with cash on hand, deposits in banks, federal funds sold, unpledged securities classified as available for sale, and loans maturing within one year. At December 31, 2023 liquid assets totaled $367.7 million as compared to $303.8 million at December 31, 2022. These amounts represent 21.41% and 20.05% of total liabilities at December 31, 2023 and 2022, respectively. Securities provide a constant source of liquidity through paydowns and maturities. Also, the Company maintains short-term borrowing arrangements, namely federal funds lines of credit, with larger financial institutions as an additional source of liquidity. The Bank's membership with the Federal Home Loan Bank of Atlanta also provides a source of borrowings with numerous rate and term structures. At December 31, 2023 and 2022, the Company had remaining credit availability in the amounts of $169.6 million and $105.7 million, respectively, with the Federal Home Loan Bank of Atlanta. The Company also had unused lines of credit with financial institutions of $78.0 million at December 31, 2023 and 2022. The Company's senior management monitors the liquidity position regularly and attempts to maintain a position which utilizes available funds most efficiently. As a result of the Company's management of liquid assets and the ability to generate liquidity through liability funding, management believes that the Company maintains overall liquidity sufficient to satisfy its depositors' requirements and meet its customers' credit needs.

OFF-BALANCE SHEET ARRANGEMENTS AND CONTRACTUAL OBLIGATIONS

Note 18 to the Consolidated Financial Statements provides information about the off-balance sheet arrangements which arise through the lending activities of the Company. These arrangements increase the degree of both credit and interest rate risk beyond that which is recognized through the financial assets and liabilities on the consolidated balance sheets.

Item 7A. Quantitative and Qualitative Disclosures about Market Risk

As the holding company of the Bank, the Company's primary component of market risk is interest rate volatility. Interest rate fluctuations will impact the amount of interest income and expense the Bank receives or pays on almost all of its assets and liabilities and the market value of its interest-earning assets and interest-bearing liabilities, excluding those which have a very short term until maturity. Interest rate risk exposure of the Company is, therefore, experienced at the Bank level. Asset / liability management attempts to maximize the net interest income of the Company by adjusting the volume and price of rate sensitive assets and liabilities. The Company does not subject itself to foreign currency exchange or commodity price risk due to prohibition through policy and the current nature of operations. Derivative instruments and hedging activities of the Company have historically been minimal.

The Bank's interest rate management strategy is designed to maximize net interest income and preserve the capital of the Company. The Bank's financial instruments are periodically subjected to various simulations whose results are discussed in the following paragraphs. These models are based on actual data from the Bank's financial statements and assumptions about the performance of certain financial instruments. Prepayment assumptions are applied to all mortgage related assets, which includes real estate loans and mortgage-backed securities. Prepayment assumptions are based on a median rate at which principal payments are received on these assets over their contractual term. The rate of principal payback is assumed to increase when rates fall and decrease when rates rise. Term assumptions are applied to non-maturity deposits, which includes demand deposits, NOW accounts, savings accounts, and money market accounts. Demand deposits and NOW accounts are generally assumed to have a term greater than one year since the total amount outstanding does not fluctuate with changes in interest rates. Savings accounts and money market accounts are assumed to be more interest rate sensitive, therefore, a majority of the amount outstanding is assumed to have a term of less than one year.

The simulation analysis evaluates the potential effect of upward and downward changes in market interest rates on future net interest income. The Bank views the immediate shock of rates as a more effective measure of interest rate risk exposure. The analysis assesses the impact on net interest income over a 12 month period after an immediate change or "shock" in rates, of 100 basis points up to 400 basis points. The simulation analysis results are presented in the table below:

Year 1 Net Interest Income Simulation
(dollars in thousands)

	Change in Net Interest Income	
Assumed Market Interest Rate Shock	**Dollars**	**Percent Change**
-400 BP	$ (994)	(1.98)%
-300 BP	201	0.40 %
-200 BP	755	1.51 %
-100 BP	1,035	2.06 %
+100 BP	(1,331)	(2.66)%
+200 BP	(2,961)	(5.91)%
+300 BP	(4,368)	(8.71)%
+400 BP	(5,776)	(11.52)%

The Bank uses simulation analysis to assess earnings at risk and economic value of equity ("EVE") analysis to assess economic value at risk. This analysis method allows management to regularly monitor the direction and magnitude of the Bank's interest rate risk exposure. The modeling techniques cannot be measured with complete precision. Maturity and repricing characteristics of assets and liabilities, prepayments on amortizing assets, non-maturity deposit sensitivity and loan and deposit pricing are key assumptions used in acquiring this analysis. There is a realm of uncertainty in using these assumptions but the analysis does provide the Bank with the ability to estimate interest rate risk position over time.

The table below examines the EVE. The EVE of the balance sheet is defined as the discounted present value of expected asset cash flows minus the discounted present value of the expected liability cash flows. The analysis involves changing the interest rates used in determining the expected cash flows and in discounting the cash flows. The model indicates a more significant exposure to falling interest rates. These results are driven primarily by the relative change in value of the Bank's core deposit base as rates rise.

Static EVE Change
(dollars in thousands)

	Change in EVE	
Assumed Market Interest Rate Shift	**Dollars**	**Percent Change**
-400 BP Shock	$ (70,607)	(29.93)%
-300 BP Shock	(31,197)	(13.22)%
-200 BP Shock	(9,636)	(4.08)%
-100 BP Shock	3,042	1.29%
+100 BP Shock	(9,271)	(3.93)%
+200 BP Shock	(25,497)	(10.81)%
+300 BP Shock	(33,777)	(14.32)%
+400 BP Shock	(42,473)	(18.00)%

Item 8. Financial Statements and Supplementary Data

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders
Eagle Financial Services, Inc.

Opinion on the Financial Statements
We have audited the accompanying consolidated balance sheets of Eagle Financial Services, Inc. and its subsidiary (the Company) as of December 31, 2023 and 2022, the related consolidated statements of income, comprehensive income (loss), changes in shareholders' equity and cash flows for the years then ended, and the related notes to the consolidated financial statements (collectively, the financial statements). In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2023 and 2022, and the results of its operations and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

Adoption of New Accounting Standard
As discussed in Note 1 of the financial statements, the Company changed its method of accounting for credit losses in 2023 due to the adoption of Accounting Standards Update 2016-13, Financial Instruments – Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, including all related amendments.

Basis for Opinion
These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the Company's financial statements based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (PCAOB) and are required to be independent with respect to the Company in accordance with U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. As part of our audits we are required to obtain an understanding of internal control over financial reporting but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion.

Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

Critical Audit Matter
The critical audit matter communicated below is a matter arising from the current period audit of the financial statements that was communicated or required to be communicated to the audit committee and that: (1) relates to accounts or disclosures that are material to the financial statements and (2) involved our especially challenging, subjective, or complex judgments. The communication of critical audit matters does not alter in any way our opinion on the financial statements, taken as a whole, and we are not, by communicating the critical audit matter below, providing a separate opinion on the critical audit matter or on the accounts or disclosures to which it relates.

Allowance for Credit Losses – Collectively Evaluated Loans

As further described in Note 1 of the consolidated financial statements, the Company changed its method of accounting for credit losses on January 1, 2023, due to the adoption of Accounting Standards Update 2016-13, *Financial Instruments – Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments,* as amended. The allowance for credit losses on loans (ACL) is a valuation allowance that represents management's best estimate of expected credit losses on loans measured at amortized cost considering available information relevant to assessing collectability over the loans' contractual terms. Loans which share common risk characteristics are pooled and collectively evaluated by the Company using historical data, as well as assessments of current conditions and reasonable and supportable forecasts of future conditions. The Company's ACL related to collectively evaluated loans represented the entirety of the total recorded ACL of $14.49 million as of December 31, 2023. The collectively evaluated ACL consists of quantitative and qualitative components.

The quantitative component consists of loss estimates derived from the Company's application of its cohort methodology, which identifies and tracks respective losses generated by specific cohorts (or pools) of loans over their remaining lives. These estimates consider large amounts of data over an extended period of time. In addition to the quantitative component, the collectively evaluated ACL also includes a qualitative component which aggregates management's assessment of available information relevant to assessing collectability that is not captured in the quantitative loss estimation process. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available.

Management exercised significant judgment when estimating the ACL on collectively evaluated loans. We identified the estimation of the collectively evaluated ACL as a critical audit matter as auditing the collectively evaluated ACL involved significant audit effort and judgment in evaluating management's assessment of the inherently subjective estimates.

How We Addressed the Matter in Our Audit

The primary audit procedures we performed to address this critical audit matter included:

- Obtaining an understanding of the Company's processes for determining its ACL on collectively evaluated loans, including the underlying methodology and significant inputs to the calculation.
- Substantively testing management's process for measuring the collectively evaluated ACL, including:
  - Evaluating the conceptual soundness of the methodology for determining the collectively evaluated ACL.
  - Testing the completeness and accuracy of data used in developing the quantitative loss calculations.
  - Evaluating the pools of collectively evaluated and individually evaluated loans for completeness.
  - Evaluating management's determination of qualitative adjustments, including the data on which the qualitative adjustments were based as well as the relative magnitude of the adjustments.
  - Testing the mathematical accuracy of the ACL for collectively evaluated loans, including the calculations underlying the quantitative component as well as application of qualitative factors to the collectively evaluated loan balances.

/s/ Yount, Hyde & Barbour, P.C.

We have served as the Company's auditor since 2015.

Winchester, Virginia
March 29, 2024

EAGLE FINANCIAL SERVICES, INC. AND SUBSIDIARY
Consolidated Balance Sheets
December 31, 2023 and 2022
(dollars in thousands, except per share amounts)

	December 31, 2023	December 31, 2022
Assets		
Cash and due from banks	$ 15,417	$ 16,629
Interest-bearing deposits with other institutions	96,649	49,902
Federal funds sold	26,287	363
Total cash and cash equivalents	138,353	66,894
Securities available for sale, at fair value	137,443	149,156
Restricted investments	9,568	9,233
Loans held for sale	1,661	153
Loans	1,462,686	1,323,783
Allowance for credit losses	(14,493)	(11,218)
Net loans	1,448,193	1,312,565
Bank premises and equipment, net	18,108	18,064
Other real estate owned, net of allowance	—	108
Bank owned life insurance	29,575	23,862
Other assets	42,696	36,682
Total assets	$ 1,825,597	$ 1,616,717
Liabilities and Shareholders' Equity		
Liabilities		
Deposits:		
Noninterest bearing demand deposits	$ 436,619	$ 478,750
Savings and interest bearing demand deposits	656,439	627,431
Time deposits	413,264	157,894
Total deposits	$ 1,506,322	$ 1,264,075
Federal funds purchased	—	32,980
Federal Home Loan Bank advances, short-term	20,000	175,000
Federal Home Loan Bank advances, long-term	145,000	—
Subordinated debt	29,444	29,377
Other liabilities	16,452	13,556
Total liabilities	$ 1,717,218	$ 1,514,988
Commitments and contingencies		
Shareholders' Equity		
Preferred stock, $10 par value; 500,000 shares authorized and unissued	$ —	$ —
Common stock, $2.50 par value; authorized 10,000,000 shares; issued and outstanding 2023, 3,520,894 including 56,914 unvested restricted stock; issued and outstanding 2022, 3,490,086 including 38,780 unvested restricted stock	8,660	8,629
Surplus	14,280	13,268
Retained earnings	103,445	100,278
Accumulated other comprehensive (loss)	(18,006)	(20,446)
Total shareholders' equity	$ 108,379	$ 101,729
Total liabilities and shareholders' equity	$ 1,825,597	$ 1,616,717

See Notes to Consolidated Financial Statements

EAGLE FINANCIAL SERVICES, INC. AND SUBSIDIARY
Consolidated Statements of Income
Years Ended December 31, 2023 and 2022
(dollars in thousands, except per share amounts)

	2023	2022
Interest and Dividend Income		
Interest and fees on loans	$ 75,520	$ 50,682
Interest and dividends on securities:		
Taxable interest income	3,141	3,292
Interest income exempt from federal income taxes	16	221
Dividends	523	109
Interest on deposits in banks	3,768	352
Interest on federal funds sold	160	30
Total interest and dividend income	$ 83,128	$ 54,686
Interest Expense		
Interest on deposits	$ 23,630	$ 2,941
Interest on federal funds purchased	70	170
Interest on Federal Home Loan Bank advances	7,720	1,295
Interest on subordinated debt	1,417	1,067
Total interest expense	$ 32,837	$ 5,473
Net interest income	$ 50,291	$ 49,213
Provision For Credit Losses	1,649	1,830
Net interest income after provision for credit losses	$ 48,642	$ 47,383
Noninterest Income		
Wealth management fees	$ 4,926	$ 4,149
Service charges on deposit accounts	1,810	1,618
Other service charges and fees	4,413	3,943
Gain on the sale of marine finance assets	435	—
Gain (loss) on the sale and disposal of bank premises and equipment	14	(11)
(Loss) on sale of securities	—	(737)
Gain on sale of loans	1,428	1,875
Bank owned life insurance income	713	626
Other operating income	1,006	1,882
Total noninterest income	$ 14,745	$ 13,345
Noninterest Expenses		
Salaries and employee benefits	$ 30,306	$ 25,730
Occupancy expenses	2,202	2,068
Equipment expenses	1,299	1,121
Advertising and marketing expenses	1,157	770
Stationery and supplies	191	199
ATM network fees	1,563	1,313
Other real estate owned expense	5	34
(Gain) on other real estate owned	(7)	—
FDIC assessment	1,585	614
Computer software expense	1,360	960
Bank franchise tax	1,255	886
Professional fees	2,540	2,019
Data processing fees	1,935	1,779
Other operating expenses	7,363	5,564
Total noninterest expenses	$ 52,754	$ 43,057
Income before income taxes	$ 10,633	$ 17,671
Income Tax Expense	1,276	3,150
Net income	$ 9,357	$ 14,521
Earnings Per Share		
Net income per common share, basic	$ 2.66	$ 4.17
Net income per common share, diluted	$ 2.66	$ 4.17

See Notes to Consolidated Financial Statements

EAGLE FINANCIAL SERVICES, INC. AND SUBSIDIARY
Consolidated Statements of Comprehensive Income (Loss)
Years Ended December 31, 2023 and 2022
(dollars in thousands)

	2023	2022
Net income	$ 9,357	$ 14,521
Other comprehensive income (loss):		
Changes in benefit obligations and plan assets for post retirement benefit plans, net of reclassification adjustments, net of deferred income tax of $(3) and $0 for the years ended December 31, 2023 and 2022, respectively	(5)	—
Unrealized gain (loss) on available for sale securities, net of reclassification adjustments, net of deferred income tax of $650 and ($5,394) for the years ended December 31, 2023 and 2022, respectively	2,445	(20,291)
Total other comprehensive income (loss)	2,440	(20,291)
Total comprehensive income (loss)	$ 11,797	$ (5,770)

See Notes to Consolidated Financial Statements

EAGLE FINANCIAL SERVICES, INC. AND SUBSIDIARY
Consolidated Statements of Changes in Shareholders' Equity
Years Ended December 31, 2023 and 2022
(dollars in thousands, except per share amounts)

	Common Stock	Surplus	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
December 31, 2021	$ 8,556	$ 12,115	$ 89,764	$ (155)	$ 110,280
Net income			14,521		14,521
Other comprehensive (loss)				(20,291)	(20,291)
Restricted stock awards, stock incentive plan (23,079 shares)	58	(58)			—
Stock-based compensation expense		1,017			1,017
Issuance of common stock, dividend investment plan (5,582 shares)	14	185			199
Issuance of common stock, employee benefit plan (4,697 shares)	12	152			164
Retirement of common stock (4,442 shares)	(11)	(143)			(154)
Dividends declared ($1.15 per share)			(4,007)		(4,007)
December 31, 2022	$ 8,629	$ 13,268	$ 100,278	$ (20,446)	$ 101,729
Cumulative effect adjustment for CECL			(1,961)		(1,961)
Net income			9,357		9,357
Other comprehensive income				2,440	2,440
Restricted stock awards, stock incentive plan (17,402 shares)	43	(43)			—
Stock-based compensation expense		1,213			1,213
Issuance of common stock, employee benefit plan (3,803 shares)	9	123			132
Repurchase and retirement of common stock (8,531 shares)	(21)	(281)			(302)
Dividends declared ($1.20 per share)			(4,229)		(4,229)
December 31, 2023	$ 8,660	$ 14,280	$ 103,445	$ (18,006)	$ 108,379

See Notes to Consolidated Financial Statements

EAGLE FINANCIAL SERVICES, INC. AND SUBSIDIARY
Consolidated Statements of Cash Flows
Years Ended December 31, 2023 and 2022
(dollars in thousands)

	2023	2022
Cash Flows from Operating Activities		
Net income	$ 9,357	$ 14,521
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	1,002	979
Amortization of other assets	988	931
Origination of loans held for sale	(41,606)	(14,276)
Proceeds from sale of loans held for sale	41,224	15,486
Net (gain) on sales of loans	(1,428)	(1,875)
Provision for credit losses	1,649	1,830
(Gain) on other real estate owned	(7)	—
(Gain) on the sale of marine finance assests	(435)	—
(Gain) loss on the sale and disposal of premises and equipment	(14)	11
Loss on the sale of securities	—	737
Amortization of subordinated debt issuance costs	67	51
Stock-based compensation expense	1,213	1,017
Premium amortization on securities, net	335	562
Bank owned life insurance income	(713)	(626)
Deferred tax (benefit)	(1,509)	(86)
Changes in assets and liabilities:		
(Increase) in other assets	(4,583)	(4,742)
Increase (decrease) in other liabilities	1,335	(706)
Net cash provided by operating activities	$ 6,875	$ 13,814
Cash Flows from Investing Activities		
Proceeds from maturities, calls, and principal payments of securities available for sale	$ 14,473	$ 27,630
Proceeds from the sale of securities available for sale	—	15,370
Purchases of securities available for sale	—	(26,819)
Proceeds from the sale of restricted investments	4,975	—
Purchase of restricted investments	(5,310)	(8,184)
Proceeds for the sale of bank premises and equipment	39	33
Purchases of bank premises and equipment	(1,071)	(838)
Purchase of bank-owned life insurance	(5,000)	—
Proceeds from the sale of other real estate owned	115	—
Changes in collateral posted with other financial institutions, net	—	(700)
Proceeds from sale of marine finance assets	53,987	—
Proceeds from sales of loans	51,871	155,525
Origination of loans, net of prinicpal collected	(243,441)	(492,592)
Funding of capital commitments related to other investments	(922)	(761)
Net cash (used in) investing activities	$ (130,284)	$ (331,336)
Cash Flows from Financing Activities		
Net (decrease) increase in demand deposits, money market and savings accounts	$ (13,123)	$ 52,530
Net increase in certificates of deposit	255,370	34,310
Net (decrease) increase in federal funds purchased	(32,980)	32,980
Net (decrease) increase in short-term Federal Home Loan Bank advances	(155,000)	175,000
Advances of long-term Federal Home Loan Bank advances	145,000	—
Issuance of subordinated debt, net of issuance costs	—	29,326
Issuance of common stock, employee benefit plan	132	164
Repurchase and retirement of common stock	(302)	(154)
Cash dividends paid	(4,229)	(3,808)
Net cash provided by financing activities	$ 194,868	$ 320,348
Increase in cash and cash equivalents	$ 71,459	$ 2,826
Cash and Cash Equivalents		
Beginning	66,894	64,068
Ending	$ 138,353	$ 66,894
Supplemental Disclosures of Cash Flow Information		
Cash payments for:		
Interest	$ 31,332	$ 4,563
Income taxes	$ 2,068	$ 4,368
Supplemental Schedule of Noncash Investing and Financing Activities:		
Unrealized gain (loss) on securities available for sale	$ 3,095	$ (25,685)
Minimum postretirement liability adjustment	$ (8)	$ —
Repossessed assets acquired in settlement of loans	$ 304	$ 108
Issuance of common stock, dividend investment plan	$ —	$ 199

See Notes to Consolidated Financial Statements

NOTE 1. Nature of Banking Activities and Significant Accounting Policies

Eagle Financial Services, Inc. (the "Company" or "Corporation") and Bank of Clarke (the "Bank") make commercial, financial, agricultural, residential and consumer loans to customers in Virginia, Maryland and the Eastern Panhandle of West Virginia. The loan portfolio is well diversified and generally is collateralized by assets of the customers. The loans are expected to be repaid from cash flows or proceeds from the sale of selected assets of the borrowers. In addition, the Bank of Clarke Wealth Management Division, a division of the Bank, provides both a full-service Trust Department and a separate brokerage area.

The accounting and reporting policies of the Company conform to accounting principles generally accepted in the United States of America and to accepted practices within the banking industry.

Principles of Consolidation

The Company owns 100% of the Bank. The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiary. All significant intercompany accounts and transactions between the Company and the Bank have been eliminated.

Wealth Management Assets

The Bank of Clarke Wealth Management Division provides both a full-service Trust Department and a separate brokerage area. The Trust Department features a full range of fiduciary expertise, including service as Trustee of personal trusts, service as guardian or conservator by court appointment, fiduciary investment management, estate settlement, and agency for trustees. The brokerage area offers advisory services and a broad selection of investment products, including Individual Retirement Accounts, mutual funds, tax-deferred annuities, 529 college savings plans, life insurance, long term care insurance, brokerage certificates of deposit, among other brokerage services. Securities and other property held by the Bank of Clarke Wealth Management Division in a fiduciary or agency capacity are not assets of the Bank and are not included in the accompanying consolidated financial statements.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. The material estimate that is particularly susceptible to significant change in the near term relates to the determination of the allowance for credit losses on loans.

Cash and Cash Equivalents

For purposes of reporting cash flows, cash and cash equivalents include cash on hand, amounts due from banks, federal funds sold, and interest bearing deposits. Generally, federal funds are purchased and sold for one-day periods.

Securities

The Company determines the appropriate classification of securities at the time of purchase. Debt securities that management has the positive intent and ability to hold to maturity are classified as "held to maturity" and recorded at amortized cost. Debt securities not classified as held to maturity are classified as "available for sale" and recorded at fair value, with unrealized gains and losses excluded from earnings and reported in other comprehensive income. Equity securities with readily determinable fair values are carried at fair value, with changes in fair value reported in income. Equity securities without readily determinable fair values are carried at cost, minus impairment, if any, plus or minus changes resulting from observable price changes in orderly transactions for the identical or a similar investment.

Purchase premiums are recognized in interest income using the effective interest rate method over the period from purchase to maturity or, for callable securities, the earliest call date, and purchase discounts are recognized in the same manner from purchase to maturity.

The Bank is required to maintain an investment in the capital stock of certain correspondent banks. No readily available market exists for this stock and it has no quoted market value. The investment in these securities is recorded at cost and they are reported on the Company's consolidated balance sheet as restricted investments.

Allowance for Credit Losses on Securities

For available for sale debt securities in an unrealized loss position, management first assesses whether the Company intends to sell, or if it is likely that the Company will be required to sell the security before recovery of its amortized cost basis. If either of the criteria regarding intent or requirement to sell is met, the security's amortized cost basis is written down to fair value through a provision for credit losses charge to earnings. For debt securities available for sale that do not meet either of these criteria, management evaluates whether the decline in fair value has resulted from credit losses or other factors. In making this assessment, management considers both quantitative and qualitative factors,

A substantial portion of the available for sale debt securities held by the Company are obligations issued by U.S. government agency and U.S. government-sponsored enterprises, including mortgage-backed securities. These securities are either explicitly or implicitly guaranteed by the U.S. government, are highly rated by major credit rating agencies and have a long history of no credit losses. For these securities, management takes into consideration the long history of no credit losses and other factors to assess the risk of nonpayment even if the U.S. government were to default. As such, the Company utilized a zero credit loss estimate for these securities.

For available for sale debt securities that are not guaranteed by U.S. government agencies and U.S. government-sponsored enterprises, management utilizes a third-party credit modeling tool based on observable market data, which assists management in identifying any potential credit risk associated with these available for sale debt securities. Qualitative factors are also considered, including the extent to which fair value is less than amortized cost, changes to the credit rating of the security by a rating agency, and adverse conditions specifically related to the security, among other factors. If a credit loss exists, an allowance for credit losses is recorded that reflects the amount of the impairment related to credit losses, limited by the amount by which the security's amortized cost basis exceeds its fair value.

Changes in the allowance for credit losses are recorded in net income in the period of change and are included in provision for credit losses. Changes in the fair value of debt securities available for sale not resulting from credit losses are recorded in other comprehensive income (loss).

Loans Held for Sale

Mortgage loans originated with the intent to sell in the secondary market are classified as loans held for sale and carried at the lower of cost or fair value as determined by commitments from investors. Mortgage loans that are sold in the secondary market are sold servicing released. The Company may also classify other loans as loans held for sale as part of its ongoing portfolio management strategies. Such other loans are generally not originated with the intent to sell. Once a decision is made to sell loans not previously classified as held for sale, such loans are transferred into the held-for-sale classification and carried at the lower of cost or fair value. In 2023, the Company sold non-mortgage loans totaling approximately $59.6 million as part of its portfolio management strategies that were previously classified as held for investment. Gains and losses on sales of loans are recorded based on the differential between the sales proceeds and carrying value of the underlying loans.

Loan Servicing Rights

Loan servicing rights are separate from the underlying loan and may be retained or sold by the Company when the related loan is sold. In connection with sale of certain loans, the Company has recognized assets for retained loan servicing rights. Capitalized loan servicing rights represent the economic benefits associated with contracts to service loans under which the benefits of servicing are expected to more than adequately compensate the Company for performing the servicing. Assets for retained loan servicing rights are initially recognized as a component of the gain recognized on the sale of the underlying loan(s) and are recorded at fair value on the consolidated balance sheets. Loan servicing rights are subsequently accounted for using the amortization method. The amortization method requires the servicing assets to be amortized in proportion to and over the period of estimated net servicing income. Additionally, the recorded balances are evaluated for impairment each reporting period and are reported at the lower of amortized cost or fair value. Assets for loan servicing rights are recorded in other assets in the consolidated balance sheets. Servicing fee income, net of amortization and impairment, if any, is reported in other service charges and fees in the consolidated statements of income.

Loans Held for Investment

The Company makes mortgage, commercial and consumer loans to customers. A substantial portion of the loan portfolio is represented by mortgage loans throughout the Counties of Clarke, Frederick, Loudoun and Fairfax, Virginia as well as the Towns of Leesburg and Purcellville and the Cities of Winchester and Frederick, Maryland. The ability of the Company's debtors to honor their contracts is dependent upon the real estate and general economic conditions in these areas.

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or pay-off generally are reported at their outstanding unpaid principal balances adjusted for the charge-offs, unearned discounts, any deferred fees or costs on originated loans, and the allowance for credit losses. The Company has elected to exclude accrued interest receivable from the amortized cost basis. Accrued interest totaled $4.6 million and $3.5 million at December 31, 2023 and 2022, and is included in the other assets line item in the Consolidated Balance Sheets.

Interest income is accrued on the unpaid principal balance. Loan fees collected and certain costs incurred related to loan originations are deferred and amortized as an adjustment to interest income over the life of the related loans. Deferred fees and costs are recorded as an adjustment to interest income using a method that approximates a constant yield.

A loan's past due status is based on the contractual due date of the most delinquent payment due. Loans are generally placed on nonaccrual status when the collection of principal or interest is 90 days or more past due, or earlier, if collection is uncertain based on an evaluation of the net realizable value of the collateral and the financial strength of the borrower. Any accrued interest receivable on loans placed on nonaccrual status is reversed by an adjustment to interest income. Loans greater than 90 days past due may remain on accrual status if management determines it has adequate collateral to cover the principal and interest. For those loans that are carried on nonaccrual status, payments are first applied to principal outstanding. A loan may be returned to accrual status if the borrower has demonstrated a sustained period of repayment performance in accordance with the contractual terms of the loan and there is reasonable assurance the borrower will continue to make payments as agreed. These policies are applied consistently across our loan portfolio.

All interest accrued but not collected for loans that are placed on nonaccrual or charged off is reversed against interest income. All payments, including any interest collected, on these loans are accounted for on the cash-basis or cost-recovery method and applied to principal, until qualifying for return to accrual status. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

In the ordinary course of business, the Company has entered into commitments to extend credit and standby letters of credit. Such financial instruments are recorded in the Consolidated Balance Sheets when they are funded.

Loan Modifications

The Company adopted Accounting Standards Update ("ASU") No. 2022-02, "Financial Instruments-Credit Losses (Topic 326), Troubled Debt Restructurings and Vintage Disclosures" on January 1, 2023. The amendments in ASU 2022-02 eliminated the recognition and measurement of troubled debt restructurings and enhanced disclosures for loan modifications to borrowers experiencing financial difficulty.

Modifications made to loans are considered for disclosure under the guidance in ASU 2022-02 if a borrower is experiencing financial difficulty, if the modification is in the form of principal forgiveness, an interest rate reduction, an other-than-insignificant payment delay, or a term extension (or a combination thereof). Modified terms are dependent upon the financial position and needs of the individual borrower. Generally, the modifications granted are extensions of terms, deferrals of payments for an extended period or interest rate reductions. If a loan was accruing prior to being modified and if the Company concludes that the borrower is able to make such payments, and there are no other factors or circumstances that would cause it to conclude otherwise, the loan will remain on accrual status. If a loan was on non-accrual status at the time of the modification, the loan will remain on non-accrual status following the modification and may be returned to accrual status based on the policy for returning loans to accrual status as noted above.

Risks by Loan Portfolio Segment

One-to-Four-Family Residential Real Estate Lending

Residential mortgage loans generally are made on the basis of the borrower's ability to make repayment from employment and other income and are secured by real estate whose value tends to be readily ascertainable. As part of the application process, information is gathered concerning income, employment and credit history of the applicant. The valuation of residential collateral is provided by independent fee appraisers who have been approved by the Bank's Directors Loan Committee.

Commercial Real Estate Lending

Commercial real estate lending entails significant additional risk as compared with residential mortgage lending. Commercial real estate loans typically involve larger loan balances concentrated with single borrowers or groups of related borrowers. Additionally, the repayment of loans secured by income producing properties is typically dependent on the successful operation of a business or a real estate project and thus may be subject, to a greater extent, to adverse conditions in the real estate market or the economy, in general.

Construction and Land Development Lending

There are two characteristics of construction lending which impact its overall risk as compared to residential mortgage lending. First, there is more concentration risk due to the extension of a large loan balance through several lines of credit to a single developer or contractor. Second, there is more collateral risk due to the fact that loan funds are provided to the borrower based upon the estimated value of the collateral after completion. This could cause an inaccurate estimate of the amount needed to complete construction or an excessive loan-to-value ratio. To mitigate the risks associated with construction lending, the Bank generally limits loan amounts to 80% of the estimated appraised value of the finished home or other real estate property.

Commercial and Industrial Lending

Commercial business loans generally have more risk than residential mortgage loans, but have higher yields. To manage these risks, the Bank generally obtains appropriate collateral and personal guarantees from the borrower’s principal owners and monitors the financial condition of the borrower. Commercial business loans typically are made on the basis of the borrower’s ability to make repayment from cash flow from its business and are secured by business assets, such as accounts receivable, equipment, inventory and boats. As a result, the availability of funds for the repayment of commercial business loans is substantially dependent on the success of the business itself. Furthermore, the collateral for commercial business loans may depreciate over time and generally cannot be appraised with as much precision as residential real estate.

Consumer Lending

Consumer loans generally entail greater risk than residential mortgage loans, particularly in the case of consumer loans which are unsecured or secured by rapidly depreciable assets such as automobiles. A portion of the Company’s consumer loans are also secured by boats. In such cases, any repossessed collateral on a defaulted consumer loan may not provide an adequate source of repayment of the outstanding loan balance as a result of the greater likelihood of damage, loss or depreciation.

Marine Lending

The Bank’s marine loan portfolio is comprised of originated retail loans. Through August 22, 2023, the marine loan portfolio also included dealer floor plan loans, classified as commercial and industrial loans. On August 23, 2023, the Company completed the sale of certain assets of its marine finance division to an unrelated third-party. Under the sales agreements, the Company sold its interest in marine floor plan loans, while retaining ownership of its marine retail loans which continue to constitute a significant portion of the Company's assets, revenues, and earnings. The Company expects to cease accepting new marine lending business and hold the retained outstanding loans until they are ultimately repaid.

The Company’s relationships were limited to well established dealers of global premium brand manufacturers, with the top three manufacturer customers have been in business between 30 and 100 years. Retail loans were generally limited to premium manufactures with established relationships with the Company, which have a vested interest in the secondary market pricing of their respective brand due to the limited inventory available for resale. Consequently, while not contractually committed, manufacturers will often support secondary resale values which can have the effect of reducing losses from non-performing retail marine loans. Retail borrowers generally have very high credit scores, substantial down payments, substantial net worth, personal liquidity, and excess cash flow.

Allowance for Credit Losses on Loans

The allowance for credit losses is established through charges to earnings in the form of a provision for credit losses. The allowance for credit losses is also increased by recoveries of amounts previously charged-off and is reduced by charge-offs on loans. Loan charge-offs are recognized as the difference between the carrying value of the loan and the estimated net realizable value or fair value of the collateral, if collateral dependent, when management believes that the collectability of the principal is unlikely. Full or partial charge-offs on collateral dependent individually analyzed loans are generally recognized when the collateral is deemed to be insufficient to support the carrying value of the loan.

The allowance represents management's current estimate of expected credit losses over the contractual term of loans held for investment, and is recorded at an amount that, in management's judgment, reduces the recorded investment in loans to the net amount expected to be collected. No allowance for credit losses is recorded on accrued interest receivable and amount written-off are reversed by an adjustment to interest income. Management's judgment in determining the level of the allowance is based on evaluations of historical loan losses, current conditions and reasonable and supportable forecasts relevant to the collectability of loans. Loans that share common risk characteristics are evaluated collectively using a loss-rate, or cohort methodology to estimate its current expected credit losses on loans. The cohort method identifies and captures the balances of pooled loans with similar risk characteristics, as a point in time to form a cohort, then tracks the respective losses generated by that cohort of loans over their remaining lives. The method encompasses loan balances for as long as the loans are outstanding.

Management's estimate of the allowance for credit losses on loans that are collectively evaluated also includes a qualitative assessment of available information relevant to assessing collectability that is not captured in the loss estimation process. Factors considered by management include economic conditions including reasonable and supportable forecasts of economic conditions; the nature and volume of the loan portfolio; the volume and severity of delinquencies and adversely classified loan balances; ending policy and procedures; credit administration and lending staff; loan review; concentrations of credit and the value of underlying collateral. This evaluation is inherently subjective, as it requires estimates that are susceptible to significant revision as more information becomes available.

Loans that do not share common risk characteristics with other loans are evaluated individually and are not included in the collective analysis. The allowance for credit losses on loans that are individually evaluated may be estimated based on their expected cash flows, or, in the case of loans for which repayment is expected substantially through the operation or sale of collateral when the borrower is experiencing financial difficulty, may be measured based on the fair value of the collateral or the fair value of collateral less estimated costs to sell.

Allowance for Credit Losses on Unfunded Commitments

The Company records a reserve, reported in other liabilities, for expected credit losses on commitments to extend credit that are not unconditionally cancelable by the Company. The reserve for unfunded commitments is measured based on the principles utilized in estimating the allowance for credit losses on loans and an estimate of the amount of unfunded commitments expected to be advanced. Changes in the reserve for unfunded commitments are recorded through the provision for credit losses. The reserve totaled $479 thousand and $65 thousand at December 31, 2023 and 2022, respectively. The initial adjustment for the adoption of ASC 326 was an increase in the reserve of $406 thousand and the Company recorded a provision of $8 thousand for the twelve months ended December 31, 2023.

Bank Premises and Equipment

Land is carried at cost. Buildings and equipment are carried at cost, less accumulated depreciation computed on the straight-line method over the estimated useful lives of the assets. Estimated useful lives range from 10 to 39 years for buildings and 3 to 10 years for furniture and equipment. Maintenance and repairs of property and equipment are charged to operations and major improvements are capitalized. Upon retirement, sale or other disposition of property and equipment, the cost and accumulated depreciation balances are cleared the differential between the proceeds, if any, and the carrying value is recorded as a gain or loss in the Company's results of operations.

Leases

The Company accounts for its leasing arrangements in accordance with ASC 842 "Leases". Refer to Note 13 for further discussion of the Company's accounting for its leasing arrangements.

Other Real Estate Owned

Assets acquired through, or in lieu of, loan foreclosure are held for sale and are initially recorded at the fair value of the property, less estimated selling costs at the date of foreclosure. Any write-downs based on the asset's fair value at the date of acquisition are charged to the allowance for loan losses. After foreclosure, valuations are periodically performed by management and property held for sale is carried at the lower of the new cost basis or fair value less estimated cost to sell. Impairment losses on property to be held and used are measured as the amount by which the carrying amount of a property exceeds its fair value. Costs of significant property improvements are capitalized, whereas costs relating to holding property are expensed. The portion of interest costs relating to development of real estate is capitalized. Valuations are periodically performed by management, and any subsequent write-downs are recorded as a charge to operations, if necessary, to reduce the carrying value of a property to the lower of its cost or fair value less cost to sell. Revenue and expenses from operations and changes in the valuation allowance are included in the (gain) loss on other real estate owned line item in the consolidated statements of income.

Bank Owned Life Insurance

The Company has purchased life insurance on certain key individuals. Bank owned life insurance is recorded at the amount that may be realized under the insurance contract at the balance sheet date, which is the cash surrender value adjusted for other charges or amounts due that are probable at settlement. These amounts are recorded in noninterest income and are generally not subject to income taxes.

Transfers of Financial Assets

Transfers of financial assets are accounted for as sales when control over the assets has been relinquished. Control over transferred assets is deemed to be surrendered when the assets have been isolated from the Company, the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets, and the Company does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

Loan Swaps

The Company enters into interest rate swaps with certain qualifying commercial loan customers to meet their interest rate risk management needs. The Company simultaneously enters into interest rate swaps with dealer counterparties, with identical notional amounts and offsetting terms. The net result of these interest rate swaps is that the customer pays a fixed rate of interest and the Company receives a floating rate. These back-to-back loan swaps are derivative financial instruments and are reported at fair value in “other assets” and “other liabilities” in the Consolidated Balance Sheets. Changes in the fair value of loan swaps are recorded in other noninterest income and sum to zero because of the offsetting terms of swaps with borrowers and swaps with dealer counterparties.

Retirement Plans

The Company sponsors a 401(k) savings plan under which eligible employees may defer a portion of their compensation on a pretax basis. The Company also provides a match to participants in this plan, as described more fully in Note 11.

Stock-Based Compensation Plan

On May 16, 2023, the Company's shareholders approved the 2023 Stock Incentive Plan which allows key employees and directors to increase their personal financial interest in the Company. The 2023 plan permits the issuance of incentive stock options and non-qualified stock options and the award of common stock, restricted stock, and stock units. The plan authorized the issuance of up to 250,000 shares of common stock. The 2023 Stock Incentive Plan replaced the 2014 Stock Incentive Plan and is discussed more fully in Note 10.

Income Taxes

Deferred income tax assets and liabilities are determined using the liability (or balance sheet) method. Under this method, the net deferred tax asset or liability is determined based on the tax effects of the temporary differences between the book and tax bases of the various assets and liabilities and gives current recognition to changes in tax rates and laws.

When tax returns are filed, it is likely that some positions taken would be sustained upon examination by the applicable taxing authority, while others are subject to uncertainty about the merits of the position taken or the amount of the position that would be ultimately sustained. The benefit of a tax position is recognized in the financial statements in the period during which, based on all available evidence, the Company believes it is "more likely than not" that the position will be sustained upon examination, including the resolution of appeals or litigation processes, if any. Tax positions taken are not offset or aggregated with other positions. Tax positions that meet the "more likely than not" recognition threshold are measured as the largest amount of tax benefit that is more than fifty percent (50%) likely of being realized upon settlement with the applicable taxing authority. The portion of the benefits associated with tax positions taken that exceeds the amount measured as described above is reflected as a liability for unrecognized tax benefits in the balance sheet along with any associated interest and penalties that would be payable to the applicable taxing authority upon examination. Interest and penalties associated with unrecognized tax benefits are classified as additional income taxes in the statement of income. The Company has no uncertain tax positions.

Advertising

The Company follows the policy of charging the costs of advertising to expense as incurred.

Reclassifications

Certain reclassifications have been made to the 2022 financial statements to conform to reporting for 2023. The results of the reclassifications are not considered material and had no effect on prior years' net income or shareholders' equity.

Earnings Per Common Share

Basic earnings per share represents income available to common shareholders divided by the weighted average number of common shares outstanding during the period. Nonvested restricted shares are included in the weighted average number of common shares used to compute basic earnings per share because of dividend participation and voting rights. Diluted earnings per share reflects additional common shares that would have been outstanding if dilutive potential common shares had been issued, as well as any adjustment to income that would result from the assumed issuance. The number of potential common shares is determined using the treasury method.

The following table shows the weighted average number of shares used in computing earnings per share and the effect on the weighted average number of shares of dilutive potential common stock.

	Twelve Months Ended December 31,	
	2023	2022
Average number of common shares outstanding	3,523,547	3,482,368
Effect of dilutive common stock	—	—
Average number of common shares outstanding used to calculate diluted earnings per share	3,523,547	3,482,368

There were no potentially dilutive securities outstanding in 2023 or 2022.

Comprehensive (Loss) Income

Accounting principles generally accepted in the United States of America require that recognized revenue, expenses, gains and losses be included in net income. Certain changes in assets and liabilities, net of income taxes, are reported within the balance sheet as a separate component of shareholders' equity. These changes, along with net income, are components of comprehensive income and are reported in the statement of comprehensive income. In addition to net income, the Company's comprehensive income includes changes in the benefit obligations and plan assets for postretirement benefit plans and unrealized gains or losses on available for sale securities.

Business Segments

The Company operates in three reportable business segments through the Bank: community banking, marine lending and wealth management. The Company's business segments are determined based on the products and services provided, as well as the nature of the related business activities, and they reflect the manner in which financial information is regularly reviewed for the purpose of allocating resources and evaluating performance of the Company's businesses. The results for these business segments are based on management's accounting process, which assigns income statement items and assets to each operating segment. Given the Company's reportable segments are contained within the Bank, management must make certain allocations of expenses, which may not be representative of the costs expected to be incurred if the specific business segments operated as stand-alone entities. For additional information, refer to Note 27. "Business Segments."

Stock Repurchase Program

On June 21, 2023, the Company renewed the stock repurchase program to repurchase up to 150,000 shares of its common stock prior to June 30, 2024. During 2023, the Company purchased 8,531 shares of its Common Stock under its stock repurchase program at an average price of $35.34. During 2022, the Company purchased 4,442 shares of its Common Stock under its stock repurchase program at an average price of $34.79. The maximum number of shares that may yet be purchased under the June 2023 plan as of December 31, 2023 is 145,059.

Recent Accounting Pronouncements and Other Authoritative Guidance

Recently Adopted

In June 2016, the FASB issued Accounting Standards Update ("ASU") 2016-13, "Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments." The ASU, as amended, requires an entity to measure expected credit losses for financial assets carried at amortized cost based on historical experience, current conditions, and reasonable and supportable forecasts. Among other things, the ASU also amended the impairment model for available for sale securities and addressed purchased financial assets with deterioration. ASU 2016-13, as amended, was effective for the Company on January 1, 2023. The adjustment recorded at adoption to the overall allowance for credit losses, which consisted of adjustments to the allowance for credit losses on loans, as well as an adjustment to the Company's reserve for unfunded loan commitments, was $2.5 million. The adjustment, net of tax, recorded to shareholders' equity totaled $2.0 million.

In March 2022, FASB issued ASU No. 2022-02, "Financial Instruments-Credit Losses (Topic 326), Troubled Debt Restructurings and Vintage Disclosures." ASU 2022-02 addresses areas identified by the FASB as part of its post-implementation review of the credit losses standard (ASU 2016-13) that introduced the CECL model. The amendments eliminated the accounting guidance for troubled debt restructurings by creditors that have adopted the CECL model and enhance the disclosure requirements for loan refinancings and restructurings made with borrowers experiencing financial difficulty. In addition, the amendments require a public business entity to disclose current-period gross write-offs for financing receivables and net investment in leases by year of origination in the vintage disclosures. ASU 2022-02 was effective for the Company on January 1, 2023. The amendments in this ASU were applied prospectively, except for the transition method related to the recognition and measurement of TDRs, which was applied using a modified retrospective transition method.

Pending Adoption

In December 2023, the FASB issued ASU 2023-09, "Income Taxes (Topic 740), Improvements to Income Tax Disclosures." The amendments in this ASU require an entity to disclose specific categories in the rate reconciliation and provide additional information for reconciling items that meet a quantitative threshold, which is greater than five percent of the amount computed by multiplying pretax income by the entity's applicable statutory rate, on an annual basis. Additionally, the amendments in this ASU require an entity to disclose the amount of income taxes paid (net of refunds received) disaggregated by federal, state, and foreign taxes and the amount of income taxes paid (net of refunds received) disaggregated by individual jurisdictions that are equal to or greater than five percent of total income taxes paid (net of refunds received). Lastly, the amendments in this ASU require an entity to disclose income (or loss) from continuing operations before income tax expense (or benefit) disaggregated between domestic and foreign and income tax expense (or benefit) from continuing operations disaggregated by federal, state, and foreign. This ASU is effective for annual periods beginning after December 15, 2024. Early adoption is permitted. The amendments should be applied on a prospective basis; however, retrospective application is permitted. The Company does not expect the adoption of ASU 2023-09 to have a material impact on our consolidated financial statements.

In November 2023, the Financial Accounting Standards Board (FASB) issued ASU 2023-07, "Segment Reporting (Topic 280): Improvements to Reportable Segment Disclosures." The amendments in this ASU are intended to improve reportable segment disclosure requirements primarily through enhanced disclosures about significant segment expenses. This ASU requires disclosure of significant segment expenses that are regularly provided to the chief operating decision mark (CODM), an amount for other segment items by reportable segment and a description of its composition, all annual disclosures required by FASB ASU Topic 280 in interim periods as well, and the title and position of the CODM and how the CODM uses the reported measures. Additionally, this ASU requires that at least one of the reported segment profit and loss measures should be the measure that is most consistent with the measurement principles used in an entity's consolidated financial statements. Lastly, this ASU requires public business entities with a single reportable segment to provide all disclosures required by these amendments in this ASU and all existing segment disclosures in Topic 280. This ASU is effective for fiscal years beginning after December 15, 2023, and interim periods within fiscal years beginning after December 15, 2024. Early adoption is permitted. The amendments should be applied retrospectively. The Company does not expect the adoption of ASU 2023-06 to have a material impact on its consolidated financial statements.

In March 2023, the FASB issued ASU 2023-02, "Investments—Equity Method and Joint Ventures (Topic 323): Accounting for Investments in Tax Credit Structures Using the Proportional Amortization Method". These amendments allow reporting entities to elect to account for qualifying tax equity investments using the proportional amortization method, regardless of the program giving rise to the related income tax credits. The ASU is effective for public business entities for fiscal years beginning after December 15, 2023, including interim periods within those fiscal years. Early adoption is permitted for all entities in any interim period. The Company does not expect the adoption of ASU 2023-02 to have a material impact on its consolidated financial statements.

NOTE 2. Securities

On January 1, 2023, the Company adopted ASC 326, which made changes to accounting for available for sale debt securities whereby credit losses should be presented as an allowance, rather than as a write-down when management does not intend to sell and does not believe it is more likely than not they will be required to sell a security prior to the recovery of its amortized cost basis. Should the Company classify debt securities as held-to-maturity in future periods, ASC 326 would also require the Company to measure an expected credit losses under the CECL methodology that would require consideration of a broader range of reasonable and supportable information to inform credit loss estimates. All securities information presented as of December 31, 2023 is in accordance with ASC 326. All securities information presented as of December 31, 2022 or a prior date is presented in accordance with previously applicable GAAP.

Amortized costs and fair values of securities available for sale at December 31, 2023 and 2022 were as follows:

	Amortized Cost		Gross Unrealized Gains		Gross Unrealized (Losses)		Fair Value
	December 31, 2023 (in thousands)						
Obligations of U.S. government corporations and agencies	$	9,258	$	—	$	(667)	$ 8,591
Mortgage-backed securities		140,052		—		(21,230)	118,822
Obligations of states and political subdivisions		6,191		1		(261)	5,931
Subordinated debt		4,750		—		(651)	4,099
	$	160,251	$	1	$	(22,809)	$ 137,443
	December 31, 2022 (in thousands)						
Obligations of U.S. government corporations and agencies	$	9,993	$	—	$	(858)	$ 9,135
Mortgage-backed securities		153,289		—		(24,136)	129,153
Obligations of states and political subdivisions		7,027		2		(422)	6,607
Subordinated debt		4,750		—		(489)	4,261
	$	175,059	$	2	$	(25,905)	$ 149,156

Accrued interest receivable on debt securities available for sale totaled $393 thousand and $431 thousand at December 31, 2023 and 2022, respectively and is included in the other assets line item in the Consolidated Balance Sheets.

Carrying amounts of restricted securities at December 31, 2023 and 2022 were as follows:

	December 31, 2023	December 31, 2022
	(in thousands)	
Federal Reserve Bank Stock	$ 344	$ 944
Federal Home Loan Bank Stock	9,084	8,149
Community Bankers' Bank Stock	140	140
	$ 9,568	$ 9,233

The amortized cost and fair value of securities available for sale at December 31, 2023, by contractual maturity, are shown below. Maturities may differ from contractual maturities primarily in mortgage-backed securities (others could be called) because the mortgages underlying the securities may be called or repaid without any penalties.

	Amortized Cost	Fair Value
	(in thousands)	
Due in one year or less	$ 1,268	$ 1,256
Due after one year through five years	6,114	5,799
Due after five years through ten years	19,434	17,568
Due after ten years	133,435	112,820
	$ 160,251	$ 137,443

During the twelve months ended December 31, 2023, the Company did not sell any available for sale securities. During the twelve months ended December 31, 2022, the Company sold $15.4 million in available for sale securities with gross gains of $6 thousand and gross losses of $743 thousand.

The fair value and gross unrealized losses for securities available for sale, totaled by the length of time that individual securities have been in a continuous unrealized loss position, at December 31, 2023 and 2022 were as follows:

	Less than 12 months		12 months or more		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
	December 31, 2023 (in thousands)					
Obligations of U.S. government corporations and agencies	$ —	$ —	$ 8,591	$ 667	$ 8,591	$ 667
Mortgage-backed securities	—	—	118,822	21,230	118,822	21,230
Obligations of states and political subdivisions	—	—	5,430	261	5,430	261
Subordinated debt	221	29	3,378	622	3,599	651
	$ 221	$ 29	$ 136,221	$ 22,780	$ 136,442	$ 22,809

	Less than 12 months		12 months or more		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
	December 31, 2022 (in thousands)					
Obligations of U.S. government corporations and agencies	$ 6,140	$ 543	$ 2,994	$ 315	$ 9,134	$ 858
Mortgage-backed securities	31,771	4,052	97,382	20,084	129,153	24,136
Obligations of states and political subdivisions	6,065	422	—	—	6,065	422
Subordinated debt	2,431	319	1,080	170	3,511	489
	$ 46,407	$ 5,336	$ 101,456	$ 20,569	$ 147,863	$ 25,905

Gross unrealized losses on available for sale securities included one hundred three (103) and one hundred four (104) debt securities at December 31, 2023 and December 31, 2022, respectively. The Company concluded that a credit loss does not exist in its securities portfolio at December 31, 2023, and no impairment loss has been recognized based on the fact that (1) changes in fair value were caused primarily by fluctuations in interest rates, (2) securities with unrealized losses had generally high credit quality, (3) the Company intends to hold these investments in debt securities to maturity and it is more-likely-than-not that the Company will not be required to sell these investments before a recovery of its investment, and (4) issuers have continued to make timely payments of principal and interest. Additionally, the Company's mortgage-backed securities are entirely issued by either U.S. government agencies or U.S. government-sponsored enterprises. Collectively, these entities provide a guarantee, which is either explicitly or implicitly supported by the full faith and credit of the U.S. government, that investors in such mortgage-backed securities will receive timely principal and interest payments.

Securities having a carrying value of $13.9 million at December 31, 2023 were pledged as security for trust accounts.

NOTE 3. Loans

The composition of loans at December 31, 2023 and 2022 was as follows:

	December 31,	
	2023	2022
	(in thousands)	
Mortgage loans on real estate:		
Construction and & Secured by Farmland	$ 84,145	$ 89,651
HELOCs	47,674	43,588
Residential First Lien - Investor	117,431	111,074
Residential First Lien - Owner Occupied	178,180	125,088
Residential Junior Liens	12,831	11,417
Commercial - Owner Occupied	251,456	232,115
Commercial - Non-Owner Occupied & Multifamily	348,879	315,326
Commercial and industrial loans:		
SBA PPP loans	51	74
Other commercial and industrial loans	107,777	99,571
Marine loans	251,168	230,874
Consumer loans	42,419	44,841
Overdrafts	253	218
Other loans	12,895	12,503
Total loans	$ 1,455,159	$ 1,316,340
Net deferred loan costs and premiums	7,527	7,443
Allowance for credit losses	(14,493)	(11,218)
	$ 1,448,193	$ 1,312,565

At December 31, 2023 and 2022, the Company was servicing loans totaling $7.7 million and $231.7 million, respectively for other financial institutions which are not included in the table above. Also excluded from the table above are net servicing assets of $153 thousand and $684 thousand at December 31, 2023 and 2022, respectively, which are recorded in other assets in the Consolidated Balance Sheets.

On August 23, 2023, the Company completed the sale of certain assets of its marine finance division to an unrelated third-party. Under the Sale Agreements, the Company sold its interest in marine floor plan loans, the servicing rights associated with marine loans that had been sold to outside investors prior to August 23, 2023, and other assets that were not individually significant. Refer to Note 27 for additional information related to this transaction.

NOTE 4. Allowance for Credit Losses on Loans

Changes in the allowance for credit losses for the years ended December 31, 2023 and 2022 were as follows:

	December 31,	
	2023	2022
	(in thousands)	
Balance, beginning	$ 11,218	$ 8,787
Cumulative effect adjustment for adoption of ASC 326	2,077	—
Provision charged to operating expense	1,641	1,830
Recoveries added to the allowance	298	1,260
Credit losses charged to the allowance	(741)	(659)
Balance, ending	$ 14,493	$ 11,218

Nonaccrual and past due loans by class at December 31, 2023 were as follows:

	December 31, 2023 (in thousands)						
	30 - 59 Days Past Due	60 - 89 Days Past Due	90 or More Days Past Due	Total Past Due	Current	Total Loans	90 or More Days Past Due Still Accruing
Mortgage real estate loans:							
Construction & Secured by Farmland	$ —	$ —	$ —	$ —	$ 84,145	$ 84,145	$ —
HELOCs	—	—	—	—	47,674	47,674	—
Residential First Lien - Investor	844	253	—	1,097	116,334	117,431	—
Residential First Lien - Owner Occupied	—	78	149	227	177,953	178,180	—
Residential Junior Liens	—	—	9	9	12,822	12,831	—
Commercial - Owner Occupied	—	—	—	—	251,456	251,456	—
Commercial - Non-Owner Occupied & Multifamily	—	—	—	—	348,879	348,879	—
Commercial and industrial loans:							
SBA PPP loans	—	—	—	—	51	51	—
Other commercial and industrial loans	9	—	26	35	107,742	107,777	14
Marine loans	—	—	552	552	250,616	251,168	—
Consumer loans	173	—	167	340	42,079	42,419	167
Overdrafts	—	—	—	—	253	253	—
Other loans	—	—	—	—	12,895	12,895	—
Total	$ 1,026	$ 331	$ 903	$ 2,260	$ 1,452,899	$ 1,455,159	$ 181

	December 31, 2023 (in thousands)		
	Nonaccruals with No Allowance for Credit Losses	Nonaccrual with an Allowance for Credit Losses	Nonaccrual Loans
Mortgage real estate loans:			
Construction & Secured by Farmland	$ 95	$ —	$ 95
HELOCs	15	—	15
Residential First Lien - Investor	1,085	—	1,085
Residential First Lien - Owner Occupied	228	—	228
Residential Junior Liens	11	—	11
Commercial - Owner Occupied	22	—	22
Commercial - Non-Owner Occupied & Multifamily	3,625	—	3,625
Commercial and industrial loans:			
SBA PPP loans	—	—	—
Other commercial and industrial loans	12	—	12
Marine loans	552	—	552
Consumer loans	—	—	—
Overdrafts	—	—	—
Other loans	—	—	—
Total	$ 5,645	$ —	$ 5,645

Nonaccrual and past due loans by class at December 31, 2022 were as follows:

	December 31, 2022 (in thousands)							
	30 - 59 Days Past Due	**60 - 89 Days Past Due**	**90 or More Days Past Due**	**Total Past Due**	**Current**	**Total Loans**	**90 or More Past Due Still Accruing**	**Nonaccrual Loans**
Mortgage real estate loans:								
Construction & Secured by Farmland	$ —	$ —	$ 101	$ 101	$ 89,550	$ 89,651	$ —	$ 397
HELOCs	149	—	—	149	43,439	43,588	—	155
Residential First Lien - Investor	—	—	—	—	111,074	111,074	—	—
Residential First Lien - Owner Occupied	222	—	39	261	124,827	125,088	—	175
Residential Junior Liens	—	—	—	—	11,417	11,417	—	6
Commercial - Owner Occupied	—	—	—	—	232,115	232,115	—	—
Commercial - Non-Owner Occupied & Multifamily	—	—	—	—	315,326	315,326	—	1,356
Commercial and industrial loans:								
SBA PPP loans	—	—	—	—	74	74	—	—
Other commercial and industrial loans	15	—	73	88	99,483	99,571	—	73
Marine loans	—	—	—	—	230,874	230,874	—	—
Consumer loans	56	—	318	374	44,467	44,841	318	—
Overdrafts	—	—	—	—	218	218	—	—
Other loans	—	—	—	—	12,503	12,503	—	—
Total	$ 442	$ —	$ 531	$ 973	$1,315,367	$ 1,316,340	$ 318	$ 2,162

Allowance for credit losses by segment as of and for the years ended December 31, 2023 and December 31, 2022 were as follows:

	December 31, 2023 (in thousands)								
	Construction and Farmland	Residential Real Estate	Commercial Real Estate & Multi Family	Commercial	Marine	Consumer	All Other Loans	Unallocated	Total
Allowance for credit losses:									
Beginning Balance	$ 2,714	$ 1,735	$ 2,221	$ 2,222	$ 1,555	$ 299	$ 472	$ —	$ 11,218
Cumulative effect adjustment for adoption of ASC 326	(1,840)	1,933	3,584	(1,102)	(285)	(123)	(90)	—	2,077
Charge-Offs	—	—	—	(312)	(126)	(121)	(182)	—	(741)
Recoveries	8	18	—	43	—	48	181	—	298
Provision	(110)	1,039	419	176	9	95	13	—	1,641
Ending balance	$ 772	$ 4,725	$ 6,224	$ 1,027	$ 1,153	$ 198	$ 394	$ —	$ 14,493
Ending balance: Individually evaluated	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —
Ending balance: collectively evaluated	$ 772	$ 4,725	$ 6,224	$ 1,027	$ 1,153	$ 198	$ 394	$ —	$ 14,493
Loans:									
Ending balance	$ 84,145	$ 356,116	$ 600,335	$ 107,828	$ 251,168	$ 42,419	$ 13,148	$ —	$ 1,455,159
Ending balance individually evaluated	$ 95	$ 1,288	$ 3,639	$ —	$ 552	$ —	$ —	$ —	$ 5,574
Ending balance collectively evaluated	$ 84,050	$ 354,828	$ 596,696	$ 107,828	$ 250,616	$ 42,419	$ 13,148	$ —	$ 1,449,585

	December 31, 2022 (in thousands)								
	Construction and Farmland	Residential Real Estate	Commercial Real Estate & Multi Family	Commercial	Marine	Consumer	All Other Loans	Unallocated	Total
Allowance for credit losses:									
Beginning Balance	$ 2,794	$ 1,671	$ 1,729	$ 1,294	$ 789	$ 219	$ 291	$ —	$ 8,787
Charge-Offs	—	(9)	—	(300)	—	(79)	(271)	—	(659)
Recoveries	9	888	197	109	—	44	13	—	1,260
Provision	(89)	(815)	295	1,119	766	115	439	—	1,830
Ending balance	$ 2,714	$ 1,735	$ 2,221	$ 2,222	$ 1,555	$ 299	$ 472	$ —	$ 11,218
Ending balance: Individually evaluated for impairment	$ —	$ 27	$ —	$ 73	$ —	$ —	$ —	$ —	$ 100
Ending balance: collectively evaluated for impairment	$ 2,714	$ 1,708	$ 2,221	$ 2,149	$ 1,555	$ 299	$ 472	$ —	$ 11,118
Loans:									
Ending balance	$ 89,651	$ 291,167	$ 547,441	$ 99,645	$ 230,874	$ 44,841	$ 12,721	$ —	$ 1,316,340
Ending balance individually evaluated for impairment	$ 1,044	$ 3,719	$ 1,695	$ 141	$ —	$ 22	$ —	$ —	$ 6,621
Ending balance collectively evaluated for impairment	$ 88,607	$ 287,448	$ 545,746	$ 99,504	$ 230,874	$ 44,819	$ 12,721	$ —	$ 1,309,719

The following table presents the amortized cost basis of collateral-dependent loans by loan portfolio segment:

	December 31, 2023 (in thousands)		
(in thousands)	Real Estate Collateral	Other Collateral	Total
Mortgage real estate loans:			
Construction & Secured by Farmland	$ 95	$ —	$ 95
HELOCs	—	—	—
Residential First Lien - Investor	1,086	—	1,086
Residential First Lien - Owner Occupied	194	—	194
Residential Junior Liens	8	—	8
Commercial - Owner Occupied	14	—	14
Commercial - Non-Owner Occupied & Multifamily	3,625	—	3,625
Commercial and industrial loans:			
SBA PPP loans	—	—	—
Other commercial and industrial loans	—	—	—
Marine loans	—	552	552
Consumer loans	—	—	—
Overdrafts	—	—	—
Other loans	—	—	—
	$ 5,022	$ 552	$ 5,574

The Company did not identify any significant changes in the extent to which collateral secures its collateral dependent loans, whether in the form of general deterioration or from other factors during the period ended December 31, 2023.

The Company 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, public information, and current economic trends, among other factors. The Company analyzes loans individually to classify the loans as to credit risk. This analysis is performed on a quarterly basis. The following table presents risk ratings by loan portfolio segment and origination year (for 2023 only). Descriptions of these ratings are as follows:

Pass — Pass loans exhibit acceptable history of profits, cash flow ability and liquidity. Sufficient cash flow exists to service the loan. All obligations have been paid by the borrower in an as agreed manner.

Special Mention — Special mention loans exhibit negative trends and potential weakness that, if left uncorrected, may negatively affect the borrower's ability to repay its obligations. The risk of default is not imminent and the borrower still demonstrates sufficient financial strength to service debt.

Classified — Classified loans include loans rated Substandard, Doubtful and Loss.

- Substandard loans exhibit well defined weaknesses resulting in a higher probability of default. The borrowers exhibit adverse financial trends and a diminishing ability or willingness to service debt.
- Doubtful loans exhibit all of the characteristics inherent in substandard loans; however given the severity of weaknesses, the collection of 100% of the principal is unlikely under current conditions.
- Loss loans are considered uncollectible over a reasonable period of time and of such little value that its continuance as a bankable asset is not warranted.

Credit quality information by class at December 31, 2023 and December 31, 2022 was as follows:

	December 31, 2023								
	Term Loan Amortized Cost Basis by Origination Year								
(in thousands)	2023	2022	2021	2020	2019	Prior	Revolving Loans Amortized Cost Basis	Revolving Loans Converted to Term	Total
Mortgage real estate loans:									
Construction & Secured by Farmland									
Pass	$ 34,617	$ 21,460	$ 7,584	$ 4,851	$ 2,389	$ 2,829	$ 7,052	$ 57	$ 80,839
Special Mention	—	1,173	—	—	1,040	815	—	—	3,028
Classified	—	—	—	145	—	133	—	—	278
Total	$ 34,617	$ 22,633	$ 7,584	$ 4,996	$ 3,429	$ 3,777	$ 7,052	$ 57	$ 84,145
Current period gross charge-offs	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —
HELOCs									
Pass	$ —	$ —	$ —	$ —	$ —	$ —	$ 47,610	$ —	$ 47,610
Special Mention	—	—	—	—	—	—	49	—	49
Classified	—	—	—	—	—	—	15	—	15
Total	$ —	$ —	$ —	$ —	$ —	$ —	$ 47,674	$ —	$ 47,674
Current period gross charge-offs	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —
Residential First Lien - Investor									
Pass	$ 19,394	$ 23,205	$ 31,371	$ 10,667	$ 4,054	$ 22,265	$ —	$ 367	$ 111,323
Special Mention	—	1,273	—	1,180	626	1,944	—	—	5,023
Classified	—	—	1,085	—	—	—	—	—	1,085
Total	$ 19,394	$ 24,478	$ 32,456	$ 11,847	$ 4,680	$ 24,209	$ —	$ 367	$ 117,431
Current period gross charge-offs	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —
Residential First Lien - Owner Occupied									
Pass	$ 59,007	$ 33,793	$ 23,749	$ 35,783	$ 3,932	$ 20,413	$ —	$ 589	$ 177,266
Special Mention	—	—	—	—	—	258	—	—	258
Classified	—	—	—	—	—	656	—	—	656
Total	$ 59,007	$ 33,793	$ 23,749	$ 35,783	$ 3,932	$ 21,327	$ —	$ 589	$ 178,180
Current period gross charge-offs	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —
Residential Junior Liens									
Pass	$ 2,562	$ 2,902	$ 3,429	$ 1,486	$ 606	$ 1,613	$ —	$ 189	$ 12,787
Special Mention	—	—	—	—	—	—	—	—	—
Classified	—	—	—	—	—	27	—	17	44
Total	$ 2,562	$ 2,902	$ 3,429	$ 1,486	$ 606	$ 1,640	$ —	$ 206	$ 12,831
Current period gross charge-offs	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —
Commercial - Owner Occupied									
Pass	$ 36,736	$ 68,868	$ 40,707	$ 22,871	$ 13,971	$ 50,059	$ 3,088	$ 4,364	$ 240,664
Special Mention	—	3,817	64	2,145	1,877	1,402	—	—	9,305
Classified	—	—	967	498	—	8	—	14	1,487
Total	$ 36,736	$ 72,685	$ 41,738	$ 25,514	$ 15,848	$ 51,469	$ 3,088	$ 4,378	$ 251,456
Current period gross charge-offs	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —
Commercial - Non-Owner Occupied & Multifamily									
Pass	$ 56,510	$ 88,518	$ 64,005	$ 65,075	$ 15,563	$ 34,619	$ 1,196	$ 5,651	$ 331,137
Special Mention	624	4,748	3,685	5,060	—	—	—	—	14,117
Classified	—	—	—	2,355	—	1,270	—	—	3,625
Total	$ 57,134	$ 93,266	$ 67,690	$ 72,490	$ 15,563	$ 35,889	$ 1,196	$ 5,651	$ 348,879
Current period gross charge-offs	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —
Commercial and industrial loans:									
SBA PPP loans									
Pass	$ —	$ —	$ 51	$ —	$ —	$ —	$ —	$ —	$ 51
Special Mention	—	—	—	—	—	—	—	—	—
Classified	—	—	—	—	—	—	—	—	—
Total	$ —	$ —	$ 51	$ —	$ —	$ —	$ —	$ —	$ 51

(in thousands)	December 31, 2023								
	Term Loan Amortized Cost Basis by Origination Year								
	2023	2022	2021	2020	2019	Prior	Revolving Loans Amortized Cost Basis	Revolving Loans Converted to Term	Total
Current period gross charge-offs	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —
Other commercial and industrial loans									
Pass	$ 15,052	$ 26,798	$ 8,659	$ 4,824	$ 2,629	$ 3,898	$ 43,188	$ 1,005	$ 106,053
Special Mention	1,125	—	—	13	1	9	220	344	1,712
Classified	—	—	—	3	—	—	9	—	12
Total	$ 16,177	$ 26,798	$ 8,659	$ 4,840	$ 2,630	$ 3,907	$ 43,417	$ 1,349	$ 107,777
Current period gross charge-offs	$ 231	$ 81	$ —	$ —	$ —	$ —	$ —	$ —	$ 312
Marine loans									
Pass	$ 86,001	$ 128,456	$ 35,492	$ 667	$ —	$ —	$ —	$ —	$ 250,616
Special Mention	—	—	—	—	—	—	—	—	—
Classified	367	185	—	—	—	—	—	—	552
Total	$ 86,368	$ 128,641	$ 35,492	$ 667	$ —	$ —	$ —	$ —	$ 251,168
Current period gross charge-offs	$ —	$ 126	$ —	$ —	$ —	$ —	$ —	$ —	$ 126
Consumer loans									
Pass	$ 3,427	$ 13,950	$ 6,205	$ 8,687	$ 1,747	$ 21	$ 8,354	$ 28	$ 42,419
Special Mention	—	—	—	—	—	—	—	—	—
Classified	—	—	—	—	—	—	—	—	—
Total	$ 3,427	$ 13,950	$ 6,205	$ 8,687	$ 1,747	$ 21	$ 8,354	$ 28	$ 42,419
Current period gross charge-offs	$ —	$ 3	$ —	$ 66	$ —	$ —	$ 52	$ —	$ 121
Overdrafts									
Pass	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —
Special Mention	—	—	—	—	—	—	—	—	—
Classified	253	—	—	—	—	—	—	—	253
Total	$ 253	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ 253
Current period gross charge-offs	$ 182	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ 182
Other loans									
Pass	$ 69	$ 10,176	$ —	$ —	$ —	$ 2,587	$ 55	$ 8	$ 12,895
Special Mention	—	—	—	—	—	—	—	—	—
Classified	—	—	—	—	—	—	—	—	—
Total	$ 69	$ 10,176	$ —	$ —	$ —	$ 2,587	$ 55	$ 8	$ 12,895
Current period gross charge-offs	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —
Total by Risk Category									
Pass	$ 313,375	$ 418,126	$ 221,252	$ 154,911	$ 44,891	$ 138,304	$ 110,543	$ 12,258	$ 1,413,660
Special Mention	1,749	11,011	3,749	8,398	3,544	4,428	269	344	33,492
Classified	620	185	2,052	3,001	—	2,094	24	31	8,007
Total	$ 315,744	$ 429,322	$ 227,053	$ 166,310	$ 48,435	$ 144,826	$ 110,836	$ 12,633	$ 1,455,159
Total current period gross charge-offs	$ 413	$ 210	$ —	$ 66	$ —	$ —	$ 52	$ —	$ 741

INTERNAL RISK RATING GRADES	As of December 31, 2022 (in thousands) Pass	Special Mention	Substandard	Doubtful	Loss	Total
Commercial - Non Real Estate:						
Commercial & Industrial	$ 247,061	$ 526	$ 72	$ —	$ —	$ 247,659
Commercial Real Estate:						
Owner Occupied	212,074	20,020	21	—	—	232,115
Non-owner occupied	257,625	16,189	1,706	—	—	275,520
Construction and Farmland:						
Residential	11,235	—	21	—	—	11,256
Commercial	69,427	153	8,815	—	—	78,395
Residential:						
Equity Lines	43,124	310	154	—	—	43,588
Single family	251,247	5,972	951	—	—	258,170
Multifamily	39,806	—	—	—	—	39,806
All other loans	12,721	—	—	—	—	12,721
Total	$1,144,320	$ 43,170	$ 11,740	$ —	$ —	$ 1,199,230

	Performing	Nonperforming
Consumer Credit Exposure by Payment Activity	$ 116,908	$ 202

NOTE 5. Restructurings for Borrowers Experiencing Financial Difficulty

The Company adopted the amendments in ASU 2022-02, which eliminated accounting guidance on TDR loans for creditors and requires enhanced disclosures for loan modifications to borrowers experiencing financial difficulty that we made on or after January 1, 2023.

The following table presents the amortized cost of loans that were modified during the twelve months ended December 31, 2023 by loan portfolio segment:

	Twelve Months Ended December 31, 2023 (in thousands) Term Extension	Total	% of Total Class of Loans
Mortgage real estate loans:			
Residential First Lien - Owner Occupied	$ 355	$ 355	0.20%
Total	$ 355	$ 355	

None of the loans that were modified defaulted during the twelve months ended December 31, 2023 and the loans remained current with contractual payments as of December 31, 2023. The financial effects of the term extensions during the period added a weighted average of 1.0 years to the life of loans which reduced the payment amounts for the borrowers.

Prior to the adoption of ASU 2022-02, the Company accounted for a modification to the contractual terms of a loan that resulted in granting a concession to a borrower experiencing financial difficulties as a TDR.

There were twenty eight (28) troubled debt restructured loans totaling $4.6 million at December 31, 2022. Two loans, totaling $133 thousand, were in nonaccrual status at December 31, 2022.

The following tables set forth information on the Company's troubled debt restructurings by class of loans occurring during the year ended December 31, 2022:

	Number of Contracts	Twelve Months Ended December 31, 2022 (in thousands) Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Commercial - Non Real Estate:			
Commercial & Industrial			
Commercial Real Estate			
Owner Occupied	1	$ 185	$ 185
Non-owner occupied	1	161	161
Construction and Farmland			
Commercial	1	639	639
Consumer:			
Installment	1	20	21
Residential			
Equity			
Single family	9	1,676	1,704
Total	13	$ 2,681	$ 2,710

During the twelve months ended December 31, 2022, the Company restructured thirteen loans by granting a concession to the borrowers experiencing financial difficulty. The Company restructured one commercial real estate owner occupied loan by granting a refinance with new terms. The Company restructured one commercial real estate non-owner occupied loan with a twelve month renewal and rate change. The Company restructured one installment loan by granting a refinance with extended terms. The Company restructured one construction and farmland commercial loan by granting a refinance with new terms. The Company restructured nine residential single family loans by granting twelve month renewals and a rate change.

There were no payment defaults during the twelve months ended December 31, 2022 for TDRs that were restructured within the preceding twelve-month period.

Management defines default as over 30 days contractually past due under the modified terms, the foreclosure and/or repossession of the collateral, or the charge-off of the loan.

NOTE 6. Bank Premises and Equipment, Net

The major classes of bank premises and equipment and the total accumulated depreciation at December 31, 2023 and 2022 were as follows:

	December 31, 2023	2022
	(in thousands)	
Land	$ 6,644	$ 6,644
Buildings and improvements	19,247	18,649
Furniture and equipment	9,729	9,345
	$ 35,620	$ 34,638
Less accumulated depreciation	17,512	16,574
Bank premises and equipment, net	$ 18,108	$ 18,064

Depreciation expense on buildings and improvements was $498 thousand and $486 thousand for the years ended 2023 and 2022, respectively. Depreciation expense on furniture and equipment was $504 thousand and $493 thousand for the years ended 2023 and 2022, respectively.

NOTE 7. Deposits

The composition of deposits at December 31, 2023 and December 31, 2022 was as follows:

	December 31, 2023	December 31, 2022
	(in thousands)	
Noninterest bearing demand deposits	$ 436,619	$ 478,750
Savings and interest bearing demand deposits:		
NOW accounts	$ 253,353	$ 189,144
Money market accounts	263,633	265,290
Regular savings accounts	139,453	172,997
	$ 656,439	$ 627,431
Time deposits:		
Balances of less than $250,000	$ 257,418	$ 87,531
Balances of $250,000 or greater	155,846	70,363
	$ 413,264	$ 157,894
	$ 1,506,322	$ 1,264,075

Savings and interest bearing demand deposits included $115.7 million and $59.5 million in reciprocal deposits at December 31, 2023 and 2022, respectively. Time deposits with balances of less than $250,000 included $30.1 million and $4.6 million in brokered certificates of deposit at December 31, 2023 and 2022, respectively.

The outstanding balance of time deposits at December 31, 2023 was due as follows:

	December 31, 2023
	(in thousands)
2024	$ 402,814
2025	5,019
2026	2,450
2027	1,844
2028	327
Thereafter	810
	$ 413,264

Deposit overdrafts reclassified as loans totaled $253 thousand and $218 thousand at December 31, 2023 and 2022, respectively.

NOTE 8. Borrowings

The Company has borrowings in the form of federal funds purchased, Federal Home Loan Bank of Atlanta ("FHLB") advances and subordinated notes.

The following table presents selected information on short-term borrowings for the years ended December 31, 2023 and 2022, consisting of FHLB advances and federal funds purchased.

	December 31,	
	2023	2022
	(dollars in thousands)	
Balance at year-end	$ 20,000	$ 207,980
Average balance during the year	$ 45,801	$ 47,470
Average interest rate during the year	4.68%	3.09%
Maximum month-end balance during the year	$ 150,000	$ 207,980

At December 31, 2023 and 2022, the Company's short-term FHLB advances totaled $20.0 million and $175.0 million, respectively, and federal funds purchased totaled $0 and $33.0 million, respectively.

The Company's long-term borrowings with the FHLB were $145.0 million and $0 at December 31, 2023 and 2022, respectively.

Federal fund lines of credit are extended to the Bank by nonaffiliated banks with which a correspondent banking relationship exists. The line of credit amount is determined by the creditworthiness of the Bank and, in particular, its regulatory capital ratios, which are discussed in Note 15. Federal funds purchased generally mature each business day. At December 31, 2023 these available lines totaled $78.0 million.

The Company had $115.6 million in irrevocable letters of credit at December 31, 2023 with the FHLB to secure public deposits.

As of December 31, 2023, Company had remaining credit availability in the amount of $169.6 million with the FHLB. This line may be utilized for short and/or long-term borrowing. Advances on the line are secured by all of the Company's eligible first lien residential real estate loans on one-to-four-unit, single-family dwellings; multi-family dwellings; home equity lines of credit; and commercial real estate loans. The amount of the available credit is limited to a percentage of the estimated market value of the loans as determined periodically by the FHLB. The amount of the available credit is also limited to 20% of total Bank assets.

On March 31, 2022, the Company entered into Subordinated Note Purchase Agreements with certain purchasers pursuant to which the Company issued and sold $30.0 million in aggregate principal amount of its 4.50% Fixed-to-Floating Rate Subordinated Notes due April 1, 2032 (the "Notes"). The net proceeds of the Notes were used for general corporate purposes, organic growth and to support the Bank's regulatory capital ratios.

The Notes were structured to qualify as Tier 2 capital for regulatory capital purposes at the holding company and bear an initial interest rate of 4.50% until April 1, 2027, with interest during this period payable semi-annually in arrears. From and including April 1, 2027, but excluding the maturity date or early redemption date, the interest rate will reset quarterly to an annual floating rate equal to three-month SOFR, plus 2.35% with interest during the period payable quarterly in arrears. The Notes are redeemable by the Company at its option, in whole or in part, on or after April 1, 2027. Initial debt issuance costs were $673 thousand. The debt balance of $30.0 million is presented net of unamortized issuance costs of $556 thousand and $623 thousand at December 31, 2023 and 2022, respectively.

NOTE 9. Income Taxes

The Company files income tax returns with the United States of America, the Commonwealth of Virginia and West Virginia. With few exceptions, the Company is no longer subject to federal, state, or local income tax examinations for years prior to 2020.

The net deferred tax asset at December 31, 2023 and 2022 consisted of the following components:

	December 31,	
	2023	2022
	(in thousands)	
Deferred tax assets:		
Allowance for credit losses	$ 3,043	$ 2,342
Reserve for unfunded commitments	101	14
Share-based compensation	327	222
Accrued postretirement benefits	18	21
Home equity origination costs	85	81
Accrued incentive benefit	89	—
Nonaccrual interest	75	48
Lease liabilities	977	1,045
Credit carryforward	1,689	648
Securities available for sale	4,790	5,440
Other	25	26
	$ 11,219	$ 9,887
Deferred tax liabilities:		
Property and equipment	$ 853	$ 710
Right-of-use assets	921	1,001
Loan servicing rights	32	144
	$ 1,806	$ 1,855
Net deferred tax asset	$ 9,413	$ 8,032

The Company has not recorded a valuation allowance for deferred tax assets because management believes that it is more likely than not that they will be ultimately realized.

Income tax expense for the years ended December 31, 2023 and 2022 consisted of the following components:

	December 31,	
	2023	2022
	(in thousands)	
Current tax expense	$ 2,785	$ 3,236
Deferred tax (benefit)	(1,509)	(86)
	$ 1,276	$ 3,150

The following table reconciles income tax expense to the statutory federal corporate income tax amount, which was calculated by applying the federal corporate income tax rate to pre-tax income for the years ended December 31, 2023 and 2022.

	December 31,	
	2023	2022
	(in thousands)	
Statutory federal corporate tax amount	$ 2,232	$ 3,711
Tax-exempt interest (income)	(76)	(81)
Officer insurance (income)	(134)	(131)
Net tax credits	(756)	(353)
Other, net	10	4
	$ 1,276	$ 3,150

The effective tax rates were 12.00% and 17.83% for years ended December 31, 2023 and 2022, respectively. The effective tax rates were impacted by tax credits on qualified affordable housing project investments as discussed in Note 25 to the Consolidated Financial Statements as well as qualified rehabilitation credits.

NOTE 10. Stock-Based Compensation

On May 16, 2023, the Company's shareholders approved the 2023 Stock Incentive Plan ("the 2023 Plan") which allows key employees and directors to increase their personal financial interest in the Company. The 2023 Plan permits the issuance of incentive stock options and non-qualified stock options and the award of common stock, restricted stock, and stock units. The plan authorizes the issuance of up to 250,000 shares of common stock. The 2023 Plan replaced the 2014 Stock Incentive Plan. To date, equity awards have only been issued in the form of restricted stock.

The Company periodically grants restricted stock to its directors, executive officers and certain non-executive officers. Restricted stock provides grantees with rights to shares of common stock upon completion of a service period or achievement of Company performance measures. During the restriction period, all shares are considered outstanding and dividends are paid to the grantee. Outside directors are periodically granted restricted shares which, beginning in 2023, vest over a period of one year. Prior to 2023 the vesting period for outside directors was typically less than nine months. Executive officers have been granted restricted shares which vest over a three year service period and restricted shares which vest based on meeting performance measures over a two year period. Certain non-executive officers also were granted restricted shares which vest over a three year service period.

The following table presents the activity for restricted stock awards for the years ended December 31, 2023 and 2022:

	Twelve Months Ended December 31,			
	2023		2022	
	Shares	Weighted Average Grant Date Fair Value	Shares	Weighted Average Grant Date Fair Value
Nonvested, beginning of period	38,780	$ 33.47	31,738	$ 30.70
Granted	37,941	35.79	31,648	35.19
Vested	(17,402)	33.26	(23,079)	32.11
Forfeited	(2,405)	35.40	(1,527)	32.13
Nonvested, end of period	56,914	$ 35.06	38,780	$ 33.47

The Company recognizes compensation expense over the vesting period based on the fair value of the Company's stock on the grant date. Compensation expense was $1.2 million and $1.0 million during December 31, 2023 and 2022, respectively. The total grant date fair value of restricted stock which vested was $579 thousand and $741 thousand for the years ended December 31, 2023 and 2022, respectively. The total vest date fair value of restricted stock which vested was $609 thousand and $819 thousand for the years ended December 31, 2023 and 2022, respectively. Unrecognized compensation cost related to unvested restricted stock was $456 thousand at December 31, 2023. This amount is expected to be recognized over a weighted average period of two years. The Company's policy is to recognize forfeitures as they occur.

NOTE 11. Employee Benefits

The Company sponsors a 401(k) savings plan under which eligible employees may defer a portion of salary on a pretax basis, subject to certain IRS limits. The Company matches 50 percent of employee contributions, on a maximum of six percent of salary deferred. The 401(k) plan includes a non-elective safe-harbor employer contribution and an age-weighted employer contribution. Qualifying employees receive non-elective safe-harbor contributions equal to three percent of their salary. Company match and safe-harbor contributions are contributed each pay period. Qualifying employees will receive an additional annual contribution based on their age and years of service. The percentage of salary for the age-weighted contribution increases on both factors, age and years of service, with a minimum of one percent of salary and a maximum of ten percent of salary. Contributions under the plan amounted to $2.2 million in 2023 and $1.9 million in 2022.

The Company has established an Executive Supplemental Income Plan for certain key employees. Benefits are to be paid in monthly installments following retirement or death. The agreement provides that if employment is terminated for reasons other than death or disability prior to age 65, the amount of benefits could be reduced or forfeited. The executive supplemental income benefit liability was $4 thousand and $8 thousand at December 31, 2023 and 2022, respectively. The executive supplemental income benefit expense, based on the present value of the retirement benefits, was $29 thousand in 2023 and 2022. The plan is unfunded; however, life insurance has been acquired on the lives of these employees in amounts sufficient to discharge the plan's obligations.

The Company's Employee Stock Ownership Plan ("ESOP") was terminated during the second quarter of 2023 and, as of December 31, 2023, all plan assets have been disbursed. As part of the termination process, and as required by applicable law, participants were offered the opportunity to direct the Company to repurchase shares of Company stock distributed from the ESOP. A total of 3,772 shares were repurchased and 91,505 shares moved to participant accounts. There were no contributions in 2023 and 2022.

NOTE 12. Commitments and Contingencies

In the normal course of business, the Company makes various commitments and incurs certain contingent liabilities, which are not reflected in the accompanying financial statements. These commitments and contingent liabilities include various guarantees, commitments to extend credit and standby letters of credit. The Company does not anticipate any material losses as a result of these commitments.

During the normal course of business, various legal claims arise from time to time which, in the opinion of management, will have no material effect on the Company's consolidated financial statements.

The Bank was required to maintain a total compensating balance on deposit with two correspondent banks in the amount of $250 thousand at December 31, 2023 and 2022.

See Note 18 with respect to financial instruments with off-balance-sheet risk.

NOTE 13. Leases

The Company leases certain office properties and equipment used in its operations in the normal course of business. Leases greater than 12 months in duration are recorded in the consolidated balance sheets at the lease commencement date and are classified as either operating or finance leases based on the Company's assessment of the underlying agreement.

Lease liabilities represent the Company's obligation to make lease payments and are presented at each reporting date as the net present value of the remaining contractual cash flows. Cash flows are discounted at the Company's incremental borrowing rate in effect at the commencement date of the lease. Right-of-use assets represent the Company's right to use the underlying asset for the lease term and are calculated as the sum of the lease liability and if applicable, prepaid rent, initial direct costs and any incentives received from the lessor.

The Company's four long-term lease agreements for office properties are all classified as operating leases. These leases offer the option to extend the lease term and the Company has included such extensions in its calculation of the lease liability to the extent the options are reasonably certain of being exercised. These lease agreements do not provide for residual value guarantees and have no restrictions or covenants that would impact dividends or require incurring additional financial obligations. Right-of-use assets and leases liabilities are included in other assets and other liabilities, respectively, in the Consolidated Balance Sheets.

The following tables present information about the Company's leases:

(dollars in thousands)	December 31, 2023	December 31, 2022
Lease liability	$ 4,653	$ 4,978
Right-of-use asset	$ 4,387	$ 4,766
Weighted average remaining lease term	14 years	14 years
Weighted average discount term	3.09 %	3.04 %

Lease Cost	Twelve Months Ended December 31, 2023	Twelve Months Ended December 31, 2022
Operating lease cost	$ 528	$ 528
Variable lease cost	—	—
Short-term lease cost	14	15
Total lease cost	$ 542	$ 543
Cash paid for amounts included in the measurement of lease liabilities	$ 473	$ 466

A maturity analysis of operating lease liabilities and reconciliation of the undiscounted cash flows to the total operating lease liabilities is as follows:

Lease payments due	As of December 31, 2023
Twelve months ending December 31, 2024	$ 480
Twelve months ending December 31, 2025	504
Twelve months ending December 31, 2026	397
Twelve months ending December 31, 2027	391
Twelve months ending December 31, 2028	395
Thereafter	3,754
Total undiscounted cash flows	$ 5,921
Discount	(1,268)
Lease liability	$ 4,653

NOTE 14. Transactions with Directors and Officers

The Bank grants loans to and accepts deposits from its directors, principal officers and related parties of such persons during the ordinary course of business. The aggregate balance of loans to directors, principal officers and their related parties was $5.0 million and $5.1 million at December 31, 2023 and 2022, respectively. These balances reflect total principal additions of $544 thousand and total principal payments of $689 thousand, during 2023. The aggregate balance of deposits from directors, principal officers and their related parties was $7.0 million and $11.1 million at December 31, 2023 and 2022, respectively.

NOTE 15. Capital Requirements

The Bank is subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of their assets, liabilities, and certain off-balance-sheet items as calculated under regulatory accounting practices. The capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

In 2019, the federal banking agencies jointly issued a final rule that provided for an optional, simplified measure of capital adequacy, the Community Bank Leverage Ratio framework (CBLR), for qualifying community banking organizations, consistent with Section 201 of the Economic Growth, Regulatory Relief, and Consumer Protection Act. The final rule became effective on January 1, 2020. The CBLR removed the requirement for qualifying banking organizations to calculate and report risk-based capital but rather only requires a Tier 1 to average assets (leverage) ratio. Qualifying banking organizations that elect to use the CBLR and that maintain a leverage ratio of greater than the required minimum will be considered to have satisfied the generally applicable risk-based and leverage capital requirements in the agencies' capital rules and, if applicable, will be considered to have met the well-capitalized ratio requirements for purposes of section 38 of the Federal Deposit Insurance Act. Under the regulatory capital rules, an institution electing to use the CBLR must maintain a minimum leverage ratio of 9%. Qualifying institutions are allowed a two-quarter grace period to correct a ratio that falls below the required amount, provided the institution maintains a ratio of more than 8%. At December 31, 2022, the Bank was a qualifying institution and elected to utilize the CBLR to measure capital adequacy. As such, the related amounts and ratios for December 31, 2022, are presented below using the CLBR. The Bank entered the CLBR two-quarter grace period on June 30, 2023, having fallen below the minimum ratio of 9%, and at December 31, 2023 its leverage ratio was 8.48%. Therefore, the amounts and ratios at December 31, 2023 are presented using the risk-based capital framework and not the CLBR.

At December 31, 2023, and 2022, management believes the Bank met all capital adequacy requirements to which it was subject. Additionally, at December 31, 2023, the most recent notification from the Federal Reserve categorized the Bank as well-capitalized under the regulatory framework for prompt corrective action. There are no conditions or events since the notification that management believes have changed the Bank's category.

The following table presents the Bank's actual capital amounts and ratios at December 31, 2023 and 2022:

	Actual		Minimum Capital Requirement		Minimum To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
			(dollars in thousands)			
December 31, 2023						
Common Equity Tier 1 Capital to Risk Weighted Assets	$ 155,453	10.27%	$ 68,121	4.50%	$ 98,397	6.50%
Total Capital to Risk Weighted Assets	168,925	11.16%	121,104	8.00%	151,380	10.00%
Tier 1 Capital to Risk Weighted Assets	155,453	10.27%	90,828	6.00%	121,104	8.00%
Tier 1 Capital to Average Assets	155,453	8.48%	73,367	4.00%	91,709	5.00%
December 31, 2022						
Tier 1 Capital to Average Assets	142,530	9.15%	n/a	n/a	140,210	9.00%

In addition to the minimum regulatory capital required for capital adequacy purposes under the risk-based capital framework, financial institutions also required to maintain a minimum capital conservation buffer of greater than 2.5% in order to avoid restrictions on capital distributions and other payments. At December 31, 2023, the Bank's capital levels exceeded the minimum regulatory capital requirements plus the capital conservation buffer. Under CLBR, the Bank was not subject to the capital conservation buffer.

NOTE 16. Restrictions On Dividends, Loans and Advances

Federal and state banking regulations place certain restrictions on dividends paid and loans or advances made by the Bank to the Company. The total amount of dividends which may be paid at any date is generally limited to the lesser of the Bank's retained earnings or the three preceding years' undistributed net income of the Bank. Loans or advances are limited to 10% of the Bank's capital stock and surplus on a secured basis. Capital stock and surplus is defined as tier 1 and tier 2 capital under the risk-based capital guidelines. In addition, dividends paid by the Bank to the Company would be prohibited if the effect thereof would cause the Bank's capital to be reduced below applicable minimum capital requirements.

At December 31, 2023, the Bank's retained earnings available for the payment of dividends to the Company was $32.3 million. Accordingly, $103.9 million of the Company's equity in the net assets of the Bank was restricted at December 31, 2023. Funds available for loans or advances by the Bank to the Company amounted to $16.9 million at December 31, 2023.

NOTE 17. Dividend Investment Plan

The Company has a Dividend Investment Plan, which allows participants' dividends to purchase additional shares of common stock at its fair market value on each dividend record date. Shares of common stock purchased through the Plan can be purchased at a price equal to the market price of the shares. No changes have been made to the operation of the dividend reinvestment features of the Plan during 2023 and 2022.

NOTE 18. Financial Instruments with Off-Balance-Sheet Risk

The Company, through its subsidiary bank, is a party to credit related financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit, unfunded commitments under lines of credit, and commercial and standby letters of credit. Such commitments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the consolidated balance sheets.

The Company's exposure to credit losses is represented by the contractual amount of these instruments. The Company uses the same credit policies in making commitments as it does for on-balance-sheet instruments. As of January 1, 2023, unfunded loan commitments that are not unconditionally cancelable by the Company are measured for expected credit losses under ASU 2016-13. The adoption of ASU 2016-13 on January 1, 2023, resulted in an adjustment to the Company's reserve for unfunded loan commitments of $406 thousand. At December 31, 2023, the reserve balance totaled $479 thousand.

At December 31, 2023 and 2022, the following financial instruments were outstanding whose contract amounts represent credit risk:

	December 31, 2023	December 31, 2022
	(dollars in thousands)	
Commitments to extend credit	$ 37,724	$ 27,927
Unfunded commitments under lines of credit	227,717	191,259
Commercial and standby letters of credit	3,964	7,069

Commitments to extend credit are agreements to lend to a customer as long as the terms offered are acceptable and certain other conditions are met. Commitments generally have fixed expiration dates or other termination clauses. Since these commitments may expire or terminate, the total commitment amounts do not necessarily represent future cash requirements. The amount of collateral obtained, with regards to these commitments, is based on management's credit evaluation of the customer.

Unfunded commitments under lines of credit are contracts for possible future extensions of credit to existing customers. Unfunded commitments under lines of credit include, but are not limited to, home equity lines of credit, overdraft protection lines of credit, credit cards, and unsecured and secured commercial lines of credit. The terms and conditions of these commitments vary depending on the line of credit's purpose, collateral, and maturity. The amount disclosed above represents total unused lines of credit for which a contract with the Bank has been established.

Commercial and standby letters of credit are conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. These letters of credit are primarily issued to support public and private borrowing arrangements. Essentially all letters of credit issued have expiration dates within one year. The credit risk involved in issuing letters of credit is essentially the same as that involved in granting loans to customers. The Bank holds collateral supporting these commitments if it is deemed necessary. At December 31, 2023, $3.8 million of the outstanding letters of credit were collateralized.

The Bank has cash accounts in other commercial banks. The amount on deposit in these banks at December 31, 2023 exceeded the insurance limits of the Federal Deposit Insurance Corporation by $9.0 million.

NOTE 19. Revenue Recognition

Substantially all of the Company's revenue from contracts with customers that is within the scope of ASC 606, "Revenue from Contracts with Customers" is reported within noninterest income. A limited amount of other in-scope items such as gains and losses on other real estate owned are recorded in noninterest expense. The recognition of interest income and certain sources of noninterest income (e.g. gains on securities transactions, bank owned life insurance income, etc.) are governed by other areas of U.S. GAAP. Significant revenue streams that are within the scope of ASC 606 and included in noninterest income are discussed in the following paragraphs.

Income from Fiduciary Activities

Trust asset management fee income is primarily comprised of fees earned from the management and administration of trusts and other customer assets. The Company’s performance obligation is generally satisfied over time and the resulting fees are recognized monthly, based upon the month-end market value of the assets under management and the applicable fee rate. Payment is generally received a few days after month end through a direct charge to customers’ accounts. The Company does not earn performance-based incentives. Optional services such as real estate sales and tax return preparation services are also available to existing trust and asset management customers. The Company’s performance obligation for these transactional-based services is generally satisfied, and related revenue recognized, at a point in time (i.e., as incurred). Payment is received shortly after services are rendered.

Service Charges on Deposit Accounts

Service charges on deposit accounts are principally comprised of overdrawn account fees, account maintenance charges and other activity based fees. The Company’s performance obligations on revenue generated from deposit accounts are generally satisfied immediately, when the transaction occurs, or by month-end. Typically, the duration of a contract does not extend beyond the services performed. Due to the short duration of most customer contracts which generate these sources of noninterest income, no significant judgments must be made in the determination of the amount and timing of revenue recognized.

Other Service Charges and Fees

The majority of the Company’s noninterest income is derived from short term contracts associated with services provided for other ancillary services such as ATM fees, brokerage commissions and loan servicing fees. The Company’s performance obligations on revenue generated from these ancillary services are generally satisfied immediately, when the transaction occurs, or by month-end. Typically, the duration of a contract does not extend beyond the services performed. Due to the short duration of most customer contracts which generate these sources of noninterest income, no significant judgments must be made in the determination of the amount and timing of revenue recognized.

The Company earns interchange fees from credit cardholder transactions conducted through the Visa payment network. Interchange fees from cardholder transactions represent a percentage of the underlying transaction value and are recognized no less than monthly.

Noninterest income disaggregated by major source, for the years ended December 31, 2023 and 2022 consisted of the following:

	December 31, 2023	December 31, 2022
	(dollar in thousands)	
Noninterest income:		
Wealth management fees(1):		
Trust asset management fees	$ 3,871	$ 3,095
Brokerage commissions	1,055	1,054
Service charges on deposit accounts(1):		
Overdrawn account fees	1,399	1,194
Monthly and other service charges	411	424
Other service charges and fees:		
Interchange fees (1)	449	366
ATM fees (1)	3,392	3,103
Secondary market fees	—	3
Other charges and fees (2)	572	471
Gain (loss) on the sale and disposal of bank premises and equipment (1)	14	(11)
Gain on the sale of marine finance assets	435	—
(Loss) on sale of securities	—	(737)
Gain on sale of loans	1,428	1,875
Bank owned life insurance income	713	626
Other operating income (3)	1,006	1,882
Total noninterest income	$ 14,745	$ 13,345

(1) Income within the scope of Topic 606.
(2) Includes income within the scope of Topic 606 of $327 thousand and $309 thousand for the years ended December 31, 2023 and 2022, respectively. The remaining balance is outside the scope of Topic 606.
(3) Includes income within the scope of Topic 606 of $778 thousand and $1.2 million for the years ended December 31, 2023 and 2022, respectively. The remaining balance is outside the scope of Topic 606.

Contract Balances

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 long-term revenue contracts with customers, and therefore, does not experience significant contract balances. As of December 31, 2023 and December 31, 2022, the Company did not have any significant contract balances.

NOTE 20. Quarterly Condensed Statements of Income - Unaudited

The Company's quarterly net income, net income per common share and dividends per common share during 2023 and 2022 are summarized as follows:

	2023			
	March 31	June 30	September 30	December 31
	(in thousands, except per share amounts)			
Total interest and dividend income	$ 18,558	$ 20,364	$ 22,191	$ 22,015
Net interest income after provision for credit losses	11,980	12,039	12,700	11,923
Noninterest income	3,526	3,357	4,209	3,653
Noninterest expenses	12,386	12,955	14,133	13,280
Income before income taxes	3,120	2,441	2,776	2,296
Net income	2,585	2,058	2,319	2,395
Net income per common share, basic	0.73	0.58	0.66	0.69
Net income per common share, diluted	0.73	0.58	0.66	0.69
Dividends per common share	0.30	0.30	0.30	0.30

	2022			
	March 31	June 30	September 30	December 31
	(in thousands, except per share amounts)			
Total interest and dividend income	$ 11,509	$ 12,647	$ 14,366	$ 16,164
Net interest income after provision for credit losses	10,599	11,559	12,899	12,326
Noninterest income	3,243	3,849	3,164	3,089
Noninterest expenses	9,923	10,528	11,058	11,548
Income before income taxes	3,919	4,880	5,005	3,867
Net income	3,250	3,992	4,082	3,197
Net income per common share, basic	0.94	1.14	1.17	0.92
Net income per common share, diluted	0.94	1.14	1.17	0.92
Dividends per common share	0.28	0.28	0.29	0.30

NOTE 21. Fair Value Measurements

GAAP requires the Company to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. The fair value of certain assets and liabilities is an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in the principal or most advantageous market in an orderly transaction between market participants as of the measurement date.

"Fair Value Measurements" defines fair value, establishes a framework for measuring fair value, establishes a three-level valuation hierarchy for disclosure of fair value measurement and enhances disclosure requirements for fair value measurements. The valuation hierarchy is based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date. The three levels are defined as follows:

- Level 1 Inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets.
- Level 2 Inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.
- Level 3 Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The following section provides a description of the valuation methodologies used for instruments measured at fair value on a recurring basis, as well as the general classification of such instruments pursuant to the valuation hierarchy:

Securities Available for Sale: Where quoted prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. Level 1 securities would include highly liquid government bonds, mortgage products and exchange traded equities. If quoted market prices are not available, then fair values are estimated by using pricing models, quoted prices of securities with similar characteristics, or discounted cash flow. Level 2 securities would include U.S. agency securities, mortgage-backed agency securities, obligations of states and political subdivisions and certain corporate, asset backed and other securities. In certain cases where there is limited activity or less transparency around inputs to the valuation, securities are classified within Level 3 of the valuation hierarchy.

Derivative instruments are recorded at fair value on a recurring basis. The Company utilizes derivative instruments as part of the management of interest rate risk to modify the re-pricing characteristics of certain portions of the Company's interest-bearing assets and liabilities. The Company has contracted with a third-party vendor to provide valuations for derivatives using standard valuation techniques and therefore classifies such valuations as Level 2. The Company has considered counterparty credit risk in the valuation of its derivative assets and has considered its own credit risk in the valuation of its derivative liabilities.

The following table presents balances of financial assets and liabilities measured at fair value on a recurring basis at December 31, 2023 and December 31, 2022:

		Fair Value Measurements at December 31, 2023 Using		
	Balance as of December 31, 2023	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
		(in thousands)		
Assets:				
Securities available for sale				
Obligations of U.S. government corporations and agencies	$ 8,591	$ —	$ 8,591	$ —
Mortgage-backed securities	118,822	—	118,822	—
Obligations of states and political subdivisions	5,931	—	5,931	—
Subordinated debt	4,099	—	4,099	—
Derivative:				
Interest rate swaps on loans	1,465	—	1,465	—
Total assets at fair value	$ 138,908	$ —	$ 138,908	$ —
Liabilities:				
Interest rate swaps on loans	$ 1,465		$ 1,465	$ —
Total liabilities at fair value	$ 1,465	$ —	$ 1,465	$ —

	Balance as of December 31, 2022	Fair Value Measurements at December 31, 2022 Using		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
		(in thousands)		
Assets:				
Securities available for sale				
Obligations of U.S. government corporations and agencies	$ 9,135	$ —	$ 9,135	$ —
U.S. treasury notes	—		—	—
Mortgage-backed securities	129,153	—	129,153	—
Obligations of states and political subdivisions	6,607	—	6,607	—
Subordinated debt	4,261	—	4,261	—
Derivative:				
Interest rate swaps on loans	1,017	—	1,017	—
Total assets at fair value	$ 150,173	$ —	$ 150,173	$ —
Liabilities:				
Interest rate swaps on loans	$ 1,017		$ 1,017	$ —
Total liabilities at fair value	$ 1,017	$ —	$ 1,017	$ —

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

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

Individually Evaluated Collateral-Dependent Loans: The estimated fair value of individually evaluated collateral-dependent loans is based on the value of the underlying collateral or the value of the underlying collateral, less estimated cost to sell, as appropriate. Collateral is generally real estate; however, collateral may include vehicles, equipment, inventory, accounts receivable, and/or other business assets. The value of real estate collateral is determined using a market valuation approach based on an appraisal conducted by an independent, licensed appraiser. The value of other assets may also be based on an appraisal, market quotations, aging schedules or other sources. Collateral-dependent individually evaluated loans are classified within Level 3 of the fair value hierarchy. Any fair value adjustments are recorded in the period incurred as a provision for credit losses on the Consolidated Statements of Income. There were no individually evaluated collateral dependent loans recorded at fair value at December 31, 2023 or 2022.

Other Real Estate Owned: Assets acquired through, or in lieu of, loan foreclosure are held for sale and are initially recorded at the fair value of the property, less estimated selling costs, establishing a new costs basis. Any write-downs based on the asset’s fair value at the date of acquisition are charged to the allowance for credit losses on loans. Costs of significant property improvements are capitalized, whereas costs relating to holding property are expensed. The portion of interest costs relating to development of real estate is capitalized. Valuations are periodically obtained by management, and any subsequent write-downs are recorded as a charge to operations, if necessary, to reduce the carrying value of a property to the lower of its cost or fair value less cost to sell. The fair value measurement of real estate held in other real estate owned is assessed in the same manner as collateral-dependent loans described above. We believe that the fair value component in its valuation follows the provisions of GAAP. The Company had a a balance of $0 and $108 thousand in other real estate owned at December 31, 2023 and 2022, respectively.

Loans Held for Sale: Loans held for sale are carried at the lower of cost or fair value. These loans consisted of one-to-four family residential loans originated for sale in the secondary market at December 31, 2023. Fair value is based on prices the secondary markets are currently offering for similar loans using observable market data which is not materially different than cost due to the short duration between origination and sale (Level 2). The Company records any fair value adjustments on a nonrecurring basis. No nonrecurring fair value adjustments were recorded on loans held for sale at December 31, 2023 and December 31, 2022.

The following table displays quantitative information about Level 3 Fair Value Measurements for certain financial assets measured at fair value on a nonrecurring basis at December 31, 2022:

Quantitative information about Level 3 Fair Value Measurements

	December 31, 2022			
	Valuation Technique(s)	**Unobservable Input**	**Range**	**Weighted Average**
Assets:				
Other real estate owned	Discounted contract price	Discount for selling costs	6 %	6 %

(1) Weighted based on the relative fair values of the specific items measured at fair value.

The following table summarizes the Company's financial and nonfinancial assets that were measured at fair value on a nonrecurring basis at December 31, 2022:

		Carrying value at December 31, 2022		
	Balance as of December 31, 2022	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**
	(in thousands)			
Nonfinancial Assets:				
Other real estate owned	$ 108	$ —	$ 108	$ —

The carrying amount and fair value of the Company's financial instruments at December 31, 2023 and 2022 were as follows:

	Carrying Value as of December 31, 2023	Fair Value Measurements at December 31, 2023 Using			Fair Value as of December 31, 2023
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
			(in thousands)		
Financial Assets:					
Cash and short-term investments	$ 138,353	$ 138,353	$ —	$ —	$ 138,353
Securities available for sale	137,443	—	137,443	—	137,443
Restricted Investments	9,568	—	9,568	—	9,568
Loans held for sale	1,661	—	1,661	—	1,661
Loans, net	1,448,193	—	—	1,377,017	1,377,017
Bank owned life insurance	29,575	—	29,575	—	29,575
Accrued interest receivable	5,008	—	5,008	—	5,008
Interest rate swaps	1,465	—	1,465	—	1,465
Financial Liabilities:					
Deposits	$ 1,506,322	$ —	$ 1,506,147	$ —	$ 1,506,147
Federal Home Loan Bank advances, short-term	20,000	—	19,954	—	19,954
Federal Home Loan Bank advances, long-term	145,000	—	145,141	—	145,141
Subordinated debt	29,444	—	25,581	—	25,581
Accrued interest payable	2,364	—	2,364	—	2,364
Interest rate swaps	1,465	—	1,465	—	1,465

	Carrying Value as of December 31, 2022	Fair Value Measurements at December 31, 2022 Using Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Fair Value as of December 31, 2022
			(in thousands)		
Financial Assets:					
Cash and short-term investments	$ 66,894	$ 66,894	$ —	$ —	$ 66,894
Securities available for sale	149,156	—	149,156	—	149,156
Restricted Investments	9,233	—	9,233	—	9,233
Loans held for sale	153		153		153
Loans, net	1,312,565	—	—	1,260,149	1,260,149
Bank owned life insurance	23,862	—	23,862	—	23,862
Accrued interest receivable	3,902	—	3,902	—	3,902
Interest rate swaps	1,017	—	1,017	—	1,017
Financial Liabilities:					
Deposits	$ 1,264,075	$ —	$ 1,262,859	$ —	$ 1,262,859
Federal funds purchased and securities sold under agreements to repurchase	32,980	—	32,980	—	32,980
Federal Home Loan Bank advances, short-term	175,000	—	174,705	—	174,705
Subordinated debt	29,377	—	26,101	—	26,101
Accrued interest payable	926	—	926	—	926
Interest rate swaps	1,017	—	1,017	—	1,017

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

NOTE 22. Change in Accumulated Other Comprehensive (Loss)

Accumulated other comprehensive (loss) includes unrealized gains and losses on available for sale securities and changes in benefit obligations and plan assets for the post retirement benefit plan. Changes to accumulated other comprehensive (loss) are presented net of tax as a component of equity. Reclassifications out of accumulated other comprehensive (loss) are recorded in the Consolidated Statements of Income either as a gain or loss.

Changes to accumulated other comprehensive (loss) by components are shown in the following tables for the years ended December 31, 2023 and 2022:

	Twelve Months Ended December 31,					
	2023			2022		
	Unrealized Gains and Losses on Available for Sale Securities	Change in Benefit Obligations and Plan Assets for the Post Retirement Benefit Plan	Total	Unrealized Gains and Losses on Available for Sale Securities	Change in Benefit Obligations and Plan Assets for the Post Retirement Benefit Plan	Total
	(dollars in thousands)			(dollars in thousands)		
January 1	$ (20,465)	$ 19	$ (20,446)	$ (174)	$ 19	$ (155)
Other comprehensive income (loss) before reclassifications	3,095	(8)	3,087	(26,422)	—	(26,422)
Reclassifications from other comprehensive (loss)	—	—	—	737	—	737
Tax effect of current period changes	(650)	3	(647)	5,394	—	5,394
Current period changes net of taxes	2,445	(5)	2,440	(20,291)	—	(20,291)
December 31	$ (18,020)	$ 14	$ (18,006)	$ (20,465)	$ 19	$ (20,446)

For the years ended December 31, 2023 and 2022, $0 and ($737) thousand, respectively, was reclassified out of accumulated other comprehensive (loss) and appeared as loss on sale of securities in the Consolidated Statement of Income. The tax benefit related to these reclassifications was $0 and $155 thousand for the years ended December 31, 2023 and 2022, respectively. The tax is included in Income Tax Expense in the Consolidated Statements of Income.

NOTE 23. Condensed Financial Information – Parent Company Only

EAGLE FINANCIAL SERVICES, INC.
(Parent Company Only)
Balance Sheets
December 31, 2023 and 2022
(dollars in thousands)

	2023	2022
Assets		
Cash held in subsidiary bank	$ 1,125	$ 8,222
Investment in subsidiary	136,130	122,767
Other assets	906	455
Total assets	$ 138,161	$ 131,444
Liabilities and Shareholders' Equity		
Subordinated debt	$ 29,444	$ 29,377
Other liabilities	338	338
Total liabilities	$ 29,782	$ 29,715
Shareholders' Equity		
Common stock	$ 8,660	$ 8,629
Surplus	14,280	13,268
Retained earnings	103,445	100,278
Accumulated other comprehensive (loss)	(18,006)	(20,446)
Total shareholders' equity	$ 108,379	$ 101,729
Total liabilities and shareholders' equity	$ 138,161	$ 131,444

EAGLE FINANCIAL SERVICES, INC.
(Parent Company Only)
Statements of Income
Years Ended December 31, 2023 and 2022
(dollars in thousands)

	2023		2022	
Income				
Dividends from subsidiary bank	$	4,000	$	—
Total income	$	4,000	$	—
Expenses				
Interest expense on subordinated debt	$	1,417	$	1,067
Other operating expenses		523		369
Total expenses	$	1,940	$	1,436
Income (loss) before income tax (benefit) and equity in undistributed earnings of subsidiary bank	$	2,060	$	(1,436)
Income Tax (Benefit)		(413)		(315)
Income (loss) before equity in undistributed earnings of subsidiary bank	$	2,473	$	(1,121)
Equity in Undistributed Net Income of Subsidiary Bank		6,884		15,642
Net income	$	9,357	$	14,521
Comprehensive income (loss)	$	11,797	$	(5,770)

EAGLE FINANCIAL SERVICES, INC.
(Parent Company Only)
Statements of Cash Flows
Years Ended December 31, 2023 and 2022
(dollars in thousands)

	2023	2022
Cash Flows from Operating Activities		
Net Income	$ 9,357	$ 14,521
Adjustments to reconcile net income to net cash provided by (used in) operating activities		
Stock-based compensation expense	1,213	1,017
Undistributed earnings of subsidiary bank	(6,884)	(15,642)
Amortization of debt issuance costs	67	51
Changes in assets and liabilities:		
(Increase) in other assets	(451)	(330)
Increase in other liabilities	—	338
Net cash provided by (used in) operating activities	$ 3,302	$ (45)
Cash Flows from Investing Activities		
Capital contribution to bank subsidiary	$ (6,000)	$ (20,000)
Net cash (used in) investing activities	$ (6,000)	$ (20,000)
Cash Flows from Financing Activities		
Issuance of subordinated debt, net of issuance costs	$ —	$ 29,326
Cash dividends paid	(4,229)	(3,808)
Issuance of common stock, employee benefit plan	132	164
Retirement of common stock	(302)	(154)
Net cash (used in) provided by financing activities	$ (4,399)	$ 25,528
(Decrease) increase in cash	$ (7,097)	$ 5,483
Cash		
Beginning	$ 8,222	$ 2,739
Ending	$ 1,125	$ 8,222

NOTE 24. Other Real Estate Owned

The following table is a summary of other real estate owned ("OREO") activity for the twelve months ended December 31, 2023 and 2022:

	Year Ended December 31, 2023	Year Ended December 31, 2022
Balance, beginning	$ 108	$ —
Net loans transferred to OREO	—	108
Gain on foreclosure	—	—
Sales	(108)	—
Valuation adjustments	—	—
Balance, ending	$ —	$ 108

The major classifications of other real estate owned in the consolidated balance sheets at December 31, 2023 and 2022 were as follows:

	As of	
	December 31, 2023	December 31, 2022
	(in thousands)	
Construction and Farmland	$ —	$ —
Residential Real Estate	—	108
Commercial Real Estate	—	—
Subtotal	$ —	$ 108
Less valuation allowance	—	—
Total	$ —	$ 108

There were no loans in the process of foreclosure at December 31, 2023 and December 31, 2022.

NOTE 25. Qualified Affordable Housing Project Investments

The Company invests in qualified affordable housing projects. The general purpose of these investments is to encourage and assist participants in investing in low-income residential rental properties located in the Commonwealth of Virginia, develop and implement strategies to maintain projects as low-income housing, provide tax credits and other tax benefits to investors, and to preserve and protect project assets.

At December 31, 2023 and 2022, the balance of the investments for qualified affordable housing projects was $2.0 million and $2.3 million, respectively. These balances are reflected in Other assets on the Consolidated Balance Sheets. There were no unfunded commitments related to the Company's qualified affordable housing projects at December 31, 2023 and 2022.

During the twelve months ended December 31, 2023 and 2022, the Company recognized amortization expense of $265 thousand and $278 thousand. The amortization expense was included in Other operating expenses on the Consolidated Statements of Income.

Total estimated credits to be received during 2023 are $354 thousand based on the most recent quarterly estimates received from the funds. Total tax credits and other tax benefits recognized during 2023 and 2022 were $389 thousand and $387 thousand, respectively.

NOTE 26. Derivatives

The Company uses derivative financial instruments primarily to manage risks to the Company associated with changing interest rates, and to assist customers with their risk management objectives. Derivative contracts that are not designated in a qualifying hedging relationships include customer accommodation loan swaps. The Company enters into interest rate swaps with certain qualifying commercial loan customers to meet their interest rate risk management needs. The Bank simultaneously enters into interest rate swaps with dealer counterparties, with identical notional amounts and offsetting terms. The net result of these interest rate swaps is that the customer pays a fixed rate of interest and the Company receives a floating rate. These back-to-back loan swaps are derivative financial instruments and are reported at fair value in "other assets" and "other liabilities" in the Consolidated Balance Sheets. Changes in the fair value of loan swaps are recorded in other noninterest income and sum to zero because of the offsetting terms of the swaps with borrowers and the swaps with dealer counterparties.

	December 31, 2023		
	Notional Amount	Assets	Liabilities
	(in thousands)		
Customer-related interest rate swap contracts:			
Matched interest rate swaps with borrower	$ 41,051	$ 844	$ 621
Matched interest rate swaps with counterparty	41,051	621	844

	December 31, 2022		
	Notional Amount	Assets	Liabilities
	(in thousands)		
Customer-related interest rate swap contracts:			
Matched interest rate swaps with borrower	$ 23,141	$ 1,017	$ —
Matched interest rate swaps with counterparty	23,141	—	1,017

NOTE 27. Business Segments

The Company has three reportable operating segments: community banking, marine lending and wealth management. Revenue from community banking operations consist primarily of net interest income related to investments in non-marine loans and securities and outstanding deposits and borrowings, fees earned on deposit accounts and debit card interchange activity. Revenue from marine lending operations consist primarily of net interest income related to commercial and consumer marine loans and gains on sales of loans. The wealth management division's net revenues are comprised primarily of income from offering wealth management services and insurance products through third-party service providers.

On August 23, 2023, the Company completed a sale of specific assets from its marine lending segment. As part of the sale, the Company sold its interest in marine vessel floor plan loans totaling $52.8 million, its rights to service loans that had been sold to secondary market investors prior to the date of sale (valued at $595 thousand on balance sheet prior to sale), and other assets that were not individually significant. The Company received total consideration, net of selling expenses, of $53.5 million and recognized a gain of $435 thousand. The assets sold as well as their related revenues and contribution to earnings did not constitute a significant portion of the Company's assets or operating results for the year ended December 31, 2023. Subsequent to the sale of these assets, the Company retained ownership of its marine vessel retail loans which continue to constitute a significant portion of the Company's assets, revenues, and earnings. The Company expects to cease accepting new marine lending business and hold the retained outstanding loans until they are ultimately repaid.

Financial information of the parent company is included in the "All Other" category. The parent company's revenue and expenses are comprised primarily of interest expense associated with subordinated debt.

The following table provides income and asset information as of and for the twelve months ended December 31, 2023 and 2022, which are included within the Consolidated Balance Sheets and Consolidated Statements of Income.

	Twelve Months Ended December 31, 2023 (in thousands)					
	Community Banking	Marine Lending	Wealth Management	All Other	Eliminations	Consolidated
Interest Income	$ 67,990	$ 15,138	$ —	$ —	$ —	$ 83,128
Interest Expense	25,850	5,570	—	1,417	—	32,837
Net Interest Income (Expense)	42,140	9,568	—	(1,417)	—	50,291
Gain on sales of loans	1,117	311	—	—	—	1,428
Other noninterest income	7,313	1,078	4,926	—	—	13,317
Net Revenue	50,570	10,957	4,926	(1,417)	—	65,036
Provision for credit losses	2,051	(402)	—	—	—	1,649
Noninterest expense	44,479	5,106	2,646	523	—	52,754
Income before taxes	4,040	6,253	2,280	(1,940)	—	10,633
Income tax expense (benefit)	(103)	1,313	479	(413)	—	1,276
Net Income	$ 4,143	$ 4,940	$ 1,801	$ (1,527)	$ —	$ 9,357
Other data:						
Capital expenditures	$ 1,035	$ 36	$ —	$ —	$ —	$ 1,071
Depreciation and amortization	1,573	224	126	67	—	1,990

	Twelve Months Ended December 31, 2022 (in thousands)					
	Community Banking	Marine Lending	Wealth Management	All Other	Eliminations	Consolidated
Interest Income	$ 47,554	$ 7,132	$ —	$ —	$ —	$ 54,686
Interest Expense	4,026	380	—	1,067	—	5,473
Net Interest Income (Expense)	43,528	6,752	—	(1,067)	—	49,213
Gain on sales of loans	478	1,397	—	—	—	1,875
Other noninterest income	7,222	99	4,149	—	—	11,470
Net Revenue	51,228	8,248	4,149	(1,067)	—	62,558
Provision for credit losses	1,059	771	—	—	—	1,830
Noninterest expense	36,401	3,695	2,590	371	—	43,057
Income before taxes	13,768	3,782	1,559	(1,438)	—	17,671
Income tax expense (benefit)	2,343	794	328	(315)	—	3,150
Net Income	$ 11,425	$ 2,988	$ 1,231	$ (1,123)	$ —	$ 14,521
Other data:						
Capital expenditures	$ 829	$ 9	$ —	$ —	$ —	$ 838
Depreciation and amortization	1,499	236	124	51	—	1,910

	Community Banking	Marine Lending	Wealth Management	All Other	Eliminations	Consolidated
Total assets at December 31, 2023	$ 1,562,600	$ 261,011	$ 1,080	$ 906	$ —	$ 1,825,597
Total assets at December 31, 2022	1,377,461	237,595	1,206	455	—	1,616,717

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

None.

Item 9A. Controls and Procedures

Disclosure Controls and Procedures

The Company, under the supervision and with the participation of management, including the Company's Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the design and operation of its disclosure controls and procedures as of the end of the period covered by this Annual Report on Form 10-K. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that the Company's disclosure controls and procedures were effective as of December 31, 2023 to ensure that information required to be disclosed by the Company in reports that it files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms and that such information is accumulated and communicated to the Company's management, including the Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

Internal Control over Financial Reporting

Management is also responsible for establishing and maintaining adequate internal control over the Company's financial reporting (as defined in Rule 13a-15(f) promulgated under the Securities Exchange Act of 1934, as amended). Pursuant to Section 404 of the Sarbanes-Oxley Act of 2002, management has conducted an assessment of the design and effectiveness of its internal controls over financial reporting based on criteria established in *Internal Control – Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO") in 2013.

Management maintains a comprehensive system of internal control 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. The system of internal control provides for appropriate division of responsibility and is documented by written policies and procedures that are communicated to employees. Those policies and procedures: 1) pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and disposition of the assets of the Company, 2) provide reasonable assurance that receipts and expenditures of the Company are being made only in accordance with authorizations of management and directors, 3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Company's assets that could have a material effect on the financial statements. Management recognizes that there are inherent limitations in the effectiveness of any internal control system, including the possibility of human error and the circumvention or overriding of internal controls. Accordingly, even effective internal control over financial reporting can provide only reasonable assurance with respect to financial statement preparation. Changes in conditions will also impact the internal control effectiveness over time. Eagle Financial Services, Inc. and its subsidiary maintain an internal auditing program, under the supervision of the Audit Committee of the Board of Directors, which independently assesses the effectiveness of the system of internal control and recommends possible improvements.

Under the supervision and with the participation of the Company's management, including its Chief Executive Officer and Chief Financial Officer, the Company has evaluated the effectiveness of its internal control over financial reporting as of December 31, 2023, using the *2013 Internal Control – Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based upon this evaluation, the Chief Executive Officer and the Chief Financial Officer have concluded as of December 31, 2023, the Company's internal control over financial reporting is adequate and effective and meets the criteria of the *Internal Control – Integrated Framework*.

Management's assessment did not determine any material weaknesses within the Company's internal control structure. There were no changes in the Company's internal control over financial reporting during the Company's quarter ended December 31, 2023 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

This annual report does not include an attestation report of the company's registered public accounting firm (Yount, Hyde & Barbour, P.C. (PCAOB Firm ID: 613)), regarding internal control over financial reporting. Management's report was not subject to attestation by the Company's registered public accounting firm pursuant to rules of the Securities and Exchange Commission that permit the Company to provide only management's report in this annual report.

Item 9B. Other Information

During the fiscal quarter ended December 31, 2023, none of our directors or officers (as defined in Rule 16a-1(f) of the Securities Exchange Act of 1934) adopted or terminated a Rule 10b5-1 trading arrangement or non-Rule 10b5-1 trading arrangement (as such terms are defined in Item 408(a) of Regulation S-K).

Item 9C. Disclosure Regarding Foreign Jurisdictions That Prevent Inspections

None.

PART III

Item 10. Directors, Executives Officers and Corporate Governance

The information required by Part III, Item 10 is incorporated herein by reference to the Proxy Statement for the 2024 Annual Meeting of Shareholders to be held May 21, 2024.

Item 11. Executive Compensation

The information required by Part III, Item 11 is incorporated herein by reference to the Proxy Statement for the 2024 Annual Meeting of Shareholders to be held May 21, 2024.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

The information required by Part III, Item 12 is incorporated herein by reference to the Proxy Statement for the 2024 Annual Meeting of Shareholders to be held May 21, 2024.

Item 13. Certain Relationships and Related Transactions, and Director Independence

The information required by Part III, Item 13 is incorporated herein by reference to the Proxy Statement for the 2024 Annual Meeting of Shareholders to be held May 21, 2024.

Item 14. Principal Accounting Fees and Services

The information required by Part III, Item 14 is incorporated herein by reference to the Proxy Statement for the 2024 Annual Meeting of Shareholders to be held May 21, 2024.

PART IV

Item 15. Exhibits, Financial Statement Schedules

(a)(1) Financial Statements

The financial statements are filed as part of this Annual Report on Form 10-K within Item 8.

(a)(2) Financial Statement Schedules

All financial statement schedules are omitted since they are not required, or are not applicable, or the required information is given in the financial statements or notes thereto.

(a)(3) Exhibits

The following exhibits, as applicable, are filed with this Form 10-K or incorporated by reference to previous filings.

Exhibit No.	Description
3.1	Articles of Incorporation of the Company, restated in electronic format only as of March 1, 2006 (incorporated herein by reference to Exhibit 3.1 of the Company's Current Report on Form 8-K dated March 1, 2006).
3.2	Bylaws of the Company (incorporated herein by reference to Exhibit 3.1 of the Company's Current Report on Form 8-K filed on May 20, 2021.
4.1	Description of Securities (incorporated herein by reference to Exhibit 4.1 of the Company's Annual Report on Form 10-K for the year ended December 31, 2019).
4.2	Form of 4.50% Fixed to Floating Rate Subordinated Note due April 1, 2032 (incorporated herein by reference to Exhibit 4.1 to the Company's Current Report on Form 8-K filed April 5, 2022).
10.1	Description of Executive Supplemental Income Plan (incorporated by reference to Exhibit 10.1 of the Company's Annual Report on Form 10-K for the year ended December 31, 1996).*
10.2	Amended and Restated Employment Agreement of Brandon C. Lorey (incorporated by reference to Exhibit 10.2 of the Company's Annual Report on Form 10-K for the year ended December 31, 2019).*
10.3	Eagle Financial Services, Inc. 2023 Stock Incentive Plan (incorporated herein by reference to Appendix A of the Proxy Statement for the Annual Meeting of Shareholders held on May 16, 2023, filed on April 5, 2023).*
10.4	Eagle Financial Services, Inc. 2014 Stock Incentive Plan (incorporated by reference to Exhibit A of the Proxy Statement for the Annual Meeting of Shareholders held on May 21, 2014, filed on April 21, 2014).*
10.5	Amended and Restated Employment Agreement of Joseph T. Zmitrovich (incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K filed on June 3, 2022).*
10.6	Amended and Restated Employment Agreement of Kaley P. Crosen (incorporated by reference to Exhibit 10.6 of the Company's Annual Report on Form 10-K for the year ended December 31, 2019).*
10.7	Amended and Restated Employment Agreement of Kathleen J. Chappell (incorporated herein by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K filed on January 16, 2020).*
10.8	Eagle Financial Services, Inc. Dividend Investment Plan (incorporated herein by reference to to the Company's Registration Statement on Form S-3, File No. 333-209460, filed on February 10, 2016).*
10.9	Amended and Restated Employment Agreement, dated December 1, 2022, between Eagle Financial Services, Inc. and Aaron M. Poffinberger (incorporated herein by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K filed on December 5, 2022).*
10.10	Form of Subordinated Note Purchase Agreement, dated March 31, 2022 (incorporated herein by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K filed April 5, 2022).
10.11	Asset Purchase and Servicing Rights Agreement, by and between Bank of Clarke and Axos Bank, dated as of August 23, 2023 (incorporated by reference to Exhibit 10.1 to Eagle Financial Services, Inc.'s Current Report on Form 8-K filed August 24, 2023).

10.12	Loan Purchase and Sale Agreement, by and between Bank of Clarke and Axos Bank, dated as of August 23, 2023 (exhibits omitted) (incorporated by reference to Exhibit 10.2 to Eagle Financial Services, Inc.'s Current Report on Form 8-K filed August 24, 2023).
21.1	Subsidiary of the Company.
23.1	Consent of Yount, Hyde & Barbour, P.C.
31.1	Certification by Chief Executive Officer pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification by Chief Financial Officer pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification by Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101	The following materials from the Eagle Financial Service, Inc. Annual Report on Form 10-K for the year ended December 31, 2023 formatted in Inline Extensible Business Reporting Language (iXBRL): (i) Consolidated Balance Sheets, (ii) Consolidated Statements of Income, (iii) Consolidated Statements of Comprehensive Income (Loss), (iv) Consolidated Statements of Changes in Shareholders" Equity, (v) Consolidated Statements of Cash Flows and (vi) notes to Consolidated Financial Statements.
104	The cover page from the Eagle Financial Services, Inc. Annual Report on Form 10-K for the year ended December 31, 2023 formatted in Inline XBRL (included with Exhibit 101).

* Management contracts and compensatory plans and arrangements.

(b) See Item 15(a)(3) above.

(c) See Item 15(a)(2) above.

Item 16. Form 10-K Summary

Not applicable.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) 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.

Eagle Financial Services, Inc.

By: /s/ BRANDON C. LOREY
Brandon C. Lorey
President and Chief Executive Officer

Date: March 29, 2024

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities indicated on March 29, 2024.

Signature	Title
/s/ BRANDON C. LOREY Brandon C. Lorey	President, Chief Executive Officer, and Director (principal executive officer)
/s/ KATHLEEN J. CHAPPELL Kathleen J. Chappell	Executive Vice President and Chief Financial Officer (principal financial and accounting officer)
/s/ THOMAS T. GILPIN Thomas T. Gilpin	Chairman of the Board and Director
/s/ ROBERT W. SMALLEY, JR. Robert W. Smalley, Jr.	Vice Chairman of the Board and Director
/s/ CARY R. CLAYTOR Cary R. Claytor	Director
/s/ MARY BRUCE GLAIZE Mary Bruce Glaize	Director
/s/ SCOTT HAMBERGER Scott Hamberger	Director
/s/ EDWARD HILL, III Edward Hill, III	Director
/s/ TATIANA C. MATTHEWS Tatiana C. Matthews	Director
/s/ JOHN R. MILLESON John R. Milleson	Director
/s/ DOUGLAS C. RINKER Douglas C. Rinker	Director
/s/ JOHN D. STOKELY, JR. John D. Stokely, Jr.	Director

EXHIBIT 21.1

SUBSIDIARY OF THE COMPANY

Bank of Clarke is a wholly-owned subsidiary of the Company. Bank of Clarke is a Virginia banking corporation, headquartered in Berryville, Virginia within the County of Clarke.

Exhibit 23.1

Consent of Independent Registered Public Accounting Firm

We consent to the incorporation by reference in Registration Statements (No. 333-269804, 333-209460, 333-172264, and 333-131877) on Form S-3 and Registration Statements (No. 333-275802, 333-198325, and 333-118319) on Form S-8 of Eagle Financial Services, Inc. of our report dated March 29, 2024, relating to the consolidated financial statements appearing in this Annual Report on Form 10-K of Eagle Financial Services, Inc. for the year ended December 31, 2023.

/s/ Yount, Hyde & Barbour, P.C.

Winchester, Virginia
March 29, 2024

EXHIBIT 31.1

CERTIFICATION BY CHIEF EXECUTIVE OFFICER PURSUANT TO RULES 13a-14(a) UNDER THE SECURITIES EXCHANGE ACT OF 1934, AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Brandon C. Lorey, certify that:

1. I have reviewed this annual report on Form 10-K of Eagle Financial Services, Inc. for the year ended December 31, 2023;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 29, 2024

By: /s/ BRANDON C. LOREY
Brandon C. Lorey
President and Chief Executive Officer

EXHIBIT 31.2

CERTIFICATION BY CHIEF EXECUTIVE OFFICER PURSUANT TO RULES 13a-14(a) UNDER THE SECURITIES EXCHANGE ACT OF 1934, AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Kathleen J. Chappell, certify that:

1. I have reviewed this annual report on Form 10-K of Eagle Financial Services, Inc. for the year ended December 31, 2023;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 29, 2024

By: /s/ KATHLEEN J. CHAPPELL

Kathleen J. Chappell
Executive Vice President and Chief Financial Officer

EXHIBIT 32.1

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the annual report on Form 10-K of Eagle Financial Services, Inc. (the “Company”) for the period ending December 31, 2023 to be filed with the Securities and Exchange Commission (the “Report”), the undersigned Chief Executive Officer and Chief Financial Officer of the Company hereby certify, pursuant to 18 U.S.C. Code Section 1350, as adopted pursuant to Code Section 906 of the Sarbanes-Oxley Act of 2002, that, to our knowledge:

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

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

Date: March 29, 2024

By: /s/ BRANDON C. LOREY
Brandon C. Lorey
President and Chief Executive Officer

/s/ KATHLEEN J. CHAPPELL
Kathleen J. Chappell
Executive Vice President and Chief Financial Officer

BOARD OF DIRECTORS - Eagle Financial Services, Inc. & Bank of Clarke

THOMAS T GILPIN
Chair

ROBERT W SMALLEY JR
Vice Chair

MARY BRUCE GLAIZE

SCOTT M HAMBERGER

DR. EDWARD HILL

BRANDON C LOREY

TANYA C MATTHEWS

JOHN R MILLESON

CARY C NELSON

DOUGLAS C RINKER

JOHN D STOKELY JR

EXECUTIVE OFFICERS - Eagle Financial Services, Inc. (EFSI) & Bank of Clarke (BOC)

BRANDON C LOREY
President/CEO
EFSI and BOC

KATHLEEN J CHAPPELL
EVP/Chief Financial Officer
EFSI and BOC

KALEY P CROSEN
Secretary- EFSI
EVP/Chief Human Resources
Officer BOC

DEBRA L PURRINGTON
EVP/Chief Fiduciary BOC

JOSEPH T ZMITROVICH
President/Chief Banking
Officer BOC

TODD A BRAITHWAITE
EVP/Chief Technology Officer
BOC

JAMES S GEORGE II
EVP/Chief Credit Officer
BOC

AARON M POFFINBERGER
EVP/COO & Chief Risk Officer
BOC

MARIANNE SCHMIDT
EVP/Chief Marketing Officer
BOC

KATHLEEN CROSON
EVP/Head of Community
Banking BOC

EAGLE FINANCIAL SERVICES, INC
ANNUAL MEETING
The annual Shareholders' meeting will be held at Barns of Rose Hill on May 21, 2024 at 10:00 AM.

CORPORATE HEADQUARTERS
2 East Main Street, Berryville VA 22611

CORPORATE MAILING ADDRESS
PO Box 391, Berryville VA 22611

TRANSFER AGENT

EQ
P.O. Box 500
Newark NJ 07101
800.937.5449

FORM 10K
A copy of the Company's 2023 Form 10K annual report to the Securities and Exchange Commission may be obtained without charge on the investor relations page of our website https://investors.bankofclarke.bank/overview/default.aspx or upon written request.

WEBSITE
www.bankofclarke.bank