Burke & Herbert Bank

At Your Service Since 1852®

2021 Audited Financial Statements

CONTENTS

BURKE & HERBERT BANK & TRUST COMPANY

BALANCE SHEETS
December 31, 2021 and 2020
In thousands, except share and per share data

ASSETS		**2021**		2020
Cash and due from banks	**$**	**8,989**	$	14,670
Interest-bearing deposits with banks		**68,374**		214,034
Cash and cash equivalents		**77,363**		228,704
Securities available for sale, at fair value		**1,605,681**		1,159,701
Restricted stock, at cost		**12,079**		12,192
Loans held for sale (HFS), at fair value		**1,249**		8,211
Loans		**1,745,073**		1,833,775
Allowance for loan losses		**(31,709)**		(32,697)
Net loans		**1,713,364**		1,801,078
Premises and equipment, net		**36,875**		40,494
Accrued interest receivable		**15,253**		13,784
Bank owned life insurance		**91,062**		88,977
Other assets		**68,817**		71,640
Total assets	**$**	**3,621,743**	$	3,424,781
LIABILITIES				
Deposits				
Non-interest bearing	**$**	**930,847**	$	852,008
Interest bearing		**2,002,570**		1,937,438
Total deposits		**2,933,417**		2,789,446
Borrowed funds		**275,000**		225,000
Accrued interest and other liabilities		**23,699**		25,458
Total liabilities		**3,232,116**		3,039,904
Commitments and contingent liabilities				
SHAREHOLDERS' EQUITY				
Common stock	**$**	**4,000**	$	4,000
$20 par value; 200,000 shares issued and authorized; outstanding 185,594 in 2021 and 186,202 in 2020				
Additional paid-in capital		**10,374**		10,178
Retained earnings		**396,120**		374,826
Accumulated other comprehensive income		**6,955**		22,580
Treasury stock		**(27,822)**		(26,707)
14,406 and 13,798 shares, at cost, at December 31, 2021 and 2020, respectively				
Total shareholders' equity		**389,627**		384,877
Total liabilities and shareholders' equity	**$**	**3,621,743**	$	3,424,781

See Notes to Financial Statements

BURKE & HERBERT BANK & TRUST COMPANY

STATEMENTS OF INCOME
Years Ended December 31, 2021 and 2020
In thousands, except per share data

	2021	2020
Interest income		
Loans	$ 73,170	$ 78,262
Taxable securities	17,537	13,288
Tax-exempt securities	9,907	8,737
Other	206	710
Total interest income	100,820	100,997
Interest expense		
Deposits	2,746	9,696
Borrowed funds	1,432	1,579
Other	39	6
Total interest expense	4,217	11,281
Net interest income	96,603	89,716
Noninterest income		
Fiduciary and wealth management	5,162	4,451
Service charges and fees	6,328	5,700
Net gains (losses) on securities	(4)	1,944
Income from life insurance	2,325	2,303
Other	3,440	4,606
Total noninterest income	17,251	19,004
Total revenue	113,854	108,720
Provision for (recapture of) loan losses	(1,002)	12,648
Noninterest expense		
Salaries and wages	37,099	33,377
Pensions and other employee benefits	7,621	7,568
Occupancy	6,444	6,003
Equipment rentals, depreciation and maintenance	5,481	4,935
Other operating	17,769	15,750
Total noninterest expense	74,414	67,633
Income before income taxes	40,442	28,439
Income tax expense	4,277	1,940
Net income	$ 36,165	$ 26,499
Earnings per common share		
Basic earnings per common share	$ 194.85	$ 142.21
Diluted earnings per common share	194.70	142.19

See Notes to Financial Statements

BURKE & HERBERT BANK & TRUST COMPANY

STATEMENTS OF COMPREHENSIVE INCOME
Years Ended December 31, 2021 and 2020
In thousands

	2021	2020
Net income	**$ 36,165**	$ 26,499
Other comprehensive income, net of tax:		
Unrealized gains (losses) on securities:		
Unrealized gains (losses) arising during period, net of tax of $4,235 for 2021 and ($6,008) for 2020	**(15,933)**	22,603
Reclassification adjustment for (gain) losses on securities, net of tax of $1 for 2021 and ($408) for 2020	**3**	(1,536)
Changes in pension plan benefits, net of tax of ($81) for 2021 and ($23) for 2020	**305**	87
Total other comprehensive income (loss)	**(15,625)**	21,154
Comprehensive income	**$ 20,540**	$ 47,653

See Notes to Financial Statements

BURKE & HERBERT BANK & TRUST COMPANY

STATEMENTS OF SHAREHOLDERS' EQUITY
Years Ended December 31, 2021 and 2020
In thousands, except share data

	Common Stock		Additional	Retained	Accumulated Other	Treasury	Total
	Shares	Amount	Paid-in Capital	Earnings	Comprehensive Income (Loss)	Stock	
Balance, December 31, 2019	186,958	$ 4,000	$ 10,032	$ $363,232	$ 1,426	$ (25,162)	$ **353,528**
Net income	-	-	-	26,499	-	-	**26,499**
Other comprehensive income	-	-	-	-	21,154	-	**21,154**
Purchase of treasury stock	(756)	-	-	-	-	(1,545)	**(1,545)**
Cash dividends declared	-	-	-	(14,905)	-	-	**(14,905)**
Share-based compensation expense	-	-	146	-	-	-	**146**
Balance, December 31, 2020	186,202	$ 4,000	$ 10,178	$ 374,826	$ 22,580	$ (26,707)	$ **384,877**
Net Income	-	-	-	36,165	-	-	**36,165**
Other comprehensive income	-	-	-	-	(15,625)	-	**(15,625)**
Purchase of treasury stock	(608)	-	-	-	-	(1,115)	**(1,115)**
Cash dividends declared	-	-	-	(14,871)	-	-	**(14,871)**
Share-based compensation expense	-	-	196	-	-	-	**196**
Balance, December 31, 2021	**185,594**	**$ 4,000**	**$ 10,374**	**$ 396,120**	**$ 6,955**	**$ (27,822)**	**$ 389,627**

See Notes to Financial Statements

BURKE & HERBERT BANK & TRUST COMPANY

STATEMENTS OF CASH FLOWS
Years Ended December 31, 2021 and 2020
In thousands

		2021		2020
Cash flows from operating activities:				
Net income	$	36,165	$	26,499
Adjustments to reconcile net income to net cash provided by operating activities:				
Depreciation and amortization		3,205		2,937
Realized (gain) loss on available for sale securities		4		(1,944)
Provision for (recapture of) loan losses		(1,002)		12,648
Income from Bank owned life insurance		(2,325)		(2,303)
Deferred tax (benefit)		(1,659)		(3,830)
(Gain) loss on disposal of fixed assets		(1,063)		7
Accretion of bond discount		(1,380)		(1,087)
Amortization of bond premium		9,870		5,791
Stock based compensation expense		196		146
(Gain) on loans held for sale		(194)		(122)
Proceeds from sale of loans held for sale		50,171		59,896
Originations of loans held for sale		(42,969)		(66,016)
(Increase) in accrued interest receivable		(1,469)		(5,671)
Decrease in other assets		9,445		4,712
(Increase) in accrued interest and other liabilities		(2,195)		(8,489)
Net cash provided by operating activities	$	54,800	$	23,174
Cash flows from investing activities:				
Proceeds from maturities of securities available for sale		194,578		188,653
Proceeds from sale of securities available for sale, net		700		49,233
Purchases of securities available for sale, net		(669,951)		(679,933)
Sales of restricted stock		1,988		2,252
Purchases of restricted stock		(1,875)		(8,500)
Proceeds from sales of property and equipment		2,561		-
Purchases of property and equipment, net of disposals		(1,083)		(2,697)
(Purchases of) proceeds from Bank owned life insurance		240		(7)
Decrease in loans made to customers, net		88,716		45,277
Net cash provided used by investing activities	$	(384,126)	$	(405,722)

(continued)

BURKE & HERBERT BANK & TRUST COMPANY

STATEMENTS OF CASH FLOWS (continued)
Years Ended December 31, 2021 and 2020
In thousands

		2021		2020
Cash flows from financing activities:				
Net increase in demand deposits, NOW accounts, savings deposits and money market accounts	$	65,132	$	457,827
Increase (decrease) in other time deposits		78,839		(63,872)
Increase in other borrowed funds		50,000		150,000
Cash dividends paid		(14,871)		(14,905)
Purchase of treasury stock		(1,115)		(1,545)
Net cash provided by financing activities	$	177,985	$	527,505
Increase (decrease) in cash and cash equivalents		(151,341)		144,957
Cash and cash equivalents				
Beginning		228,704		83,747
Ending	$	77,363	$	228,704
Supplemental Disclosures of Cash Flow Information				
Cash payments for:				
Interest paid to depositors	$	2,856	$	10,194
Interest paid on other borrowed funds	$	1,430	$	1,456
Interest paid on finance lease	$	39	$	6
Income taxes	$	1,347	$	1,400
Change in unrealized gains on available for sale Securities	$	(20,165)	$	26,668
Change in pension plan benefits	$	386	$	110
Lease liability arising from obtaining ROU assets	$	2,221	$	3,310
Premises & equipment transferred to property HFS	$	2,697	$	447

See Notes to Financial Statements

Note 1. Nature of Banking Activities and Significant Accounting Policies

Nature of banking activities: Burke & Herbert Bank & Trust Company (the Bank) conducts its banking business primarily in northern Virginia. The Bank's branch locations accept business and consumer deposits from a diverse customer base. The Bank's deposit products include checking, savings, and term certificate accounts. The Bank's loan portfolio includes commercial and consumer loans, a substantial portion of which are secured by area real estate.

A summary of the Bank's significant accounting policies follows:

Subsequent events: The Bank has evaluated subsequent events for recognition and disclosure through March 7, 2022, which is the date the financial statements were available to be issued.

Use of estimates: To prepare financial statements in conformity with U.S. generally accepted accounting principles (U.S. GAAP), management makes estimates and assumptions based on available information that affects 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.

Cash, cash equivalents and cash flows: For purposes of reporting cash flows, cash and cash equivalents include cash on hand and amounts due from banks, including cash items in process of clearing. Cash flows from loans, federal funds purchased and sold, securities sold under agreements to repurchase and deposits are reported on a net basis.

Restriction on cash: No reserve balances were required at December 31, 2021 and December 31, 2020. There was no reserve requirement with the Federal Reserve as of December 31, 2021 or December 31, 2020.

Debt & equity securities: Management determines the appropriate classification of debt securities at the time of purchase. Debt securities that the Bank has both the positive intent and ability to hold to maturity are classified as held to maturity and are reported at cost, adjusted for amortization of premiums and accretion of discounts. Debt securities that the Bank intends to hold for an indefinite period of time, but not necessarily to maturity, are classified as available for sale and are reported at fair value. Unrealized gains and losses on investments classified as available for sale have been accounted for as a separate component of accumulated other comprehensive income or loss, net of the related deferred tax effect. Amortization of premiums and accretion of discounts are recognized in interest income over the terms of the securities. Any decision to sell a security classified as available for sale would be based on various factors, including significant movements in interest rates, changes in the maturity mix of the Bank's assets and liabilities, liquidity needs, regulatory capital considerations, and other similar factors. Gains and losses on the sale of securities are recorded on the trade date and are determined using the specific identification method.

Equity securities are carried at fair value with changes in fair value reported in net 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.

Note 1. Nature of Banking Activities and Significant Accounting Policies (continued)

The Bank evaluates debt securities for other-than-temporary impairment (OTTI). For debt securities in an unrealized loss position, management considers the extent and duration of the unrealized loss, and the financial condition and near-term prospects of the issuer. Management also assesses whether it intends to sell, or it is more likely than not that it will be required to sell, a debt security in an unrealized loss position before recovery of its amortized cost basis. If either of the criteria regarding intent or requirement to sell is met, the entire difference between amortized costs and fair value is recognized as impairment through earnings. For debt securities that do not meet the aforementioned criteria, the amount of impairment is split into two components as follows: 1) OTTI related to credit loss, which must be recognized in the income statement and 2) OTTI related to other factors, which is recognized in other comprehensive income. The credit loss is defined as the difference between the present value of the cash flows expected to be collected and the amortized cost basis.

Due to the nature of, and restrictions placed upon, the equity securities of the Federal Home Loan Bank and Community Bankers' Bank, these securities have been classified as restricted stock and are carried at cost. These equity securities are not subject to the classifications above.

Loans held for sale: Loans held for sale are those loans the Bank has the intent to sell in the foreseeable future. The Bank has elected to use the fair value accounting option for loans held for sale. Gains and losses on sales of loans are recognized at settlement dates and are determined by the difference between the sales proceeds and the fair value of the loans. All sales are made without recourse, and are sold with servicing released.

Loan commitments and related financial instruments: Financial instruments include off-balance sheet credit instruments, such as commitments to make loans and commercial letters of credit, issued to meet customer financing needs. The face amount for these items represents the exposure to loss before considering customer collateral or ability to repay. Such financial instruments are recorded when they are funded.

Mortgage banking & financial derivatives: The Bank enters into commitments to originate loans whereby the interest rate on the loan is determined prior to funding (interest rate lock commitments). Interest rate lock commitments on mortgage loans to be held for sale are accounted for as free standing derivatives. The period of time between issuance of a loan commitment and closing and sale of the loan generally ranges from 15 to 90 days. The Bank protects itself from changes in interest rates through the use of best efforts forward delivery commitments, whereby the Bank commits to sell a loan at the time the borrower commits to an interest rate with the intent that the buyer has assumed interest rate risk on the loan. As a result, the Bank is not exposed to significant losses nor will it realize significant gains related to rate lock commitments due to changes in interest rates. The Bank has elected to use the fair value accounting option for best effort forward sales commitments.

Financial derivatives are reported at fair value in other assets and other liabilities. The accounting for changes in fair value of a derivative depends on whether it has been designated and qualifies as part of a hedging relationship.

Note 1. Nature of Banking Activities and Significant Accounting Policies (continued)

Loans: The Bank extends commercial and consumer loans, primarily in northern Virginia. Portfolio segments include (i) commercial real estate, (ii) single family residential (1-4 units), (iii) owner-occupied commercial real estate, (iv) acquisition, construction and development, (v) commercial & industrial, and (vi) consumer non-real estate and other.

Risk factors evaluated include the economic environment's impact on each portfolio segment and the following specific risk factors:

- Commercial real estate loans carry risk associated with either the net operating income generated from the lease of the real estate collateral or income generated from the sale of the collateral. Other risk factors include the credit-worthiness of the sponsor and the value of the collateral.
- Single family residential (1-4 units) loans for consumer purposes carry risks associated with the continued credit-worthiness of the borrower and the value of the collateral. Single family residential (1-4 units) loans for investment purposes carry risks associated with the continued credit-worthiness of the borrower, the value of the collateral, and either the net operating income generated from the lease of the real estate collateral or income generated from the sale of the collateral.
- Owner-occupied commercial real estate loans carry risk associated with the operations of the business that occupies the property and the value of the collateral.
- Acquisition, construction and development loans carry risk associated with the credit-worthiness of the borrower, project completion within budget, sale after completion, and the value of the collateral.
- Commercial & industrial loans carry risk associated with the operations of the business and the value of the collateral, if any.
- Consumer non-real estate and other loans carry risk associated with the credit-worthiness of the borrower and the value of the collateral, if any.

The Bank's recorded investment in loans that management has the intent and ability to hold for the foreseeable future, until maturity or until pay-off, generally are reported at their outstanding unpaid principal balances, adjusted for partial charge-offs, the allowance for loan losses, and any deferred fees and costs on originated loans. Interest income is accrued on the unpaid principal balance. Loan origination fees and costs are deferred and recognized as an adjustment of the related loan yield using the interest method without anticipating prepayments.

For all portfolio segments, the accrual of interest is discontinued at the time a loan becomes 90 days delinquent, unless the credit is well-secured and in process of collection. Loans also are placed on nonaccrual if collection of principal or interest is considered impaired. All interest accrued, but not received, for loans placed on non-accrual is reversed against interest income. Interest received on such loans is accounted for on the cash-basis or cost-recovery method until qualifying for return to accrual. Under the cost-recovery method, interest income is not recognized until the loan balance is reduced to zero. Under the cash-basis method, interest income is recorded when the payment is received in cash. For all portfolio segments, loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and a history of on-time payments has again been established.

Note 1. Nature of Banking Activities and Significant Accounting Policies (continued)

With the passage of the Paycheck Protection Program (PPP), administered by the Small Business Administration (SBA), the Bank is actively participating in assisting its customers through the program. Most of the PPP loans the Bank made have a two-year term and earn interest at 1%. Guidance issued by the SBA during the second wave of funding provided terms of up to five years. If borrowers request a change from two years to five years, the Bank will likely grant that request. The Bank believes that the majority of these loans will ultimately be forgiven by the SBA in accordance with the terms of the program. The Bank holds $37.8 million and $118.2 million in PPP loans, net of deferred fees and costs as of December 31, 2021 and 2020, respectively. It is the Bank's understanding that loans funded through the PPP are fully guaranteed by the U.S. government. Should these circumstances change, the Bank could be required to establish additional allowance for loan loss through the provision for loan loss charged to earnings.

<u>Concentrations of credit</u>: Substantially all of the Bank's loans, commitments, and standby letters of credit have been granted to customers in the Bank's market area. Such customers are generally depositors of the Bank. Some investments in state and municipal securities also involve governmental entities within the Bank's market area. The distribution of commitments to extend credit approximates the distribution of loans outstanding. Standby letters of credit were granted primarily to commercial borrowers.

<u>Troubled debt restructuring</u>: In situations where, for economic or legal reasons related to a borrower's financial condition, management may grant a concession to the borrower that it would not otherwise consider. The related loan is classified as a Troubled Debt Restructuring (TDR). Management strives to identify borrowers in financial difficulty early and work with them to modify their loan to more affordable terms before their loan reaches nonaccrual status. These modified terms may include rate reductions, principal forgiveness, payment forbearance and other actions intended to minimize the economic loss and to avoid foreclosure or repossession of collateral. In cases where borrowers are granted new terms that provided for a reduction of either interest or principal, management measures any impairment on the restructuring as noted above for any impaired loans.

In accordance with regulatory guidance and provisions in the CARES Act to provide relief during the COVID-19 pandemic, the Bank has provided short-term concessions to certain borrowers. The Bank holds $173.1 million and $148.4 million in loans that were under deferral under the CARES Act provisions as of December 31, 2021 and 2020, respectively. For loans to qualify for COVID-19 related modifications, these loans could not be more than 30 days past due as of December 31, 2019. As such, these loans were not considered TDRs based on the relief provisions of the CARES Act and recent regulatory interagency guidance.

The Bank is monitoring COVID-19 related modifications. If loans within this population require subsequent modifications, including payment extensions beyond six months, the Bank will consider the borrower's financial status at the time of the request and the effect of all modifications, past and requested, on the loan. If the borrower is deemed to be in financial difficulty that is not short-term and the impact of all modifications is considered to amount to a concession under U.S. GAAP, the loan will be designated a TDR. The Bank is also monitoring the population to determine whether other credit-related action should be taken, possibly including downgrading credit risk ratings, designating as nonaccrual, or determining a charge-off.

Note 1. Nature of Banking Activities and Significant Accounting Policies (continued)

Allowance for loan losses: The allowance for loan losses is established to absorb probable losses inherent in outstanding loans through a provision for loan losses charged to earnings. Credit losses are charged against the allowance. Subsequent recoveries, if any, are credited to the allowance.

The allowance for loan losses is evaluated on a quarterly basis by management and is based upon (i) historical loss norms for each portfolio segment as adjusted by environmental factors plus a risk adjustment based on the risk rating of the loan, and (ii) a loan by loan analysis of all other loans which are rated as either in a nonaccrual status or classified as troubled debt restructuring. Loan ratings include:

- Pass rated loans include all loans which are considered to be either high quality, good quality or acceptable quality. Borrowers have an acceptable financial condition with demonstrated repayment ability.
- Special mention loans have potential developing weaknesses that deserve extra attention. If the developing weakness is not corrected or mitigated, there may be deterioration in the ability of the borrower to repay.
- Substandard is a regulatory classification. Loans rated substandard are considered to have well-defined weakness and there is a possibility that some future loss will be sustained by the Bank if such weakness is not corrected.
- Doubtful is a regulatory classification. Loans rated doubtful have all of the weaknesses inherent in those rated substandard, with the added characteristic that the severity of the weaknesses makes collection or liquidation in full highly questionable. The probability of some loss is high.
- Loss represents a classification for loans which are considered uncollectable and are in the process of being charged off.

Historical credit losses for each portfolio segment are adjusted by environmental factors which include (i) changes in lending policies and procedures, including underwriting standards, and collection, charge-off, and recovery practices; (ii) changes in national and local economic and business conditions, including the conditions of various market segments; (iii) changes in the nature and volume of the portfolio; (iv) changes in the experience, ability, and depth of lending management and staff; (v) changes in the volume and severity of past due and classified loans and the volume of nonaccruals, troubled debt restructurings, and other loan modifications; (vi) changes in the quality of the Bank's loan review system and the degree of oversight by the Bank's Board of Directors; (vii) the existence and effect of any concentrations of credit and changes in the level of such concentrations; and (viii) the effect of external factors, such as competition and legal and regulatory requirements, on the level of estimated credit losses in the Bank's current portfolio. This evaluation is inherently subjective since it requires estimates that are susceptible to significant revision as additional information becomes available or as economic conditions change.

Impaired, collateral dependent loans may be charged down to the net realizable value of the collateral. Alternatively, a specific allowance may be established when the discounted cash flows (or collateral value of observable market price) of the impaired loan are lower than the carrying value of that loan.

Note 1. Nature of Banking Activities and Significant Accounting Policies (continued)

For all portfolio segments, a loan is considered impaired when, based on current information and events, it is probable that the Bank will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed.

Premises and equipment: Land is carried at cost. Premises and equipment are carried at cost less accumulated depreciation. Buildings and related components are depreciated using the straight-line method with useful lives ranging from 10 to 39 years. Furniture, fixtures and equipment are depreciated using the straight-line method (or accelerated) method with useful lives ranging from 3 to 10 years. Maintenance and repairs are charged to expense as incurred and major improvements are capitalized.

Bank owned life insurance: The Bank has purchased life insurance policies on certain employees. Bank owned life insurance is recorded at the amount that can be realized under the insurance contract at the balance sheet date, which is the cash surrender value.

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 Bank, 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 Bank does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

Other real estate owned (OREO): Assets acquired through foreclosure or other proceedings are initially recorded at fair value at the date of foreclosure less estimated costs of disposal, which establishes a new cost. After foreclosure, valuations periodically are performed by management and the foreclosed assets held for sale are carried at the lower of cost or fair value less estimated costs of disposal. Any write-down to fair value at the time of transfer to foreclosed assets is charged to the allowance for loan losses. All subsequent gains on sale, losses on sale, and additional write-downs are included in net gains/(losses) on other real estate owned. Revenue and expenses from the operations of foreclosed assets are included in other noninterest income and other operating expenses.

Note 1. Nature of Banking Activities and Significant Accounting Policies (continued)

Income taxes: The Bank accounts for income taxes in accordance with income tax accounting guidance. The Bank has adopted the accounting guidance related to accounting for uncertainty in income taxes, which sets out a consistent framework to determine the appropriate level of tax reserves to maintain for uncertain tax positions.

The income tax accounting guidance results in two components of income tax expense: current and deferred. Current income tax expense reflects taxes to be paid or refunded for the current period by applying the provisions of the enacted tax law to the taxable income or excess of deductions over revenues. The Bank determines deferred income taxes using the liability (or balance sheet) method. Under this method, the net deferred tax asset or liability is based on the tax effects of the differences between the book and tax bases of assets and liabilities, and enacted changes in tax rates and laws are recognized in the period in which they occur.

Deferred income tax expense results from changes in deferred tax assets and liabilities between periods. Deferred tax assets are recognized if it is more-likely-than-not, based on the technical merits, that the tax position will be realized or sustained upon examination. The term more-likely-than-not means a likelihood of more than 50 percent; the terms examined and upon examination also include resolution of the related appeals or litigation processes, if any. A tax position that meets the more-likely-than-not recognition threshold is initially and subsequently measured as the largest amount of tax benefit that has a greater than 50 percent likelihood of being realized upon settlement with a taxing authority that has full knowledge of all relevant information. The determination of whether or not a tax position has met the more-likely-than-not recognition threshold considers the facts, circumstances, and information available at the reporting date and is subject to management's judgment. Deferred tax assets are reduced by a valuation allowance if, based on the weight of evidence available, it is more likely than not that some portion or all of a deferred tax asset will not be realized.

The Bank recognizes interest and penalties on income taxes as a component of income tax expense.

Employee benefits: The Bank has a noncontributory defined benefit pension plan that was frozen to new participants on June 1, 2005. The Bank also has a defined contribution plan (The Investment and Savings Plan) with a salary deferral provision, which covers all employees in the month following their date of hire if they have reached the age of 18. The Bank's funding policy for the defined benefit plan is to make annual contributions to the Plan in amounts that are determined based on actuarial valuations and recommendations and which meet the minimum funding requirements of the Employee Retirement Income Security Act of 1974.

Authoritative accounting literature requires an employer to recognize the overfunded or underfunded status of a defined benefit postretirement plan as an asset or liability in its balance sheet and to recognize changes in the funded status in the year in which the changes occur through comprehensive income. The funded status of a benefit plan will be measured as the difference between plan assets at fair value and the benefit obligation. For a pension plan, the benefit obligation is the projected benefit obligation. For any other postretirement plan, the benefit obligation is the accumulated postretirement benefit obligation. Authoritative accounting literature also requires an employer to measure the funded status of a plan as of the date of its year-end balance sheet. The guidance also requires additional disclosure in the notes to financial statements about certain effects on net periodic benefit cost for the next fiscal year that arise from delayed recognition of the gains or losses, prior service costs or credits, and transition asset or obligation.

Note 1. Nature of Banking Activities and Significant Accounting Policies (continued)

Per share data: The Bank's capital structure includes an equity-based compensation plan, which may be dilutive to earnings per share (EPS). Basic EPS is calculated by dividing net income by the weighted average number of shares outstanding during the year. The weighted average number of shares outstanding during 2021 and 2020, was 185,610 and 186,341 shares, respectively. Diluted EPS is calculated by assuming dilution of common shares and adjusting net income for compensation cost attributable to the equity based compensation plan. Weighted average dilutive shares for 2021 and 2020, was 185,750 and 186,362 shares, respectively.

Trust assets and fees: Assets of the trust department, other than trust cash on deposit at the Bank, are not included in these financial statements because they are not assets of the Bank. Trust fees are recognized in income using the accrual method.

Loss contingencies: Loss contingencies, including claims and legal actions arising in the ordinary course of business, are recorded as liabilities when the likelihood of loss is probable and an amount or range of loss can be reasonably estimated. Management does not believe there now are such matters that will have a material effect on the financial statements.

Comprehensive income: Comprehensive income consists of net income and other comprehensive income. Other comprehensive income (loss) includes unrealized gains (losses) on securities available for sale, unrealized losses related to factors other than credit on debt securities, and changes in the funded status of the pension plan which also are recognized as separate components of equity.

Leases: Lease liabilities represent the Bank'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 Bank's incremental borrowing rate in effect at the commencement date of the lease. Right-of-use assets represent the Bank'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.

Fair value of financial instruments: Fair values of financial instruments are estimated using relevant market information and other assumptions. Fair value estimates involve uncertainties and matters of significant judgment regarding interest rates, credit risk, prepayments, and other factors, especially in the absence of broad markets for particular items. Changes in assumptions or in market conditions could significantly affect the estimates.

Equity-based compensation: Compensation cost is recognized for equity awards issued to employees, based on the fair value of these awards at the date of grant using an observable market price. The Bank classifies stock awards as equity. Compensation cost is recognized over the required service period on a straight-line basis. The Bank's accounting policy is to recognize forfeitures as they occur.

Revenue from contracts with customers: Accounting Standards Codification (ASC) 606 does not apply to revenue associated with financial instruments such as interest income from loans and securities. However, ASC 606 is applicable to noninterest revenue streams such as trust and asset management income, deposit related fees, interchange fees, merchant income, and annuity and insurance commissions. However, the recognition of these revenue streams did not significantly change the recognition upon the adoption of ASC 606.

Note 1. Nature of Banking Activities and Significant Accounting Policies (continued)

Segment reporting: The Bank operates in one segment – Community Banking and the financial performance of this one segment is used to make resource allocations and performance decisions.

Reclassifications: Some items in the prior year financial statements were reclassified to conform to the current presentation. Reclassifications had no effect on prior year net income or shareholder's equity.

Recent Accounting Pronouncements

In June 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2016-13: *Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments.* The amendments in this ASU, among other things, require the measurement of all expected credit losses for financial assets held at the reporting date based on historical experience, current conditions, and reasonable and supportable forecasts. Financial institutions and other organizations will now use forward-looking information to better inform their credit loss estimates. Many of the loss estimation techniques applied today will still be permitted, although the inputs to those techniques will change to reflect the full amount of expected credit losses. In addition, the ASU amends the accounting for credit losses on available-for-sale debt securities and purchased financial assets with credit deterioration. For public companies that are not SEC filers, the amendments in this ASU are effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2022. The Bank is currently assessing the impact that ASU 2016-13 will have on its financial statements.

In November 2019, the FASB issued ASU 2019-11: *Codification Improvements to Topic 326, Financial Instruments – Credit Losses.* This ASU addresses issues raised by stakeholders during the implementation of ASU No. 2016-13, "Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments." Among other narrow-scope improvements, the new ASU clarifies guidance around how to report expected recoveries. "Expected recoveries" describes a situation in which an organization recognizes a full or partial write-off of the amortized cost basis of a financial asset, but then later determines that the amount written off, or a portion of that amount, will in fact be recovered. While applying the credit losses standard, stakeholders questioned whether expected recoveries were permitted on assets that had already shown credit deterioration at the time of purchase (also known as PCD assets). In response to this question, the ASU permits organizations to record expected recoveries on PCD assets.

In addition to other narrow technical improvements, the ASU also reinforces existing guidance that prohibits organizations from recording negative allowances for available-for-sale debt securities. The ASU includes effective dates and transition requirements that vary depending on whether or not an entity has already adopted ASU 2016-13. The Bank is currently assessing the impact that ASU 2019-11 will have on its financial statements.

In August 2018, the FASB issued ASU 2018-14*: Compensation—Retirement Benefits—Defined Benefit Plans—General (Subtopic 715-20): Disclosure Framework—Changes to the Disclosure Requirements for Defined Benefit Plans*. These amendments modify the disclosure requirements for employers that sponsor defined benefit pension or other postretirement plans. Certain disclosure requirements have been deleted while the following disclosure requirements have been added: the weighted-average interest crediting rates for cash balance plans and other plans with promised interest crediting rates and an explanation of the reasons for significant gains and losses related to changes in the benefit obligation for the period.

Note 1. Nature of Banking Activities and Significant Accounting Policies (continued)

The amendments also clarify the disclosure requirements in paragraph 715-20-50-3, which state that the following information for defined benefit pension plans should be disclosed: The projected benefit obligation (PBO) and fair value of plan assets for plans with PBOs in excess of plan assets and the accumulated benefit obligation (ABO) and fair value of plan assets for plans with ABOs in excess of plan assets. The amendments are effective for fiscal years ending after December 15, 2021. Early adoption is permitted. The Bank does not expect the adoption of ASU 2018-14 to have a material impact on its financial statements.

In December 2019, the FASB issued ASU 2019-12: *Income Taxes (Topic 740) – Simplifying the Accounting for Income Taxes.* The ASU is expected to reduce cost and complexity related to the accounting for income taxes by removing specific exceptions to general principles in Topic 740 (eliminating the need for an organization to analyze whether certain exceptions apply in a given period) and improving financial statement preparers' application of certain income tax-related guidance. This ASU is part of the FASB's simplification initiative to make narrow-scope simplifications and improvements to accounting standards through a series of short-term projects. The amendments are effective for fiscal years beginning after December 15, 2021. Early adoption is permitted. The Bank is currently assessing the impact that ASU 2019-12 will have on its financial statements.

In March 2020, the FASB issued ASU No. 2020-04: *Reference Rate Reform (Topic 848): Facilitation of the Effects of Reference Rate Reform on Financial Reporting.* These amendments provide temporary optional guidance to ease the potential burden in accounting for reference rate reform. The ASU provides optional expedients and exceptions for applying generally accepted accounting principles to contract modifications and hedging relationships, subject to meeting certain criteria, that reference LIBOR or another reference rate expected to be discontinued. It is intended to help stakeholders during the global market-wide reference rate transition period. The guidance is effective for all entities as of March 12, 2020 through December 31, 2022.

Subsequently, in January 2021, the FASB issued ASU No. 2021-01: *Reference Rate Reform (Topic 848): Scope*. This ASU clarifies that certain optional expedients and exceptions in Topic 848 for contract modifications and hedge accounting apply to derivatives that are affected by the discounting transition. The ASU also amends the expedients and exceptions in Topic 848 to capture the incremental consequences of the scope clarification and to tailor the existing guidance to derivative instruments affected by the discounting transition. An entity may elect to apply ASU No. 2021-01 on contract modifications that change the interest rate used for margining, discounting, or contract price alignment retrospectively as of any date from the beginning of the interim period that includes March 12, 2020, or prospectively to new modifications from any date within the interim period that includes or is subsequent to January 7, 2021, up to the date that financial statements are available to be issued. The Bank does not believe this will have material impacts on its financial statements.

An entity may elect to apply ASU No. 2021-01 to eligible hedging relationships existing as of the beginning of the interim period that includes March 12, 2020, and to new eligible hedging relationships entered into after the beginning of the interim period that includes March 12, 2020. The Bank has limited exposure to the number of loans tied to LIBOR and the loan documents allow for the index to move to an alternative rate if the index currently in place, LIBOR, no longer exists. For any new loans, the Bank is using an alternative rate as an index. ASU 2020-01 will not have material impact on the Bank.

Note 1. Nature of Banking Activities and Significant Accounting Policies (continued)

In March 2020 (revised in April 2020), various regulatory agencies, including the Board of Governors of the Federal Reserve System and the Federal Deposit Insurance Corporation, ("the agencies") issued an interagency statement on loan modifications and reporting for financial institutions working with customers affected by the Coronavirus. The interagency statement was effective immediately and impacted accounting for loan modifications. Under ASC 310-40: *Receivables – Troubled Debt Restructurings by Creditors*, a restructuring of debt constitutes a TDR if the creditor, for economic or legal reasons related to the debtor's financial difficulties, grants a concession to the debtor that it would not otherwise consider. The agencies confirmed with the staff of the FASB that short-term modifications made on a good faith basis in response to COVID-19 to borrowers who were current prior to any relief, are not to be considered TDRs. This includes short-term (e.g., six months) modifications such as payment deferrals, fee waivers, extensions of repayment terms, or other delays in payment that are insignificant. Borrowers considered current are those that are less than 30 days past due on their contractual payments at the time a modification program is implemented. In August 2020, a joint statement on additional loan modifications was issued. Among other things, the Interagency Statement addresses accounting and regulatory reporting considerations for loan modifications, including those accounted for under Section 4013 of the Coronavirus Aid, Relief, and Economic Security (CARES) Act. The CARES Act was signed into law on March 27, 2020 to help support individuals and businesses through loans, grants, tax changes and other types of relief. The most significant impacts of the Act related to accounting for loan modifications and establishment of the PPP. On December 21, 2020, the Consolidated Appropriates Act of 2021 (CAA) was passed. The CAA extends or modifies many of the relief programs first created by the CARES Act, including the PPP and treatment of certain loan modifications related to the COVID-19 pandemic. Additionally, the Bank provided short-term concessions to borrowers as prescribed in the CARES Act. Mainly in the form of interest deferrals. The Bank is closely monitoring particular loan segments and specific loans within its portfolio where it has provided these concessions.

Note 2. Securities

Securities have been classified in the Balance Sheets according to management's intent. The carrying amount of securities and their approximate fair values at December 31, 2021 and 2020, are summarized as follows (in thousands):

	December 31, 2021			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Securities Available for Sale				
U.S. Treasuries and government agencies	**$ 185,085**	**$ 98**	**$ 742**	**$ 184,441**
Obligations of states and municipalities	**651,000**	**20,285**	**5,718**	**665,567**
Residential mortgage backed – agency	**63,568**	**372**	**1,153**	**62,787**
Residential mortgage backed – non-agency	**245,794**	**863**	**2,349**	**244,308**
Commercial mortgage backed – agency	**78,830**	**411**	**358**	**78,883**
Commercial mortgage backed – non-agency	**170,048**	**2,492**	**336**	**172,204**
Asset backed	**192,930**	**3,127**	**532**	**195,525**
Other	**2,000**	**-**	**34**	**1,966**
	$ 1,589,255	**$ 27,648**	**$ 11,222**	**$ 1,605,681**

	December 31, 2020			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Securities Available for Sale				
U.S. Treasuries and government agencies	$ 50,470	$ 648	$ -	$ 51,118
Obligations of states and municipalities	483,187	26,682	296	509,573
Residential mortgage backed – agency	16,680	547	2	17,225
Residential mortgage backed – non-agency	188,807	2,259	480	190,586
Commercial mortgage backed – agency	63,339	368	95	63,612
Commercial mortgage backed – non-agency	132,903	5,567	279	138,191
Asset backed	187,724	2,770	1,098	189,396
Other	-	-	-	-
	$ 1,123,110	$ 38,841	$ 2,250	$ 1,159,701

At December 31, 2021 and 2020, securities with amortized costs of $498.1 million and $610.4 million, respectively, and with estimated fair values of $518.6 million and $641.6 million, respectively, were pledged to secure public deposits, repurchase agreements, and for other purposes required or permitted by law.

The gross realized gains, realized losses, and proceeds from the sale of securities for the years ended December 31, 2021 and 2020 were as follows (in thousands):

	2021	**2020**
Gross realized gains	**$ -**	$ 1,957
Gross realized losses	**(4)**	(13)
Proceeds from sale of securities	**700**	49,116

Note 2. Securities (continued)

The maturities of securities available for sale at December 31, 2021, were as follows: (Expected maturities may differ from contractual maturities because borrowers have the right to call or prepay some obligations with or without call or prepayment penalties)

	December 31, 2021				
	Amortized Cost				
	One Year or Less	One to Five Years	Five to Ten Years	After Ten Years	Total
Securities Available for Sale					
U.S. Treasuries and government agencies	$ 14,988	$ 5,438	$ 164,659	$ -	$ 185,085
Obligations of states and municipalities	49,041	49,378	420,587	131,994	651,000
Residential mortgage backed – agency	44	13,979	49,545	-	63,568
Residential mortgage backed – non-agency	64,774	133,935	42,378	4,707	245,794
Commercial mortgage backed – agency	1,005	49,325	28,500	-	78,830
Commercial mortgage backed – non-agency	19,443	140,441	5,176	4,988	170,048
Asset backed	3,812	31,286	157,832	-	192,930
Other	-	-	2,000	-	2,000
	$ 153,107	$ 423,782	$ 870,677	$ 141,689	$ 1,589,255

	December 31, 2021				
	Fair Value				
	One Year or Less	One to Five Years	Five to Ten Years	After Ten Years	Total
Securities Available for Sale					
U.S. Treasuries and government agencies	$ 15,059	$ 5,289	$ 164,093	$ -	$ 184,441
Obligations of states and municipalities	49,827	52,337	434,156	129,247	665,567
Residential mortgage backed – agency	44	14,350	48,393	-	62,787
Residential mortgage backed – non-agency	64,814	133,111	41,807	4,576	244,308
Commercial mortgage backed – agency	1,024	49,426	28,433	-	78,883
Commercial mortgage backed – non-agency	19,439	142,764	5,020	4,981	172,204
Asset backed	3,809	31,191	160,525	-	195,525
Other	-	-	1,966	-	1,966
	$ 154,016	$ 428,468	$ 884,393	$ 138,804	$ 1,605,681

Note 2. Securities (continued)

The following table shows the gross unrealized losses and fair value of the Bank's securities with unrealized losses that are not deemed to be other-than-temporarily impaired, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position at December 31, 2021 and 2020.

Available for sale securities in a continuous unrealized loss position for less than twelve months and more than twelve months are as follows (in thousands):

	December 31, 2021				
	Less Than Twelve Months		More Than Twelve Months		
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Total Unrealized Losses
Securities Available for Sale					
U.S. Treasuries and government agencies	**$ 134,379**	**$ 392**	**$ 10,082**	**$ 350**	**$ 742**
Obligations of states and municipalities	**218,099**	**4,938**	**14,521**	**780**	**5,718**
Residential mortgage backed – agency	**48,167**	**1,153**	**-**	**-**	**1,153**
Residential mortgage backed – non-agency	**149,640**	**1,624**	**31,024**	**725**	**2,349**
Commercial mortgage backed – agency	**33,703**	**274**	**6,456**	**84**	**358**
Commercial mortgage backed – non-agency	**36,307**	**321**	**4,137**	**15**	**336**
Asset backed	**50,005**	**402**	**17,372**	**130**	**532**
Other	**1,966**	**34**	**-**	**-**	**34**
	$ 672,266	**$ 9,138**	**$ 83,592**	**$ 2,084**	**$ 11,222**

	December 31, 2020				
	Less Than Twelve Months		More Than Twelve Months		
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Total Unrealized Losses
Securities Available for Sale					
U.S. Treasuries and government agencies	**$ -**	**$ -**	**$ -**	**$ -**	**$ -**
Obligations of states and municipalities	**53,213**	**296**	**-**	**-**	**296**
Residential mortgage backed – agency	**274**	**2**	**-**	**-**	**2**
Residential mortgage backed – non-agency	**75,376**	**480**	**5**	**-**	480
Commercial mortgage backed – agency	**3,775**	**24**	**9,994**	**71**	**95**
Commercial mortgage backed – non-agency	**28,472**	**181**	**4,902**	**98**	**279**
Asset backed	**16,937**	**195**	**71,316**	**903**	**1,098**
Other	**-**	**-**	**-**	**-**	**-**
	$ 178,047	**$ 1,178**	**$ 86,217**	**$ 1,072**	**$ 2,250**

Note 2. Securities (continued)

The Bank determines whether unrealized losses are temporary in nature in accordance with U.S. GAAP and the evaluation is based upon factors such as the creditworthiness of the underlying borrowers, performance of the underlying collateral, if applicable, and the level of credit support in the security structure. The Bank also evaluates other factors and circumstances that may be indicative of an OTTI condition. This evaluation includes, but is not limited to, an evaluation of the type of security, length of time and extent to which the fair value has been less than cost, and near-term prospects of the issuer.

FASB ASC 320-10, requires the Bank to assess if an OTTI exists by considering whether the Bank has the intent to sell the security, or more likely than not, will be required to sell the security before recovery. If either of these situations applies, the guidance requires the Bank to record an OTTI charge to earnings on debt securities for the difference between the amortized cost basis and the fair value of the security. If neither of these situations applies, the Bank will assess whether it is expected to recover the entire amortized costs basis of the security. If the Bank is not expected to recover the entire amortized cost basis of the security, we will bifurcate the identified OTTI into a credit loss component and a component representing loss related to other factors.

As of December 31, 2021, the Bank had no cumulative OTTI. There were no OTTI charges in earnings as a result of credit losses on investments in the years ended December 31, 2021 and 2020.

Securities of U.S. Treasury and Federal Agencies and Federal Agency Mortgage (Residential and Commercial) Backed Securities: At December 31, 2021, the unrealized losses associated with U.S. Treasuries and Government Agency securities (10), Residential Mortgage Backed – Agency securities (8), and Commercial Mortgage Backed – Agency securities (14) are generally driven by changes in interest rates and not due to credit losses given the explicit or implicit guarantees provided by the U.S. government.

Securities of U.S. States and Municipalities: At December 31, 2021, the unrealized losses associated with State and Municipal securities (99) were primarily caused by changes in interest rates and not the credit quality of the securities. These investments are investment grade and were generally underwritten in accordance with our own investment standards prior to the decision to purchase, without relying on a bond insurer's guarantee in making the investment decision. These securities will continue to be monitored as part of our ongoing impairment analysis but are expected to perform, even if the rating agencies reduce the credit rating of the bond insurers. As a result, we expect to recover the entire amortized cost basis of these securities.

Residential & Commercial Mortgage Backed – Non-Agency Securities: At December 31, 2021, the unrealized losses associated with Residential Mortgage Backed – Non-Agency securities (41) and Commercial Mortgage Backed – Non-Agency securities (9) are generally driven by changes in interest rates, credit spreads, and projected collateral losses. We assess for credit impairment by estimating the present value of expected cash flows. The key assumptions for determining expected cash flows include default rates, loss severities, and/or prepayment rates. Based on our assessment of the expected credit losses and the credit enhancement level of the securities, we expect to recover the entire amortized cost of these securities.

Note 2. Securities (continued)

Asset Backed Securities: At December 31, 2021, the unrealized losses associated with Asset Backed securities (18) are generally driven by changes in interest rates, credit spreads, and projected collateral losses. We assess for credit impairment by estimating the present value of expected cash flows. The key assumptions for determining expected cash flows include default rates, loss severities, and/or prepayment rates. Based on our assessment of the expected credit losses and the credit enhancement level of the securities, we expect to recover the entire amortized cost of these securities.

Other Securities: At December 31, 2021, the unrealized losses associated with one security was primarily driven by interest rates and not the credit quality of the security. This investment was underwritten in accordance with our own investment standards prior to the decision to purchase, without relying on a bond insurer's guarantee in making the investment decision. This security will continue to be monitored as part of our ongoing impairment analysis, but is expected to perform. As a result, we expect to recover the entire amortized cost basis of this security.

Restricted stock, at cost

The Bank's investment in FHLB stock totaled $12.0 million and $12.1 million at December 31, 2021 and 2020, respectively. FHLB stock is generally viewed as a long-term investment and as a restricted investment security, which is carried at cost, because there is no market for the stock other than the FHLB or member institutions. Therefore, when evaluating FHLB stock for impairment, its value is based on the ultimate recoverability of the par value rather than by recognizing temporary declines in value. The Bank does not consider this investment to be other-than-temporarily impaired at December 31, 2021, and no impairment has been recognized. FHLB stock is included in a separate line item on the Balance Sheets (Restricted stock, at cost) and is not part of the Bank's investment securities portfolio. The Bank's restricted securities also include an investment in Community Bankers' Bank, totaling $50 thousand at both December 31, 2021 and 2020, which is carried at cost.

Note 3. Loans

Major classifications of loans are as follows (in thousands):

		2021		2020
Commercial real estate	**$**	**1,031,641**	$	959,475
Owner-occupied commercial real estate		**125,613**		130,558
Acquisition, construction & development		**109,518**		154,250
Commercial & industrial		**58,818**		134,287
Single family residential (1-4 units)		**415,594**		431,472
Consumer non-real estate and other		**3,889**		23,733
		1,745,073		1,833,775
Allowance for loan losses		**(31,709)**		(32,697)
	$	**1,713,364**	$	1,801,078

Net deferred loan fees included in the above loan categories totaled $4.4 million and $4.9 million at December 31, 2021 and 2020, respectively.

The following tables present, as of December 31, 2021 and 2020, the total allowance for loan losses, the allowance by impairment methodology (individually evaluated or collectively evaluated for impairment), total loans by impairment methodology (individually evaluated or collectively evaluated for impairment) (in thousands):

	December 31, 2021						
	Commercial Real Estate	Owner-occupied Commercial Real Estate	Acquisition, Construction & Development	Commercial & Industrial	Single Family Residential (1-4 units)	Consumer Non-Real Estate and Other	Total
Allowance for loan losses:							
Beginning balance	**$ 23,356**	**$ 1,196**	**$ 4,255**	**$ 68**	**$ 3,757**	**$ 65**	**$ 32,697**
Charge-offs	**(127)**	**-**	**-**	**-**	**(16)**	**(99)**	**(242)**
Recoveries	**13**	**17**	**-**	**20**	**183**	**23**	**256**
Provision	**1,870**	**(602)**	**(886)**	**72**	**(1,490)**	**34**	**(1,002)**
Ending balance	**$ 25,112**	**$ 611**	**$ 3,369**	**$ 160**	**$ 2,434**	**$ 23**	**$ 31,709**
Allowance Ending Balance:							
Individually evaluated	**$ 7,558**	**$ 14**	**$ -**	**$ -**	**$ 107**	**$ -**	**$ 7,679**
Collectively evaluated	**17,554**	**597**	**3,369**	**160**	**2,327**	**23**	**24,030**
Loans:							
Ending balance	**$ 1,031,641**	**$ 125,613**	**$ 109,518**	**$ 58,818**	**$ 415,594**	**$ 3,889**	**$ 1,745,073**
Ending Balance:							
Individually evaluated	**$ 20,110**	**$ 2,843**	**$ -**	**$ -**	**$ 7,831**	**$ -**	**$ 30,784**
Collectively evaluated	**1,011,531**	**122,770**	**109,518**	**58,818**	**407,763**	**3,889**	**1,714,289**

Note 3. Loans (continued)

	December 31, 2020						
	Commercial Real Estate	Owner-occupied Commercial Real Estate	Acquisition, Construction & Development	Commercial & Industrial	Single Family Residential (1-4 units)	Consumer Non-Real Estate and Other	Total
Allowance for loan losses:							
Beginning balance	$ 11,396	$ 2,310	$ 1,697	$ 5,952	$ 2,791	$ 55	$ 24,201
Charge-offs	-	-	-	(5,858)	(44)	(94)	(5,996)
Recoveries	14	-	-	1,726	65	39	1,844
Provision	11,946	(1,114)	2,558	(1,752)	945	65	12,648
Ending balance	$ 23,356	$ 1,196	$ 4,255	$ 68	$ 3,757	$ 65	$ 32,697
Ending Balance:							
Individually evaluated	$ 5	$ 36	$ -	$ -	$ 112	$ -	$ 153
Collectively evaluated	23,351	1,160	4,255	68	3,645	65	32,544
Loans:							
Ending balance	$ 959,475	$ 130,558	$ 154,250	$ 134,287	$ 431,472	$ 23,733	$ 1,833,775
Ending Balance:							
Individually evaluated	$ 974	$ 3,118	$ -	$ -	$ 10,349	$ -	$ 14,441
Collectively evaluated	958,501	127,440	154,250	134,287	421,123	23,733	1,819,334

Note 3. Loans (continued)

The recorded investment in loans excludes accrued interest receivable and loan origination fees, net due to immateriality. The following table presents the aging of the recorded investment in past due loans as of December 31, 2021 and 2020 by class of loans:

Aging and Nonaccrual Loans (in thousands)

	December 31, 2021							
	30-59 Days Past Due	60-89 Days Past Due	90 Days or More Past Due	Total Past Due	Current	Total Loans	90 Days Past Due & Still Accruing	Non-accrual Loans
Commercial real estate	$ -	$ -	$ 19,531	$ 19,531	$ 1,012,110	$ 1,031,641	$ -	$ 19,594
Owner-occupied commercial real estate	121	-	820	941	124,672	125,613	-	1,399
Acquisition, construction & development	-	-	-	-	109,518	109,518	-	-
Commercial & industrial	21	-	-	21	58,797	58,818	-	-
Single family residential (1-4 units)	365	-	649	1,014	414,580	415,594	-	5,268
Consumer non-real estate and other	-	-	-	-	3,889	3,889	-	-
Total	$ 507	$ -	$ 21,000	$ 21,507	$ 1,723,566	$ 1,745,073	$ -	$ 26,261

Note 3. Loans (continued)

	December 31, 2020							
	30-59 Days Past Due	60-89 Days Past Due	90 Days or More Past Due	Total Past Due	Current	Total Loans	90 Days Past Due & Still Accruing	Non-accrual Loans
Commercial real estate	$ -	$ 1,679	$ 417	$ 2,096	$ 957,379	$ 959,475	$ -	$ 20,011
Owner-occupied commercial real estate	779	-	1,284	2,063	128,495	130,558	-	1,615
Acquisition, construction & development	1,152	285	345	1,782	152,468	154,250	345	-
Commercial & industrial	-	-	-	-	134,287	134,287	-	-
Single family residential (1-4 units)	1,141	1,045	1,293	3,479	427,993	431,472	-	6,204
Consumer non-real estate and other	9	-	-	9	23,724	23,733	-	-
Total	$ 3,081	$ 3,009	$ 3,339	$ 9,429	$ 1,824,346	$ 1,833,775	$ 345	$ 27,830

Note 3. Loans (continued)

The following table presents information related to impaired loans by class of loans as of December 31, 2021 and 2020:

Impaired Loans (in thousands)

	December 31, 2021				
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
With no related allowance:					
Commercial real estate	$ -	$ -	$ -	$ -	$ -
Owner-occupied commercial real estate	**2,327**	**2,460**	**-**	**2,437**	**129**
Acquisition, construction & development	-	-	-	-	-
Commercial & industrial	-	-	-	-	-
Single family residential (1-4 units)	**5,673**	**6,230**	**-**	**5,848**	**245**
Consumer non-real estate and other	-	-	-	-	-
With an allowance recorded:					
Commercial real estate	**$ 20,110**	**$ 20,236**	**$ 7,558**	**$ 20,130**	**$ 30**
Owner-occupied commercial real estate	**516**	**516**	**14**	**530**	**32**
Acquisition, construction & development	-	-	-	-	-
Commercial & industrial	-	-	-	-	-
Single family residential (1-4 units)	**2,159**	**2,285**	**107**	**2,203**	**122**
Consumer non-real estate and other	-	-	-	-	-

Note 3. Loans (continued)

	December 31, 2020				
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
With no related allowance:					
Commercial real estate	$ 417	$ 417	$ -	$ 432	$ 12
Owner-occupied commercial real estate	1,615	1,878	-	1,653	69
Acquisition, construction & development	-	-	-	-	-
Commercial & industrial	-	-	-	-	-
Single family residential (1-4 units)	7,157	7,589	-	7,316	271
Consumer non-real estate and other	-	-	-	-	-
With an allowance recorded:					
Commercial real estate	$ 557	$ 557	$ 5	$ 577	$ 35
Owner-occupied commercial real estate	1,503	1,503	36	1,528	70
Acquisition, construction & development	-	-	-	-	-
Commercial & industrial	-	-	-	-	-
Single family residential (1-4 units)	3,192	3,311	112	3,233	152
Consumer non-real estate and other	-	-	-	-	-

Note 3. Loans (continued)

Loans by credit quality indicators as of December 31, 2021 and 2020 were as follows:

Loans by Credit Quality (in thousands)

	December 31, 2021				
	Internal Risk Rating Grades				
	Pass	Special Mention	Substandard	Doubtful	Loss
Commercial real estate	**$ 868,787**	**$ 75,397**	**$ 87,457**	**$ -**	**$ -**
Owner-occupied commercial real estate	**122,065**	**2,149**	**1,399**	**-**	**-**
Acquisition, construction & development	**72,895**	**36,623**	**-**	**-**	**-**
Commercial & industrial	**58,763**	**55**	**-**	**-**	**-**
Single family residential (1-4 units)	**410,227**	**99**	**5,268**	**-**	**-**
Consumer non-real estate and other	**3,889**	**-**	**-**	**-**	**-**
Total	**$ 1,536,626**	**$ 114,323**	**$ 94,124**	**$ -**	**$ -**

	December 31, 2020				
	Internal Risk Rating Grades				
	Pass	Special Mention	Substandard	Doubtful	Loss
Commercial real estate	$ 783,214	$ 101,793	$ 74,468	$ -	$ -
Owner-occupied commercial real estate	124,506	2,999	3,053	-	-
Acquisition, construction & development	105,434	48,816	-	-	-
Commercial & industrial	134,016	271	-	-	-
Single family residential (1-4 units)	422,125	2,379	6,968	-	-
Consumer non-real estate and other	23,733	-	-	-	-
Total	$ 1,593,028	$ 156,258	$ 84,489	$ -	$ -

Note 3. Loans (continued)

There were zero Trouble Debt Restructurings during the years ended December 31, 2021 and 2020, respectively.

There were zero Troubled Debt Restructurings that subsequently defaulted within twelve months of restructuring in the years ending, December 31, 2021 and December 31, 2020, respectively.

For purposes of this disclosure, the Bank defines default as any payment that occurs more than 90 days past the due date, charge-off, or foreclosure subsequent to modification.

As of December 31, 2021 and 2020, there was no other real estate owned. As of December 31, 2021 and 2020, there were no loans in the process of foreclosure.

Note 4. Premises and Equipment

Premises and equipment are included in the Balance Sheets at December 31, 2021 and 2020 were as follows (in thousands):

	Estimated Useful Lives		2021		2020
Cost:					
Land		**$**	**12,791**	$	14,081
Premises	10 – 39 years		**44,109**		45,323
Furniture and equipment	3 – 10 years		**23,792**		24,146
		$	**80,692**	$	83,550
Less accumulated depreciation			**(43,817)**		(43,056)
Net book value		**$**	**36,875**	$	40,494

Depreciation and amortization (e.g. leasehold improvements) expense for the years ended December 31, 2021 and 2020 was $3.2 million and $2.9 million, respectively. As of December 31, 2021, the Bank has one premise held for sale and is accounting for this premise at the lesser of cost or fair value.

Note 5. Deposits

The aggregate amount of time deposits, each with a minimum denomination of $250,000, was approximately $52.4 million and $67.1 million in 2021 and 2020, respectively. There were no brokered time deposits at December 31, 2021 or December 31, 2020. Time deposits through the Certificate of Deposit Account Registry Service (CDARS) program totaled $18.9 million at December 31, 2021, compared to $21.2 million at December 31, 2020. Deposits through the CDARS program are generated from major customers with substantial relationships with the Bank.

At December 31, 2021, the scheduled maturities of time deposits were as follows (in thousands):

Years ending December 31,		
2022	$	247,177
2023		21,469
2024		8,591
2025		3,796
2026		3,819
	$	284,852

At December 31, 2021 and 2020, amounts included in time deposits for individual retirement accounts totaled $42.9 million and $43.7 million, respectively.

Overdrafts of $94 thousand for 2021 and $75 thousand for 2020 were reclassified to loans.

Note 6. Short Term Borrowings

Federal funds purchased: The Bank has unsecured federal fund lines of credit from correspondent banking relationships, which can provide up to $90 million in liquidity. There were no borrowings of federal fund lines of credit outstanding at December 31, 2021 or 2020.

Note 7. Other Borrowed Funds

The Bank has fixed rate advances outstanding with the Federal Home Loan Bank of Atlanta of $275 million and $225 million at December 31, 2021 and 2020, respectively. At December 31, 2021, the interest rate on this debt ranged from 0.1800% to 0.7725%. At December 31, 2020, the interest rate on this debt ranged from 0.6080% to 0.7725%. The weighted average interest rate at December 31, 2021 and 2020 was 0.545% and 0.626%, respectively. The average balance outstanding during 2021 and 2020 was $227.0 million and $216.6 million, respectively.

The Bank has available an $889.1 million line of credit with the Federal Home Loan Bank of Atlanta. Advances on the line are secured by both securities and loans. The amount of securities and loans pledged against the line as of December 31, 2021 and December 31, 2020 were $637.2 million and $681 million, respectively.

The contractual maturities of this debt as of December 31, 2021 are as follows (in thousands):

Due in 2022	$	50,000
Due in 2029		25,000
Due in 2030		200,000
	$	275,000

Note 8. Income Taxes

The income tax expense for 2021 and 2020 was as follows (in thousands):

		2021		2020
Current expense:				
Federal	**$**	**5,564**	$	5,770
State		**372**		-
		5,936		5,770
Deferred expense:				
Federal		**(1,401)**		(3,830)
State		**(258)**		-
	$	**(1,659)**	$	(3,830)
	$	**4,277**	$	1,940

Note 8. Income Taxes (continued)

The following reconciles income taxes reported in the financial statements to taxes that would be obtained by applying statutory tax rates to income before taxes (in thousands):

		2021		2020
Expected taxes using statutory rates	**$**	**8,493**	$	5,972
Benefit of tax exempt income net of nondeductible interest		**(1,993)**		(1,644)
Nontaxable income from life insurance		**(502)**		(496)
Low income tax credits, net of amortization		**(1,843)**		(1,231)
State taxes, net of federal benefit		**294**		-
Other adjustment, net		**(172)**		(661)
	$	**4,277**	$	1,940

The net deferred tax amounts in the accompanying Balance Sheets include the following components (in thousands):

		2021		2020
Deferred tax assets:				
Provision for loan losses	**$**	**6,962**	$	7,156
Lease Liability		**2,451**		2,345
Compensation accruals		**1,184**		1,100
Other		**1,954**		1,995
Tax credit carryforward		**7,272**		5,765
	$	**19,823**	$	18,361
Deferred tax liabilities:				
Unrealized gains on securities available for sale		**(3,449)**		(7,684)
Tax over book depreciation		**(1,369)**		(1,506)
Pension accrual		**(890)**		(873)
Right of use asset		**(2,349)**		(2,298)
	$	**(8,057)**	$	(12,361)
Net deferred tax asset	**$**	**11,766**	$	6,000

The Bank files income tax returns in the U.S. federal and applicable state jurisdictions. The Bank is no longer subject to tax examination by tax authorities for years prior to 2018.

Note 9. Defined Benefit Pension Plan

The Bank provides pension benefits for eligible employees through a defined benefit pension plan. Employees hired prior to June 1, 2005 participate in the retirement plan on a non-contributing basis and were fully vested after five years of service. The following tables set forth the Plan's status and related disclosures (in thousands):

		2021		2020
Changes in benefit obligation:				
Benefit obligation at beginning of year	**$**	**43,371**	$	36,668
Service cost		**998**		911
Interest cost		**1,042**		1,159
Actuarial (gain) loss		**(2,131)**		5,599
Distributions		**(983)**		(966)
Benefit obligation at end of year	**$**	**42,297**	$	43,371
Change in plan assets:				
Fair value of plan assets at beginning of year	**$**	**47,526**	$	41,333
Adjustment to beginning of year fair value		**-**		(56)
Actual return on plan assets		**(526)**		7,215
Employer contribution		**-**		-
Distributions		**(983)**		(966)
Fair value of plan assets at end of year	**$**	**46,017**	$	47,526
Funded status recognized as accrued pension cost	**$**	**3,720**	$	4,155
Amounts recognized in accumulated other comprehensive (income) loss:				
Net loss	**$**	**7,621**	$	8,008
Deferred income tax benefit		**(1,601)**		(1,683)
Total amount recognized	**$**	**6,020**	$	6,325
Accumulated benefit obligation	**$**	**38,315**	$	38,879

At December 31, 2021 and 2020, the assumptions used to determine the benefit obligation were as follows:

	2021	2020
Discount rate	**2.76%**	2.42%
Rate of compensation increase	**3.50%**	3.50%

Note 9. Defined Benefit Pension Plan (continued)

	2021	2020
Components of net periodic pension cost:		
Service cost	**$ 998**	$ 911
Interest cost	**1,042**	1,159
Expected return on plan assets	**(1,612)**	(1,938)
Amortization of prior service cost	**-**	-
Amortization of net loss	**393**	488
Net periodic pension cost	**$ 821**	$ 620
Other changes recognized in other comprehensive (income) loss:		
Net loss	**$ 7**	$ 378
Amortization of net loss	**(393)**	(488)
Deferred tax expense	**81**	23
Total recognized in accumulated other comprehensive (income) loss	**$ (305)**	$ (87)
Total recognized in net periodic pension cost and other comprehensive loss	**$ 516**	$ 533

For the years ended December 31, 2021 and 2020, the assumptions used to determine net periodic pension cost were as follows:

	2021	2020
Discount rate	**2.76%**	2.42%
Expected long-term rate of return on plan assets	**3.75%**	5.10%
Annual salary increase	**3.50%**	3.50%

The expected long-term return on plan assets assumption was developed as a weighted average rate based on the target asset allocation of the plan and the long-term capital market assumptions. The overall return for each asset class was developed by combining a long-term inflation component and the associated expected real rates. The development of the capital market assumptions utilized a variety of methodologies, including, but not limited to, historical analysis, stock valuation models, such as dividend discount models, and earnings yield models, expected economic growth outlook, and market yields analysis.

The Bank's pension plan asset allocations at December 31, 2021 and 2020, were as follows:

	2021	2020
Equity securities	**11%**	11%
Debt securities	**89%**	89%
Total	**100%**	100%

Note 9. Defined Benefit Pension Plan (continued)

As of December 31, 2021 and 2020, the fair value of plan assets was as follows (in thousands):

	December 31, 2021			
	Fair Value Measurements Using			
	Level 1	Level 2	Level 3	Assets at Fair Value
Cash and cash equivalents	**$ 82**	**$ -**	**$ -**	**$ 82**
Equity securities	**-**	**5,154**	**-**	**5,154**
Debt securities	**-**	**40,782**	**-**	**40,782**
Total pension assets	**$ 82**	**$ 45,936**	**$ -**	**$ 46,018**

	December 31, 2020			
	Fair Value Measurements Using			
	Level 1	Level 2	Level 3	Assets at Fair Value
Cash and cash equivalents	$ 77	$ -	$ -	$ 77
Equity securities	-	5,242	-	5,242
Debt securities	-	42,207	-	42,207
Total pension assets	$ 77	$ 47,449	$ -	$ 47,526

Assets are valued using a combination of methods including quoted prices for similar assets in active or non-active markets.

The fund is sufficiently diversified to maintain a reasonable level of risk without imprudently sacrificing return, with a targeted asset allocation of 9% equities and 91% fixed income and cash. Investments are selected by officers experienced in financial matters and risk management, and implementation of approved investment strategies is monitored on a regular basis. Both actively and passively managed investment strategies are considered, and funds are allocated across asset classes to develop an efficient investment structure.

It is the responsibility of the trustee to consider costs in administering the portfolio, while maintaining high quality investments. Costs include, but are not limited to, management and custodial fees, consulting fees, transaction costs, and other administrative costs which may be charged to the trust.

The Bank does not expect to contribute to its pension plan in 2022.

Note 9. Defined Benefit Pension Plan (continued)

Estimated future benefit payments, which reflect expected future service, as appropriate, are as follows (in thousands):

Years Ending December 31,		
2022	$	1,339
2023		1,392
2024		1,405
2025		1,390
2026		1,438
2027-2031		8,706

Note 10. Investment and Savings Plan

The Bank has an investment and savings plan for its employees. In the month following date of hire, an employee is eligible to participate in the investment and savings plan if they are at least 18 years old. A participant may elect to defer up to 90% of their annual compensation, not to exceed limitations established by the Internal Revenue Code. The Bank contributes on behalf of each participant who makes the election an amount up to 3.5% of the amount contributed by the participant. The Bank's contributions in 2021 and 2020 totaled $1.02 million and $990 thousand, respectively, which was included within pensions and other employee benefits on the Statements of Income.

Note 11. Retirement Plans

The Bank has a deferred compensation plan for some of its directors and senior officers that provides benefits payable at age 65. The deferred compensation is to be paid to the individual or beneficiary over a period of 15 years. Amounts deferred are invested in increasing whole life insurance policies on the participants' lives with the Bank as owner and beneficiary. Amounts recognized for the increase in the cash surrender value of the policies are offset against the expense. The Bank recognized net income of $57 thousand in 2021 and $51 thousand in 2020, related to this deferred compensation plan.

In 2021, the Bank formed a new deferred compensation plan (2021 Deferred Compensation Plan) for current directors and senior officers. The plan is funded with director fees and salary reductions which are placed in a trust account invested by the Bank. The trust investments consist of the Bank's stock, fixed income investments, and cash. The trust account balance totaled $108 thousand at December 31, 2021 and is directly offset in other liabilities. Expenses for the trust totaled $104 thousand in 2021.

In 2010, the Bank adopted a Supplemental Executive Retirement Plan for a number of its executive officers. The plan is intended to be unfunded and maintained primarily for the purpose of providing deferred compensation to its participants. The benefits of the plan vest incrementally based on years of service. Plan expenses for the years ending December 31, 2021 and 2020, amounted to $459 thousand and $442 thousand, respectively.

Note 12. Leased Property

Long term leases at twelve of the Bank's locations are classified as operating leases, while one lease entered into in the fourth quarter of 2020 has been classified as a finance lease upon management's assessment. Certain leases offer the option to extend the lease term, and the Bank has included such extensions in its calculation of the lease liabilities to the extent the options are reasonably assured of being exercised. The 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. The right-of-use asset and lease liability are included in other assets and other liabilities, respectively, in the Balance Sheets.

The following tables present information about the Bank's operating leases:

As of December 31, 2021 (dollars in thousands):		
Lease liabilities	$	8,268
Right-of-use assets		7,869
Weighted average remaining lease term		4.12 years
Weighted average discount rate		2.89%
Operating lease cost (in thousands)	$	2,517
Cash paid for amounts included in the measurement of operating lease liabilities (in thousands)	$	2,141

As of December 31, 2020 (dollars in thousands)		
Lease liabilities	$	9,108
Right-of-use assets		8,902
Weighted average remaining lease term		4.57 years
Weighted average discount rate		2.94%
Operating lease cost (in thousands)	$	2,344
Cash paid for amounts included in the measurement of operating lease liabilities (in thousands)	$	2,304

Note 12. Leased Property (continued)

A maturity analysis of operating lease liabilities and reconciliation of the undiscounted cash flows to the total of operating lease liabilities at December 31, 2021 is as follows:

Lease payments due (in thousands):		
Twelve months ending December 31, 2022	$	2,303
Twelve months ending December 31, 2023		2,373
Twelve months ending December 31, 2024		2,053
Twelve months ending December 31, 2025		682
Twelve months ending December 31, 2026		320
Twelve months ending December 31, 2027		267
Thereafter		560
Total undiscounted cash flows	$	8,558
Discount		(290)
Lease Liabilities	$	8,268

The following tables present information about the Bank's finance lease:

As of December 31, 2021 (dollars in thousands):		
Lease liabilities	$	2,897
Right-of-use assets		2,824
Weighted average remaining lease term		13.76 years
Weighted average discount rate		2.22%
Lease Cost As of December 31, 2021 (dollars in thousands):		
Amortization of right-of-use asset	$	34
Interest on lease liability		11
Total lease cost	$	45
Cash paid for amounts included in the measurement of finance lease liabilities (in thousands)	$	36
As of December 31, 2020 (dollars in thousands)		
Lease liabilities	$	2,059
Right-of-use assets		2,040
Weighted average remaining lease term		9.76 years
Weighted average discount rate		1.70%
Lease Cost As of December 31, 2020 (dollars in thousands)		
Amortization of right-of-use asset	$	34
Interest on lease liability		6
Total lease cost	$	40
Cash paid for amounts included in the measurement of finance lease liabilities (in thousands)	$	22

Note 12. Leased Property (continued)

A maturity analysis of the finance lease liability and reconciliation of the undiscounted cash flows to the total of finance lease liabilities as of December 31, 2021 is as follows:

Lease payments due (in thousands):		
Twelve months ending December 31, 2022	$	215
Twelve months ending December 31, 2023		220
Twelve months ending December 31, 2024		224
Twelve months ending December 31, 2025		228
Twelve months ending December 31, 2026		233
Twelve months ending December 31, 2027		238
Thereafter		2,033
Total undiscounted cash flows	$	3,391
Discount		(494)
Lease Liability	$	2,897

Note 13. Regulatory Matters

As of December 31, 2021, the most recent notification from the FDIC categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, the Bank must maintain minimum total risk-based, Common Equity Tier 1 risk-based, Tier 1 risk-based, and Tier 1 leverage ratios as set forth in the table below. There are no conditions or events since that notification that management believes have changed the Bank's well capitalized category.

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 Bank's 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 regulators regarding components, risk weightings, and other factors.

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios of Total, Common Equity Tier 1, and Tier 1 Capital (as defined in the regulations) to risk weighted assets (as defined) and Tier 1 Capital (as defined) to average assets (as defined). Management believes, as of December 31, 2021 and 2020, the Bank met all capital adequacy requirements to which it was subject.

Note 13. Regulatory Matters (continued)

The table below also reflects the actual and required capital amounts (in millions) and ratios are presented below at year-end.

	Actual		Minimum Required For Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2021:						
Total capital (to risk-weighted assets)	**$ 409,923**	**18.84%**	**$ 174,050**	**≥8%**	**$ 217,562**	**≥10%**
Tier I common equity (to risk-weighted assets)	**382,672**	**17.59**	**97,903**	**>4.5**	**141,415**	**>6.5**
Tier I capital (to risk-weighted assets)	**382,672**	**17.59**	**130,537**	**≥6**	**174,050**	**≥8**
Tier I capital (to average assets)	**382,672**	**10.81**	**141,594**	**≥4**	**176,992**	**≥5**
As of December 31, 2020:						
Total capital (to risk-weighted assets)	$ 390,274	17.47%	$ 178,672	≥8%	$ 223,340	≥10%
Tier I common equity (to risk-weighted assets)	362,297	16.22	100,503	>4.5	145,171	>6.5
Tier I capital (to risk-weighted assets)	362,297	16.22	134,004	≥6	178,672	≥8
Tier I capital (to average assets)	362,297	10.75	134,762	≥4	168,453	≥5

At December 31, 2021, approximately $181.5 million of retained earnings was available for dividend declaration without regulatory approval.

Note 14. Derivatives, Commitments and Contingencies

Derivatives not designated as hedges: The Bank enters into interest rate swaps with its loan customers to facilitate their financing requests. Upon entering into swaps with our loan customers, the Bank will enter into corresponding offsetting derivatives with third parties. These derivatives represent economic hedges and do not qualify as hedges for accounting. These back-to-back loan swaps are reported at fair value in "other assets" and "other liabilities" in the Bank's Balance Sheet. Changes in the fair value of loan swaps are recorded in other noninterest expense and sum to zero because of offsetting terms of swaps with borrowers and swaps with dealer counterparties.

A summary of the Bank's interest rate swaps at December 31, 2021 and 2020, is as follows (in thousands):

	December 31, 2021	
Interest rate swap agreements:	Notional Amount	Estimated Fair Value
Pay fixed/receive variable swaps	**$ 37,508**	**$ (1,589)**
Pay variable/receive fixed swaps	**37,508**	**1,589**

	December 31, 2020	
Interest rate swap agreements:	Notional Amount	Estimated Fair Value
Pay fixed/receive variable swaps	$ 38,490	$ (3,275)
Pay variable/receive fixed swaps	38,490	3,275

Interest rate lock commitments: At December 31, 2021, the Bank had interest rate lock commitments with respect to origination of mortgages through its consumer mortgage business. The Bank has entered into corresponding commitments with third party investors to sell each of these loans that close. As a result of these agreements with investors, the Bank is not exposed to losses with respect to the rate lock commitments. Interest rate lock commitments were $13 thousand and $645 thousand at December 31, 2021 and 2020, respectively. The notional amount of loan pipeline that resulted in interest rate lock commitments at December 31, 2021 and 2020 was $926 thousand and $24.7 million, respectively. Rate lock commitments and forward sales contracts with loan customers and dealer counterparties are not designated as hedging instruments, and therefore changes in the fair value of these instruments are reported as noninterest income and noninterest expense, as applicable.

Credit extension commitments: The Bank's financial statements do not reflect various financial instruments which arise in the normal course of business and which involve elements of credit risk, interest rate risk and liquidity risk. These financial instruments include commitments to extend credit, commercial letters of credit, and revolving lines of credit.

Note 14. Derivatives, Commitments and Contingencies (continued)

A summary of the contractual amounts of the Bank's financial instruments outstanding at December 31, 2021 and 2020, is as follows (in thousands):

	2021	2020
Commitments to extend credit	**$ -**	$ 27,084
Commercial letters of credit	**7,660**	9,031
Undisbursed balance—revolving lines of credit	**240,179**	219,138

Commitments to extend credit, commercial letters of credit and revolving lines of credit all include exposure to some credit loss in the event of nonperformance of the customer. The Bank's credit policies and procedures for credit commitments and financial guarantees are the same as those for extensions of credit that are recorded on the Balance Sheets. Many of these instruments have fixed maturity dates, and many of them will expire without being drawn upon; accordingly, they do not generally present any significant liquidity risk to the Bank.

Litigation: The Bank is a party to litigation and claims arising in the normal course of business. Management, after consultation with legal counsel, believes that the liabilities, if any, arising from such litigation and claims will not be material to the Bank's financial position.

Note 15. Transactions with Related Parties

Directors and principal officers of the Bank, including their immediate families and affiliated companies in which they have a direct or indirect material interest, are considered to be related parties.

Aggregate loan balances with related parties were as follows (in thousands):

(Dollars In Thousands)	**2021**
Balance, beginning	**$ 31,127**
New loans	**12,941**
Repayments	**(3,323)**
Balance, December 31	**$ 40,745**

Deposits from related parties at year-end 2021 and 2020 were as follows (in thousands):

	2021	2020
Balance, December 31	**$ 100,650**	$ 96,858

Note 16. Fair Value Measurements

Determination of Fair Value

Fair value is the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. There are three levels of inputs that may be used to measure fair values:

Level 1 – Quoted prices (unadjusted) for identical assets or liabilities in active markets that the entity has the ability to access as of the measurement date.

Level 2 – Significant other observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.

Level 3 – Significant unobservable inputs that reflect our own assumptions that market participants would use in pricing an asset or liability.

The Bank used the following methods and significant assumptions to estimate fair value:

Securities available for sale: Securities available for sale are recorded at fair value on a recurring basis. Fair value measurement is based upon quoted market prices, when available (Level 1). If quoted market prices are not available, fair values are measured utilizing independent valuation techniques of identical or similar securities for which significant assumptions are derived primarily from or corroborated by observable market data. Third party vendors compile prices from various sources and may determine the fair value of identical or similar securities by using price models that consider observable market data (Level 2). For securities where quoted prices or market prices of similar securities are not available, fair values are calculated using discounted cash flows or other market indicators (Level 3).

Derivatives: The fair values of derivatives are based on valuation models using observable market data as of the measurement date (Level 2). The Bank has contracted with a third party vendor to provide valuations for interest rate swaps using standard swap valuation techniques. The Bank has considered counterparty credit risk in the valuation of its interest rate swap assets and has considered its own credit risk in the valuation of its interest rate swap liabilities. The Bank recognizes interest rate lock commitments at fair value. Fair value of interest rate lock commitments is based on the price of underlying loans obtained from an investor for loans that will be delivered on a best effort basis (Level 2).

Loans held for sale, at fair value: The fair value of loans held for sale is determined using quoted prices for similar assets, adjusted for specific attributes of that loan (Level 2). These loans currently consist of one-to-four family residential loans originated for sale in the secondary market. Gains and losses on the sale of loans are recorded within noninterest income on the Statements of Income. Loans held for sale were $1.2 million at December 31, 2021 and were $8.2 million at December 31, 2020, respectively.

Note 16. Fair Value Measurements (continued)

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

Impaired loans: Loans are designated as impaired, when, in the judgment of management based on current information and events, it is probable that all amounts due according to the contractual terms of the loan agreement will not be collected when due. The measurement of loss associated with impaired loans can be based on either the observable market price of the loan or the fair value of the collateral. Generally, the fair value of impaired loans with specific allocations of the allowance for loan losses is based on recent real estate appraisals. Fair value is measured based on the value of the collateral securing the loans, less estimated costs of disposal. Collateral may be in the form of real estate or business assets including equipment, inventory, and accounts receivable. The vast majority of the collateral is real estate. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Any fair value adjustments are recorded in the period incurred as provision for loan losses on the Statements of Income and will result in a Level 3 fair value classification. Non-real estate collateral may be valued using an appraisal, net book value per the borrower's financial statements, or aging reports, adjusted or discounted based on management's historical knowledge, changes in market conditions from the time of the valuation, and management's expertise and knowledge of the client and client's business, resulting in a Level 3 fair value classification.

Other real estate owned: Assets acquired through foreclosure or other proceedings are initially recorded at fair value less costs to sell when acquired, establishing a new cost basis. These assets are subsequently accounted for at lower of cost or fair value less estimated costs to sell. Fair value is commonly based on recent real estate appraisals which are updated no less frequently than annually. Any fair value adjustments are recorded in the period incurred and expensed against current earnings.

Note 16. Fair Value Measurements (continued)

Assets and liabilities measured at fair value on a recurring basis are summarized below (in thousands):

		Fair Value Measurements Using:		
	Balance	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
As of December 31, 2021:				
Financial Assets				
Securities available for sale:				
U.S. Treasuries and government agencies	**$ 184,441**	**$ 169,382**	**$ 15,059**	**$ -**
Obligations of state and municipalities	**665,567**	**-**	**665,567**	**-**
Residential mortgage backed - agency	**62,787**	**-**	**62,787**	**-**
Residential mortgage backed – non agency	**244,308**	**-**	**244,308**	**-**
Commercial mortgage backed – agency	**78,883**	**-**	**78,883**	**-**
Commercial mortgage backed – non agency	**172,204**	**-**	**172,204**	**-**
Asset backed	**195,525**	**-**	**195,525**	**-**
Other	**1,966**	**-**	**1,966**	**-**
Total	**$ 1,605,681**	**$ 169,382**	**$ 1,436,299**	**$ -**
Loans held for sale	**$ 1,249**	**$ -**	**$ 1,249**	**$**
Derivatives	**$ 1,603**	**$ -**	**$ 1,603**	**$ -**
Financial Liabilities				
Derivatives	$ **1,589**	**$ -**	**$ 1,589**	**$ -**
As of December 31, 2020:				
Financial Assets				
Securities available for sale:				
U.S. Treasuries and government agencies	$ 51,118	$ 10,560	$ 40,558	$ -
Obligations of state and municipalities	509,573	-	509,573	-
Residential mortgage backed - agency	17,225	-	17,225	-
Residential mortgage backed – non agency	190,586	-	190,586	-
Commercial mortgage backed – agency	63,612	-	63,612	-
Commercial mortgage backed – non agency	138,191	-	138,191	-
Asset backed	189,396	-	189,396	-
Other	-	-	-	-
Total	$ 1,159,701	$ 10,560	$ 1,149,141	$
Loans held for sale	$ 8,211	$ -	$ 8,211	$
Derivatives	$ 3,749	$ -	$ 3,479	$ -
Financial Liabilities				
Derivatives	$ 3,275	$ -	$ 3,275	$ -

Note 16. Fair Value Measurements (continued)

Assets that were measured at fair value on a nonrecurring basis during the period are summarized below (in thousands):

	Total	Fair Value Measurements Using: Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
As of December 31, 2021:				
Impaired loans:				
Commercial real estate	**$ 12,552**	**$ -**	**$ -**	**$ 12,552**
Owner-occupied commercial real estate	**502**	**-**	**-**	**502**
Acquisition, construction & development	**-**	**-**	**-**	**-**
Commercial & industrial	**-**	**-**	**-**	**-**
Single family residential	**2,052**	**-**	**-**	**2,052**
Consumer non-real estate and other	**-**	**-**	**-**	**-**
Other real estate owned	**-**	**-**	**-**	**-**
As of December 31, 2020:				
Impaired loans:				
Commercial real estate	$ 552	$ -	$ -	$ 552
Owner-occupied commercial real estate	1,468	-	-	1,468
Acquisition, construction & development	-	-	-	-
Commercial & industrial	-	-	-	-
Single family residential	3,080	-	-	3,080
Consumer non-real estate and other	-	-	-	-
Other real estate owned	-	**-**	**-**	-

The following table presents quantitative information about Level 3 Fair Value Measurements for assets measured at fair value on a non-recurring basis at December 31, 2021 and 2020 (in thousands):

Description	Fair Value	Valuation Techniques	Unobservable Inputs	Range	Weighted Average
As of December 31, 2021:					
Assets					
Impaired loans	**$ 15,106**	Discounted appraised value		7% - 9%	8%
		Discounted cash flow analysis	Market rate for borrower	4% - 6%	5.40%
As of December 31, 2020:					
Assets					
Impaired loans	$ 5,100	Discounted appraised value		6% - 9%	8%
		Discounted cash flow analysis	Market rate for borrower	3.25% - 6%	4.9%

Note 16. Fair Value Measurements (continued)

Fair values of financial instruments

The carrying amounts and estimated fair values of financial instruments not carried at fair value, at December 31, 2021 and 2020 were as follows (in thousands):

	Carrying Amount	Fair Value Measurements: Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
At December 31, 2021:					
Financial assets:					
Cash and due from banks	**$ 8,989**	**$ 8,989**	**$ -**	**$ -**	**$ 8,989**
Interest-bearing deposits with banks	**68,374**	**68,374**	**-**	**-**	**68,374**
Loans, net	**1,713,364**	**-**	**-**	**1,697,752**	**1,697,752**
Accrued interest	**15,253**	**-**	**15,253**	**-**	**15,253**
Financial liabilities:					
Non-interest, bearing	**$ 930,847**	**$ -**	**$ 930,847**	**$ -**	**$ 930,847**
Interest bearing	**2,002,570**	**-**	**2,002,089**	**-**	**2,002,089**
Other borrowed funds	**275,000**	**-**	**274,999**	**-**	**274,999**
Accrued interest	**309**	**-**	**309**	**-**	**309**

	Carrying Amount	Fair Value Measurements: Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
At December 31, 2020:					
Financial assets:					
Cash and due from banks	$ 14,670	$ 14,670	$ -	$ -	$ 14,670
Interest-bearing deposits with banks	214,034	214,034	-	-	214,034
Loans, net	1,801,078	-	-	1,795,719	1,795,719
Accrued interest	13,784	-	13,784	-	13,784
Financial liabilities:					
Non-interest, bearing	$ 852,008	$ -	$ 852,008	$ -	$ 852,008
Interest bearing	1,937,438	-	1,936,955	-	1,936,955
Other borrowed funds	225,000	-	214,029	-	214,029
Accrued interest	417	-	417	-	417

Note 17. Common Stock Transactions

During 2021, the Bank purchased shares of its own common stock on the open market in arms-length transactions. It acquired 2,251 shares at an aggregate cost of $4.4 million at prices ranging from $1,810 to $2,000 per share. Additionally, in 2021, the Bank sold 1,600 shares at $2,000 per share and reissued 43 shares of treasury stock to satisfy the vesting of restricted stock units.

In 2020, the Bank acquired 756 shares at an aggregate cost of $1.545 million at prices ranging from $1,875 to $2,250 per share.

During 2021 and 2020, the Bank declared and paid cash dividends of $80 per share.

Note 18. Accumulated Other Comprehensive Income

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

	Net Unrealized Gains (Losses) on Securities	Adjustments Related to Pension and Other Post Retirement Benefits	Accumulated Other Comprehensive Income (Loss)
Balance at December 31, 2019	$ 7,838	$ (6,412)	$ 1,426
Unrealized holding gains/(losses), net of tax of ($6,008)	22,603	-	22,603
Reclassification adjustment for (gains)/losses on securities, net of tax of ($408)	(1,536)	-	(1,536)
Changes in pension plan benefits, net of tax of ($23)	-	87	87
Balance at December 31, 2020	$ 28,905	$ (6,325)	$ 22,580
Unrealized holding gains/(losses), net of tax of $4,236	**(15,933)**	**-**	**(15,933)**
Reclassification adjustment for (gains)/losses on securities, net of tax of $1	**3**	**-**	**3**
Changes in pension plan benefits, net of tax of ($81)	**-**	**305**	**305**
Balance at December 31, 2021	$ **12,975**	**$** **(6,020)**	**$** **6,955**

Note 19. Reclassifications Out of Accumulated Other Comprehensive Income

Details about Accumulated Other Comprehensive Income Components	Amounts Reclassified from Accumulated Other Comprehensive Income (Loss) 2021	2020	Affected Line Item in the Statements of Income
Available for sale securities:			
Realized gain/(loss) on sales	**$ (4)**	$ 1,944	Net gains/(losses) on securities
	(4)	1,944	Income before income taxes
	1	(408)	Income tax expense (benefit)
	(3)	1,536	Net income
Defined benefit pension plan items:			
Amortization of actuarial gain/(loss)	**386**	110	Pension and other employee benefits
	386	110	Income before income taxes
	(81)	(23)	Income tax expense (benefit)
	305	87	Net income
Total reclassifications	**$ 302**	$ 1,623	Net income

Note: The Defined benefit pension plan items are included in the computation of net periodic pension cost. See Note 9, *Defined Benefit Pension Plan*, for additional information.

Note 20. Other Operating Expense

Other Operating Expense from the Statements of Income for years ended December 31, 2021 and 2020 is as follows (in thousands):

	2021	**2020**
Directors' Fees	**$ 1,093**	$ 1,147
Consultant fees	**1,548**	1,064
Advertising expense	**1,086**	509
Historic tax credit amortization	**2,717**	2,718
Virginia franchise tax	**2,366**	2,249
(Recapture of) Provision for off-balance sheet exposure	**-**	(1,380)
Network expense	**1,592**	1,459
FDIC assessment	**920**	460
IT related	**1,306**	965
(Gain)/loss on sale of building	**(1,063)**	7
Other	**6,204**	6,552
Total	**$ 17,769**	$ 15,750

Note 21. Qualified Affordable Housing Project and Historic Tax Investments

The Bank invests in qualified affordable housing projects. At December 31, 2021 and 2020, the balance of the investment for qualified affordable housing projects was $29.7 million and $36.4 million, respectively. These balances are reflected in the other assets line on the Balance Sheets. Total unfunded commitments related to the investments in qualified affordable housing projects totaled $1.6 million and $1.7 million at December 31, 2021 and 2020, respectively. The Bank expects to fulfill the majority of these commitments during 2022.

During the year ended December 31, 2021 and 2020, the Bank recognized total amortization expense of $6.8 million and $7.1 million, respectively. In both 2021 and 2020, $2.7 million was included in noninterest expense on the Statements of Income related to historic tax credit investments that do not qualify for the proportional amortization method. The remainder of the amortization expense was recorded as income tax expense.

Note 22. Revenue from Contracts with Customers

The Bank's revenue from contracts with customers in the scope of ASC 606 is recognized within noninterest income. ASC 606 is applicable to noninterest revenue streams such as trust and wealth management income, deposit related fees, interchange fees, merchant income, and annuity and insurance commissions. A description of the Bank's revenue streams accounted for under ASC 606 follows:

Income from fiduciary & wealth management activities
Fiduciary and wealth management income is primarily comprised of fees earned from the management and administration of trusts and other customer assets. The Bank'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 Bank 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 Bank's performance obligation for these transactional-based services is generally satisfied at a point in time (i.e., as incurred), and that allows the Bank to recognize the related revenue associated with that transaction. Payment is received shortly after services are rendered.

Annuity and insurance income primarily consists of commissions received on annuity product sales. The Bank acts as an intermediary between the Bank's customer and the insurance carrier. The Bank's performance obligation is generally satisfied upon the issuance of the annuity policy. Shortly after the policy is issued, the carrier remits the commission payment to the Bank, and the Bank recognizes the revenue. The Bank does not earn a significant amount of trailer fees on annuity sales. The majority of the trailer fees relates to variable annuity products and are calculated based on a percentage of market value at period end. Revenue is not recognized until the annuity's market value can be determined.

Other noninterest income consists of other recurring revenue streams, such as commissions from sales of mutual funds and other investments, investment advisor fees from the Bank's wealth management product, safety deposit box rental fees, and other miscellaneous revenue streams. Commissions from the sale of mutual funds and other investments are payable on the trade date and are received in the following month, which is when the Bank has satisfied its performance obligation. The Bank also receives periodic service fees (i.e., trailers) from mutual fund companies typically based on a percentage of net asset value. Trailer revenue is recorded over time, usually monthly or quarterly, as net asset value is determined. Investment

Note 22. Revenue from Contracts with Customers (continued)

advisor fees from the wealth management product are earned over time and based on an annual percentage rate of the net asset value. The investment advisor fees are charged to the customer's account in advance on the first month of the quarter, and the revenue is recognized over the following three-month period.

Service charges and fees
Service charges and fees on deposit accounts consist of monthly service fees, check orders, and other deposit account related fees. Check orders and other deposit account related fees are largely transactional based, and therefore, the Bank's performance obligation is satisfied at a point in time, and the related revenue recognized. Payment for service charges on deposit accounts is primarily received immediately or in the following month through a direct charge to customers' accounts.

Fees, exchange, and other service charges are primarily comprised of debit and credit card income, ATM fees, merchant services income, and other service charges. Debit and credit card income is primarily comprised of interchange fees earned whenever the Bank's debit and credit cards are processed through card payment networks such as Visa. Merchant services income mainly consists of fees charged to merchants to process their debit and credit card transactions, in addition to account management fees. Other service charges include revenue from processing wire transfers, bill pay service, cashier's checks, and other services. The Bank's performance obligation for fees, exchange, and other service charges are largely satisfied, and related revenue recognized, when the services are rendered or upon completion. Payment is typically received immediately or in the following month.

Safe deposit box rental fees are charged to the customer on an annual basis and recognized upon receipt of payment. The Bank determined that since rentals and renewals occur fairly consistently over time, revenue is recognized on a basis consistent with the duration of the performance obligation.

Note 23. Stock-Based Compensation

The Bank has one share-based incentive plan described below that allows it to offer a variety of equity compensation awards subject to approval. Total compensation cost that has been charged against income for the awards granted was $283 thousand and $146 thousand for 2021 and 2020, respectively. The total income tax benefit was $59 thousand and $31 thousand for 2021 and 2020, respectively.

<u>2019 Stock Incentive Plan</u>
In 2019, the Bank's Stock Incentive Plan (2019 Plan) was approved by the Board of Directors. Since 2019 Plan's approval, the Bank has issued Restricted Stock Units (RSUs) that vest based on a service condition. Each approved RSU award indicates the number of RSUs and the required service period in order for the RSU award to vest. As these awards vest, the number of RSUs will convert to an equal number of shares of the Bank. The Bank has a policy of using shares held as treasury stock to satisfy vested awards. Currently, the Bank has a sufficient number of treasury shares to satisfy expected vesting of awards.

The fair value for each RSU is based on the fair value of the share of the Bank as of the grant date. As of December 31, 2021, there was $617 thousand of total unrecognized compensation cost related to nonvested RSUs granted under the plan. The cost is expected to be recognized over a weighted average period of 1.5 years.

Note 24. Earnings Per Share

Basic earnings per share excludes dilution and is computed by dividing net income by the weighted average number of common shares outstanding for the period. Diluted earnings per share reflects the potential impact of contingently issuable shares.

The following shows the weighted average number of shares used in computing earnings per share and the effect of weighted average number of shares dilutive potential common stock. Dilutive potential common stock has no effect on income available to common shareholders.

		2021		2020
Net Income ($ in thousands)	$	**36,165**	$	26,499
Weighted average number of shares		**185,610**		186,341
Options effect of dilutive shares		**140**		21
Weighted average dilutive shares		**185,750**		186,362
Basic EPS	$	**194.85**	$	142.21
Diluted EPS	$	**194.70**	$	142.19

Note 25. Subsequent Events

In accordance with FASB ASC Topic 855-10, the Bank evaluates subsequent events for recognition and disclosure that have occurred after the balance sheet date but before the financial statements are available to be issued. There are two types of subsequent events: (1) recognized, or those that provide additional evidence about conditions that existed at the date of the balance sheet, including the estimates inherent in the process of preparing financial statements, and (2) non-recognized, or those that provide evidence about conditions that did not exist at the date of the balance sheet but arose after that date. The Bank evaluated subsequent events through March 7, 2022, which is the date the financial statements were available to be issued.

Based on the evaluation, the Bank did not identify any recognized or non-recognized subsequent events that would have required adjustment to or disclosure in the financial statements.

Crowe LLP
Independent Member Crowe Global

INDEPENDENT AUDITOR'S REPORT

Shareholders and the Board of Directors
Burke & Herbert Bank & Trust Company
Alexandria, Virginia

Report on the Audit of the Financial Statements

Opinion

We have audited the financial statements of Burke & Herbert Bank & Trust Company, which comprise the balance sheets as of December 31, 2021, and the related statement of income, comprehensive income, changes in shareholders' equity, and cash flows for the year then ended, and the related notes to the financial statements.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of Burke & Herbert Bank & Trust Company as of December 31, 2021, and the results of its operations and its cash flows for the year then ended, in accordance with accounting principles generally accepted in the United States of America.

We also have audited, in accordance with auditing standards generally accepted in the United States of America, Burke & Herbert Bank & Trust Company's internal control over financial reporting as of December 31, 2021, based on criteria established in the *Internal Control—Integrated Framework* (2013), issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) relevant to reporting objectives for the express purpose of meeting the regulatory requirements of Section 112 of the Federal Deposit Insurance Corporation Improvement Act (FDICIA) and our report dated March 7, 2022 expressed an unmodified opinion.

Basis for Opinion

We conducted our audit in accordance with auditing standards generally accepted in the United States of America (GAAS). Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report. We are required to be independent of Burke & Herbert Bank & Trust Company and to meet our other ethical responsibilities, in accordance with the relevant ethical requirements relating to our audits. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Other Matter

The financial statements of Burke & Herbert Bank & Trust Company for the year ended December 31, 2020, were audited by other auditors, who expressed an unmodified opinion on those statements on March 8, 2021.

Responsibilities of Management for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with accounting principles generally accepted in the United States of America, and for the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about Burke & Herbert Bank & Trust Company's ability to continue as a going concern for one year from the date the financial statements are available to be issued.

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with GAAS will always detect a material misstatement when it exists. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Misstatements are considered material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the financial statements.

In performing an audit in accordance with GAAS, we:

- Exercise professional judgment and maintain professional skepticism throughout the audit.
- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances.
- Evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the financial statements.
- Conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about Burke & Herbert Bank & Trust Company's ability to continue as a going concern for a reasonable period of time.

We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings, and certain internal control–related matters that we identified during the audit.

CROWE LLP

Crowe LLP

Washington, D.C.
March 7, 2022