SAVI FINANCIAL CORPORATION, INC.
AND SUBSIDIARY
BURLINGTON, WASHINGTON

AUDITED FINANCIAL STATEMENTS
AND OTHER FINANCIAL INFORMATION

DECEMBER 31, 2022 AND 2021

C O N T E N T S

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Shareholders and the
Board of Directors
of Savi Financial Corporation, Inc.
Burlington, Washington

Opinion on the Financial Statements

We have audited the accompanying consolidated financial statements of Savi Financial Corporation and Subsidiary ("Corporation") which comprise the balance sheets as of December 31, 2022 and 2021, the related statements of income, comprehensive income, changes in shareholders' equity and cash flows for the years then ended, and the related notes to the consolidated financial statements.

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Savi Financial Corporation and Subsidiary as of December 31, 2022 and 2021, and the results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Adoption of New Accounting Standard

As discussed in Notes 2, 3 and 4 to the consolidated financial statements, the Corporation changed its method for accounting for credit losses during 2022 as a result of the adoption of Accounting Standards Update (ASU) No. 2016-13, *Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*.

Basis for Opinion

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

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

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

Other Matters

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements taken as a whole. The other financial information on pages 54-55 is presented for the purpose of additional analysis and is not a required part of the financial statements. Such information is the responsibility of management and was derived from, and relates directly to, the underlying accounting and other records used to prepare the financial statements. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the other financial information is fairly stated in all material aspects in relation to the financial statements taken as a whole.

We have served as the Corporation's auditor since 2007.

Stovall, Grandey & Allen, LLP

STOVALL, GRANDEY & ALLEN, LLP
Fort Worth, Texas
April 27, 2023

SAVI FINANCIAL CORPORATION, INC. AND SUBSIDIARY
CONSOLIDATED BALANCE SHEETS
DECEMBER 31, 2022 AND 2021

	2022	2021
ASSETS		
Cash and due from banks	$ 6,084,792	$ 8,045,911
Interest-bearing deposits in other financial institutions maturing in less than three months	14,099,673	49,752,842
Federal funds sold	-	7,715,384
Cash and cash equivalents	20,184,465	65,514,137
Investment securities - Note 3	38,102,579	34,266,650
Federal Home Loan Bank stock, at cost - Note 2	1,975,100	691,100
Pacific Coast Bankers' Bank stock, at cost - Note 2	190,000	190,000
Loans held-for-sale - Note 4	1,523,000	2,838,911
Loans receivable, net of allowance for credit losses and deferred loan fees and costs - Note 4	427,065,685	345,167,233
Premises and equipment, net - Note 6	15,949,476	15,786,082
Foreclosed and repossessed assets	669,022	921,748
Accrued interest receivable	1,458,376	960,304
Core deposit intangibles, net - Note 7	1,041,366	1,155,887
Bank-owned life insurance - Note 8	9,702,288	9,433,134
Deferred tax asset - Note 10	1,746,380	492,573
SBA servicing asset - Note 5	1,378,032	880,773
Other assets	2,345,783	891,243
Total Assets	$ 523,331,552	$ 479,189,775
LIABILITIES		
Deposits - Note 9	$ 430,708,526	$ 432,423,735
Federal Home Loan Bank borrowings - Note 12	35,000,000	5,000,000
Subordinated debt - Note 14	17,000,000	-
Note payable - related party - Note 15	2,500,000	2,500,000
Accrued interest payable	394,924	93,414
Accrued expenses and other liabilities	1,451,365	1,589,134
Total Liabilities	487,054,815	441,606,283
Commitments and contingencies - Notes 6, 12, 13, 16, 17 and 21		
SHAREHOLDERS' EQUITY - Note 19		
Common stock, no par value; authorized: 10,000,000 shares Issued and outstanding: 3,441,882 and 3,439,192 at December 31, 2022 and 2021, respectively.	28,271,839	28,258,618
Additional paid-in capital	668,814	577,336
Retained earnings	10,925,100	9,046,006
Accumulated other comprehensive loss, net of tax benefit of $954,042 and $79,340 at December 31, 2022 and 2021, respectively	(3,589,016)	(298,468)
Total Shareholders' Equity	36,276,737	37,583,492
Total Liabilities and Shareholders' Equity	$ 523,331,552	$ 479,189,775

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

SAVI FINANCIAL CORPORATION, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF INCOME
FOR THE YEARS ENDED DECEMBER 31, 2022 AND 2021

	2022	2021
Interest income		
Interest and fees on loans	$ 18,917,262	$ 18,051,712
Interest on investment securities	912,213	295,610
Interest on federal funds sold and interest-bearing deposits with financial institutions	386,217	90,680
Total interest income	20,215,692	18,438,002
Interest expense		
On deposits	740,859	1,204,860
On borrowed funds	903,373	349,896
Total interest expense	1,644,232	1,554,756
Net interest income	18,571,460	16,883,246
Provision for credit losses - Note 4	413,865	818,572
Net interest income after provision for credit losses	18,157,595	16,064,674
Non-interest income		
Service charges on deposit accounts	871,867	657,104
Loss on sales of investment securities (includes $690 of accumulated other comprehensive loss reclassifications for unrealized gains/losses on available-for-sale securities for 2022)	(3,442)	-
Gain on sales of loans	4,928,326	4,274,974
Loss on sales of other real estate owned	(167,118)	-
Earnings on bank-owned life insurance - Note 8	269,154	133,134
Other	756,045	481,094
Total non-interest income	6,654,832	5,546,306
Non-interest expense		
Salaries and employee benefits	13,570,687	10,875,229
Occupancy and equipment	2,368,986	2,144,287
Amortization of core deposit intangibles - Note 7	114,521	93,429
Data processing fees	707,289	695,643
Professional fees	439,538	421,760
FDIC assessment	380,235	304,500
OREO expense and writedowns	28,345	151,437
Directors and officers insurance	113,897	105,878
Director fees	237,204	197,577
Regulatory examination fees	53,048	51,707
B & O taxes	488,956	446,771
Other expense	1,716,891	1,612,955
Total non-interest expense	20,219,597	17,101,173
Income before federal income tax	4,592,830	4,509,807
Federal income tax - Note 10	870,142	926,216
Net Income	$ 3,722,688	$ 3,583,591

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

SAVI FINANCIAL CORPORATION, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
FOR THE YEARS ENDED DECEMBER 31, 2022 AND 2021

	2022	2021
Net Income	$ 3,722,688	$ 3,583,591
Other Comprehensive Loss		
Securities available-for-sale:		
Reclassification adjustment for net realized gains/losses on sales during the year	690	-
Change in net unrealized gains/losses, net of tax benefit, during the year	(3,291,238)	(330,695)
Other comprehensive loss, net of tax benefit	(3,290,548)	(330,695)
Comprehensive Income	$ 432,140	$ 3,252,896

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

SAVI FINANCIAL CORPORATION, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
FOR THE YEARS ENDED DECEMBER 31, 2022 AND 2021

	Shares of Common Stock	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
Balance at January 1, 2021	3,434,272	$ 28,233,128	$ 504,896	$ 5,462,415	$ 32,227	$ 34,232,666
Stock-based compensation, stock options			59,546			59,546
Restricted stock compensation	1,200		12,894			12,894
Exercise of stock options	3,720	25,490				25,490
Comprehensive income (loss) for the year ended December 31, 2021				3,583,591	(330,695)	3,252,896
Balance at December 31, 2021	3,439,192	28,258,618	577,336	9,046,006	(298,468)	37,583,492
Cumulative-effect adjustment for implementation of ASU No. 2016-13 - Note 2				(1,843,594)		(1,843,594)
Stock-based compensation, stock options			78,769			78,769
Restricted stock compensation	1,200		12,709			12,709
Exercise of stock options	1,490	13,221				13,221
Comprehensive income (loss) for the year ended December 31, 2022				3,722,688	(3,290,548)	432,140
Balance at December 31, 2022	3,441,882	$ 28,271,839	$ 668,814	$ 10,925,100	$ (3,589,016)	$ 36,276,737

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

SAVI FINANCIAL CORPORATION, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2022 AND 2021

	2022	2021
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 3,722,688	$ 3,583,591
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	914,917	842,033
Provision for credit losses	413,865	818,572
Net amortization on investment securities	35,991	67,756
Loss on sales of investment securities	3,442	-
Originations of mortgage loans held-for-sale	(71,751,726)	(59,441,231)
Proceeds from sales of mortgage loans held-for-sale	74,741,747	58,119,231
Gain on sales of mortgage loans held-for-sale	(1,674,110)	(1,516,911)
Gain on sales of SBA loans	(3,254,216)	(2,758,063)
Loss on sales of other real estate owned	167,118	-
Writedowns on other real estate owned	-	78,406
Stock-based compensation, stock options	78,769	59,546
Restricted stock compensation	12,709	12,894
Earnings on bank-owned life insurance	(269,154)	(133,134)
Amortization of core deposit intangibles	114,521	93,429
Deferred income tax expense	110,965	563,662
(Increase) decrease in other assets	(2,464,398)	134,554
Increase (decrease) in other liabilities	(173,580)	410,207
Total adjustments	(2,993,140)	(2,649,049)
Net Cash Provided by Operating Activities	729,548	934,542
CASH FLOWS FROM INVESTING ACTIVITIES:		
Decrease in interest-bearing deposits in other financial institutions maturing in more than three months	-	10,000,000
Purchases of investment securities:		
Available-for-sale	(26,355,171)	(26,163,663)
Held-to-maturity	(2,000,000)	(3,050,000)
Principal payments on investment securities:		
Available-for-sale	4,591,718	2,611,383
Proceeds from maturities and calls of investment securities:		
Available-for-sale	15,150,000	1,065,000
Proceeds from sales of investment securities:		
Available-for-sale	72,841	-
Purchases of FHLB stock	(1,984,400)	(116,700)
Redemptions of FHLB stock	700,400	800,400
Net (increase) decrease in loans receivable	(80,420,281)	150,314
Cash proceeds from sales of other real estate owned	100,135	138,867
Purchases of premises and equipment	(1,214,911)	(839,098)
Proceeds from sales of premises and equipment	2,437	-
Premiums paid for purchases of bank-owned life insurance	-	(9,300,000)
Proceeds received from seller on branch acquisition	-	19,874,570
Net Cash Used by Investing Activities	$ (91,357,232)	$ (4,828,927)

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

SAVI FINANCIAL CORPORATION, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS, Continued
FOR THE YEARS ENDED DECEMBER 31, 2022 AND 2021

	2022	2021
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net increase (decrease) in deposits	$ (1,715,209)	$ 59,435,334
Net advances (repayments) of FHLB borrowings	30,000,000	(20,000,000)
Proceeds from issuance of subordinated debt	17,000,000	-
Proceeds from note payable	-	2,500,000
Proceeds from exercise of stock options	13,221	25,490
Net Cash Provided by Financing Activities	45,298,012	41,960,824
Net increase (decrease) in cash and cash equivalents	(45,329,672)	38,066,439
Cash and cash equivalents at beginning of year	65,514,137	27,447,698
Cash and cash equivalents at end of year	$ 20,184,465	$ 65,514,137
SUPPLEMENTAL SCHEDULE OF OPERATING AND INVESTING ACTIVITIES:		
Cash paid for interest	$ 1,342,722	$ 1,661,597
Income taxes paid	660,248	435,015
Other real estate acquired through loan foreclosures	-	654,495

SAVI FINANCIAL CORPORATION, INC. AND SUBSIDIARY
NOTES TO FINANCIAL STATEMENTS
(CONSOLIDATED AND BANK ONLY)
DECEMBER 31, 2022 AND 2021

Note 1 Description of Business

SaviBank is a commercial bank chartered in the State of Washington. The Bank began operations April 11, 2005 and has 10 branch locations in Anacortes, Burlington, Bellingham, Concrete, Friday Harbor, Mt. Vernon, Oak Harbor, Sedro-Woolley and Freeland, Washington. During 2021, the Corporation started a mortgage department for the purpose of originating residential 1-4 family loans that are sold in the secondary market. A loan production office was opened in Friday Harbor, Washington in 2021 and was converted to a branch during 2022. A loan production office was opened in Olympia during 2022. The Bank provides loan and deposit services to customers who are predominantly small and middle-market businesses and individuals in and around Skagit, Island and Whatcom counties. The Bank operates under a state bank charter and is subject to regulation by the State of Washington Department of Financial Institutions (DFI) and the Federal Deposit Insurance Corporation (FDIC). The holding company is regulated by the Federal Reserve Board (Fed). Application has been filed with the DFI, FDIC and Fed to spin-off the Bellingham branch into a separate bank, Orca Bank, that will be owned by the holding company to service Whatcom County, Washington.

On July 6, 2017, Savi Financial Corporation, Inc. (the Corporation) was formed in the State of Washington as a financial holding company. Effective December 31, 2017, the Corporation and SaviBank entered into a Share Exchange Agreement in order to effect the transfer of 100% of the issued and outstanding common stock of the Bank. Each issued and outstanding share of common stock of the Bank was automatically converted into one share of common stock of the Corporation. As a result of the Share Exchange, the Corporation became the sole shareholder of the common stock of the Bank and the Bank will continue in existence as a wholly-owned subsidiary of the Corporation.

Effective September 10, 2018, the Corporation effected a 1-for-5 reverse stock split of issued and outstanding common shares. The reverse stock split decreased the number of issued shares from 17,113,064 to 3,422,684, including 356 additional shares issued to shareholders with fractional shares. Share and per share amounts included in the consolidated financial statements and notes reflect the effect of this split for all periods presented.

Note 2 Summary of Significant Accounting Policies

Financial Statement Presentation

The financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America and practices within the banking industry. The consolidated balance sheets of the Corporation include its accounts and those of its one hundred percent (100%) owned subsidiary, SaviBank. All significant intercompany accounts and transactions have been eliminated upon consolidation.

Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Note 2 Summary of Significant Accounting Policies, continued

Estimates, continued

The determination of the adequacy of the allowance for credit losses is based on estimates that are particularly susceptible to significant changes in the economic environment and market conditions. In connection with the determination of the estimated losses on loans, management obtains independent appraisals for significant collateral.

The Corporation's loans are generally secured by specific items of collateral including real property, consumer assets and business assets. Although the Bank has a diversified loan portfolio, a substantial portion of its debtors' ability to honor their contracts is dependent on local economic conditions.

While management uses available information to recognize losses on loans, further reductions in the carrying amounts of loans may be necessary based on changes in local economic conditions. In addition, regulatory agencies, as an integral part of their examination process, periodically review the estimated losses on loans. Such agencies may require the Corporation to recognize additional losses based on their judgments about information available to them at the time of their examination. Because of these factors, it is reasonably possible that the estimated losses on loans may change materially in the near term. However, the amount of the change that is reasonably possible cannot be estimated.

Comprehensive Income (Loss)

The Corporation has adopted authoritative guidance issued by the FASB which establishes standards for reporting and display of comprehensive income (loss) and its components. These standards require that recognized revenue, expenses, gains and losses be included in net income. Certain changes in assets and liabilities, such as unrealized gains and losses on available-for-sale investment securities, are reported as a separate component in shareholders' equity. These items, along with net income, are components of comprehensive income (loss). The Corporation reports comprehensive income (loss) in the statement of comprehensive income (loss).

Cash and Cash Equivalents

Cash and due from banks consist of vault cash, cash items in the process of collection, and non-interest-bearing deposits with financial institutions. For purposes of the statements of cash flows, the Corporation considers cash and cash equivalents to include cash, due from banks, interest-bearing deposits, investments with an original maturity of three months or less and federal funds sold.

Investment Securities

The Corporation accounts for investment securities according to authoritative guidance issued by the Financial Accounting Standards Board (FASB). Under the provisions of the FASB authoritative guidance, debt securities that management has the ability and intent to hold to maturity are classified as held-to-maturity and carried at amortized cost. Accretion of discounts are recognized in interest income using methods approximating the interest method over the period to maturity. Amortization of premiums are recognized in interest income using methods approximating the interest method over the earlier of the period to maturity or the first callable date.

Note 2 Summary of Significant Accounting Policies, continued

Investment Securities, continued

Debt securities not classified as held-to-maturity are classified as available-for-sale. Securities available-for-sale are carried at fair value with unrealized gains and losses reported in other comprehensive income (loss). Realized gains (losses) on securities available-for-sale are included in other income, and when applicable, are reported as a reclassification adjustment, in other comprehensive income (loss). Gains and losses on sales of securities are determined on the specific-identification method.

After adoption of Accounting Standards Update (ASU) No. 2016-13 during 2022, an allowance for credit losses was established for declines in the fair value of individual held-to-maturity and available-for-sale securities below their amortized cost that are other-than-temporary. Prior to adoption of ASU No. 2016-13, declines in the fair value of individual held-to-maturity and available-for-sale securities below their amortized cost that are other-than-temporary resulted in writedowns of the individual securities to their fair value. The related writedowns are included in earnings as realized losses. In estimating other-than-temporary impairment losses, management considered (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer and (3) the intent and ability of the Corporation to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value.

Federal Home Loan Bank and Pacific Coast Bankers' Bank Stock

At December 31, 2022 and 2021, the Corporation held stock in the Federal Home Loan Bank (FHLB) totaling $1,975,100 and $691,100, respectively. As a member of the FHLB system, the Corporation is required to maintain a minimum level of investment in FHLB stock based on specific percentages of its outstanding FHLB advances. The Corporation is required to purchase or redeem shares as the level of outstanding advances increase or decrease. This stock is classified as a restricted investment security, carried at cost and evaluated annually for impairment. No impairment loss was recorded in 2022 or 2021.

The Corporation owns stock in Pacific Coast Bankers' Bank (PCBB). The carrying amount of the PCBB stock was $190,000 at December 31, 2022 and 2021. The investment in PCBB stock is a restricted investment carried at cost, which reasonably approximates its fair value. As a holder of PCBB stock, the Corporation is allowed to borrow at a lower interest rate than a non-holder and to receive dividends.

Loans Held-for-Sale

Mortgage loans originated for sale in the foreseeable future in the secondary market are carried at the lower of aggregate cost or fair value. Gains and losses on sales of loans are recognized at the settlement date and are determined by the difference between the sales proceeds and the carrying value of the loans. Sales are made without recourse. Net unrealized losses, if any, are recognized through a valuation allowance established by charges to income.

Note 2 Summary of Significant Accounting Policies, continued

Loans Held-for-Sale, continued

The Corporation issues various representations and warranties associated with the sale of loans. During 2022 and 2021, there were no losses incurred regarding these representations and warranties.

Loans

Loans that management has the intent and ability to hold for the foreseeable future are stated at the principal amount outstanding, net of allowance for credit losses and deferred loan fees and costs. Loan fees and certain direct loan origination costs are deferred, and the net fee or cost is recognized as an adjustment to interest income using the interest method. Interest on loans is calculated using the simple interest method based on the daily balance of principal amount outstanding and is credited to income when earned. Interest is accrued as earned unless management doubts the collectability of interest or principal, at which time the loan is placed on nonaccrual status and accrued but unpaid interest is charged against income in that period. Any loan delinquent 90 days or more is placed on nonaccrual. Accrual of interest income is resumed when the borrower demonstrates the ability to make scheduled payments of both principal and interest. Past due status is determined based on contractual terms.

Management considers a loan impaired when it is probable that the Corporation will not be able to collect all amounts as scheduled under a loan agreement. Impaired loans are measured based on the present value of expected future cash flows, discounted at the loan's effective interest rate, or, as a practical expedient, at the loan's observable market price or the fair value of the collateral if the loan is collateral dependent. Changes in these values will be reflected in income and as adjustments to the allowance for possible credit losses.

The accrual of interest on impaired loans is discontinued when, in management's opinion, the borrower may be unable to meet payments as they become due, unless the loan is well secured and in the process of collection. When interest accrual is discontinued, all unpaid accrued interest is reversed. Interest income is subsequently recognized only to the extent cash payments are received, or payment is considered certain.

Allowance for Credit Losses

As further discussed below, the Corporation adopted ASU No. 2016-13, *Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*, during 2022. Accounting Standards Codification (ASC) Topic 326 replaced the previous "incurred" loss model for measuring credit losses, which encompassed allowances for current known and inherent losses within the portfolio, with an "expected loss" model, which encompasses allowances for losses expected to be incurred over the life of the portfolio. The new current expected credit loss (CECL) model requires the measurement of all expected credit losses for financial assets measured at amortized cost and certain off-balance-sheet exposures based on historical experience, current conditions, and reasonable and supportable forecasts. In connection with the adoption of ASC 326, management revised certain accounting policies and implemented certain accounting policy elections. Management made the election to utilize the Weighted Average Remaining Maturing (WARM) model. This model includes the required components of CECL, including the use of a historical loss rate, current economic condition factors, weighted average remaining maturity of the portfolio and forecasted future economic factors. The revised accounting policies are described on the next page.

Note 2 Summary of Significant Accounting Policies, continued

Allowance for Credit Losses, continued

Allowance for Credit Losses – Held-to-Maturity (HTM) Securities: The allowance for credit losses on HTM securities is a contra-asset valuation account, calculated in accordance with ASC 326 that is deducted from the amortized cost basis of HTM securities to present management's best estimate of the net amount expected to be collected. HTM securities are charged-off against the allowance when deemed to be uncollectible by management. Adjustments to the allowance are reported in the income statement as a component of the provision for credit losses. Management measures expected credit losses on HTM securities on a collective basis by major security type with each type sharing similar risk characteristics and considers historical credit loss information that is adjusted for current conditions and reasonable and supportable forecasts. Management has made the accounting policy election to exclude accrued interest receivable on HTM securities from the estimate of credit losses. Further information regarding the policies and methodology used to estimate the allowance for credit losses on HTM securities is presented in Note 3 – Investment Securities.

Allowance for Credit Losses – Available-for-Sale (AFS) Securities: For AFS securities in an unrealized loss position, management first assesses whether (i) there is an intent to sell or (ii) it is more likely than not that the Corporation will be required to sell the security before recovery of its amortized cost basis. If either case is affirmative, any previously recognized allowances are charged-off and the security's amortized cost is written down to fair value through income. If neither case is affirmative, the security is evaluated to determine whether the decline in fair value has resulted from credit losses or other factors. In making this assessment, management considers the extent to which the fair value is less than amortized cost, any changes to the rating of the security by a rating agency and any adverse conditions specifically related to the security, among other factors. If this assessment indicates that a credit loss exists, the present value of cash flows expected to be collected from the security is compared to the amortized cost basis of the security. If the present value of cash flows expected to be collected is less than the amortized cost basis, a credit loss exists and an allowance for credit losses is recorded for the credit loss, limited by the amount that the fair value is less than the amortized cost basis. Any impairment that has not been recorded through an allowance for credit losses is recognized in other comprehensive income (loss). Adjustments to the allowance are reported in the income statement as a component of the provision for credit losses. Management has made the accounting policy election to exclude accrued interest receivable on AFS securities from estimates of credit losses. AFS securities are charged against the allowance, or in the absence of any allowance, written down through income when deemed uncollectible by management or when either of the aforementioned criteria regarding intent or requirement to sell is met.

Prior to adoption of ASU No. 2016-13, declines in the fair value of HTM and AFS securities below their cost that were deemed to be other-than-temporary were reflected in earnings as realized losses. In estimating other-than-temporary impairment prior to 2022, management considered, among other things, (i) the length of time and the extent to which the fair value had been less than cost, (ii) the financial condition and near-term prospects of the issuer and (iii) the intent and ability to retain the investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value.

Allowance for Credit Losses – Loans: The allowance for credit losses on loans is a contra-asset valuation account, calculated in accordance with ASC 326 that is deducted from the amortized cost basis of loans to present management's best estimate of the net amount expected to be collected. The allowance is comprised of amounts charged against income in the form of the provision for credit losses, less charged-off loans, net of recoveries. Loans are charged-off against the allowance when management believes that collection of principal is unlikely. Subsequent recoveries, if any, are credited to the allowance for credit

Note 2 Summary of Significant Accounting Policies, continued

Allowance for Credit Losses, continued

losses. Management has made the accounting policy election to exclude accrued interest receivable on loans from the estimate of credit losses. Further information regarding the policies and methodology used to estimate the allowance for credit losses is presented in Note 4 – Loans.

The allowance for credit losses is maintained at a level sufficient to provide for probable credit losses on loans based on evaluating known and inherent risks in the loan portfolio. The allowance is provided based upon management's continuing analysis of the pertinent factors underlying the quality of the loan portfolio. These factors include changes in the size and composition of the loan portfolio, delinquency levels, actual loan loss experience, current economic conditions, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral and a detailed analysis of individual loans for which full collectability may not be assured. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available.

The allowance consists of specific, general and unallocated components. A specific reserve is established when, in accordance with authoritative guidance issued by the FASB, it is probable that a creditor will be unable to collect all amounts (principal and interest) due according to the contractual terms of the loan agreement. Smaller balance homogenous loans, such as residential mortgage loans and consumer loans, are collectively evaluated for potential loss. When a loan has been identified as being impaired, the amount of impairment is measured by using the discounted cash flows, except when, as a practical expedient, the current fair value of the collateral, reduced by costs to sell, is used. When the measurement of the impaired loan is less than the recorded investment in the loan, impairment is recognized by creating or adjusting an allocation of the allowance for credit losses. The general component relates to allocations for loans that are classified as doubtful, substandard or special mention, as well as a component to cover non-classified loans, and is based on historical loss experience adjusted for qualitative factors. An unallocated component is maintained to cover uncertainties that could affect management's estimate of probable losses. The unallocated component of the allowance reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating specific and general losses in the portfolio.

When available information confirms that specific loans or portions thereof are uncollectible, identified amounts are charged against the allowance for credit losses. The existence of some or all of the following criteria will generally confirm that a loss has been incurred: the loan is significantly delinquent and the borrower has not demonstrated the ability or intent to bring the loan current; the Corporation has no recourse to the borrower, or if it does, the borrower has insufficient assets to pay the debt; the estimated fair value of the loan collateral is significantly below the current loan balance, and there is little or no near-term prospect for improvement.

A provision for credit losses is charged against income and is added to the allowance for credit losses based on regular assessments of the loan portfolio. The allowance for credit losses is allocated to certain loan categories based on the relative risk characteristics, asset classifications and actual loss experience of the loan portfolio. While management has allocated the allowance for credit losses to various loan portfolio segments, the allowance is general in nature and is available for the loan portfolio in its entirety.

The ultimate recovery of all loans is susceptible to future market factors beyond the Corporation's control. These factors may result in losses or recoveries differing significantly from those provided in the consolidated financial statements. In addition, regulatory agencies periodically review the Corporation's

Note 2 Summary of Significant Accounting Policies, continued

Allowance for Credit Losses, continued

allowance for credit losses as an integral part of their examination process and may require the Corporation to make additions to the allowance based on their judgment about information available to them at the time of their examination.

Prior to adoption of ASU No. 2016-13, the allowance for credit losses on loans was a contra-asset valuation account established through a provision for loan losses charged to expense, which represented management's best estimate of inherent losses that had been incurred within the existing portfolio of loans. The allowance for credit losses on loans included allowance allocations calculated in accordance with ASC Topic 310, *Receivables*, and allowance allocations calculated in accordance with ASC Topic 450, *Contingencies*.

Allowance for Credit Losses – Off-Balance-Sheet Credit Exposures: The allowance for credit losses on off-balance-sheet credit exposures is a liability account, calculated in accordance with ASC 326, representing expected credit losses over the contractual period for which the Corporation is exposed to credit risk resulting from a contractual obligation to extend credit. No allowance is recognized if the Corporation has the unconditional right to cancel the obligation. The allowance is reported as a component of accrued expenses and other liabilities in the amount of $544,087 and $166,001 at December 31, 2022 and 2021, respectively. Adjustments to the allowance are reported in the income statement as a component of the provision for credit losses since adoption of ASU No. 2016-13. Prior to adoption of ASU No. 2016-13, adjustments to the allowance are reported in other non-interest expense.

Transfers of Financial Assets

Transfers of financial assets are accounted for as sales when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when: (1) the assets have been isolated from the Corporation, (2) 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 (3) the Corporation does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

Premises and Equipment

Property, equipment and leasehold improvements are recorded at cost, net of accumulated depreciation and amortization. Gains and losses on dispositions are reflected in operations. Expenditures for improvements and major renewals are capitalized, and ordinary maintenance, repairs and small purchases are charged to operations as incurred.

Depreciation and Amortization

Property, equipment and leasehold improvements are depreciated or amortized over the estimated useful life of the related asset, which ranges from three to 50 years. The Corporation uses the straight-line method of recognizing depreciation and amortization expenses. Leasehold improvements are amortized over lease terms or the estimated useful life, whichever is less, on a straight-line basis.

Note 2 Summary of Significant Accounting Policies, continued

Other Real Estate Owned

Other real estate owned is foreclosed property held pending disposition and is initially recorded at fair value less estimated selling costs when acquired, establishing a new cost basis. At foreclosure, if the fair value of the real estate acquired less estimated selling costs is less than the Corporation's recorded investment in the related loan, a writedown is recognized through a charge to the allowance for credit losses. Costs of significant property improvements are capitalized, whereas costs relating to holding property are expensed. Valuations are periodically performed by management, and any subsequent writedowns are recorded as a charge to income, if necessary, to reduce the carrying value of the property to its fair value less estimated selling costs. Sales of other real estate owned are accounted for according to authoritative guidance issued by the FASB.

Intangibles and Other Long-Lived Assets

Intangible assets are acquired assets that lack physical substance but can be distinguished from goodwill because of contractual or other legal rights or because the asset is capable of being sold or exchanged either on its own or in combination with a related contract, asset or liability. The Corporation's intangible assets relate to core deposits. Intangible assets with definite useful lives are amortized on an accelerated basis over their estimated life. Intangible assets with indefinite useful lives are not amortized until their lives are determined to be definite. Intangible assets, premises and equipment and other long-lived assets are tested for impairment whenever events or changes in circumstances indicate the carrying amount of the assets may not be recoverable from future undiscounted cash flows. If impaired, the assets are recorded at fair value. See Note 7 – Other Intangible Assets for additional information.

Income Taxes

Income taxes are provided for the tax effects of the transactions reported in the financial statements and consist of taxes currently due plus deferred taxes related primarily to differences between the tax and financial reporting of the allowance for credit losses, accumulated depreciation, organization costs and conversion from accrual to cash basis.

The deferred tax assets and liabilities represent the future tax return consequences of those differences, which will either be taxable or deductible when the assets and liabilities are recovered or settled. Deferred tax assets and liabilities are reflected at income tax rates applicable to the period in which the deferred tax assets or liabilities are expected to be realized or settled. As changes in tax laws or rates are enacted, deferred tax assets and liabilities are adjusted through the provision for income taxes.

The Corporation and the Bank file consolidated federal income tax returns. The Corporation and the Bank maintain their records for financial reporting on the accrual basis of accounting and for income tax reporting on the cash basis of accounting.

Note 2 Summary of Significant Accounting Policies, continued

Income Taxes, continued

In accordance with authoritative guidance issued by the FASB, the Corporation performed an evaluation to determine if there were any uncertain tax positions that would have an impact on the financial statements. No uncertain tax positions were identified. The December 31, 2019 through December 31, 2022 tax years remain subject to examination by the Internal Revenue Service. The Corporation does not believe that any reasonably possible changes will occur within the next 12 months which will have a material impact on the financial statements. The Corporation records incurred penalties and interest in other non-interest expense. There were no penalties and interest assessed by taxing authorities during 2022 or 2021.

Advertising Costs

The Corporation expenses advertising costs as they are incurred. Total advertising expense was $142,163 and $96,831 for the years ended December 31, 2022 and 2021, respectively.

Stock-Based Employee Compensation

The Corporation has a stock-based compensation plan described more fully in Note 19. The Corporation has adopted authoritative guidance issued by the FASB regarding stock compensation.

The consolidated statements of income include $78,769 and $59,546 of compensation expense related to stock-based compensation for stock options for the years ended December 31, 2022 and 2021, respectively. The consolidated statements of income include $12,709 and $12,894 of compensation expense related to stock-based compensation for restricted stock for the years ended December 31, 2022 and 2021, respectively.

Financial Instruments

In the ordinary course of business, the Corporation has entered into off-balance-sheet financial instruments consisting of commitments to extend credit and commercial letters of credit. Such financial instruments are recorded in the financial statements when they are funded, or related fees are incurred or received.

Fair Values of Financial Instruments

The FASB has issued authoritative guidance which requires disclosure of fair value information about financial instruments, whether or not recognized in the balance sheet. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. In that regard, the derived fair value estimates cannot be substantiated by comparison to independent markets and, in many cases, could not be realized in immediate settlement of the instruments. The FASB authoritative guidance excludes certain financial instruments and all nonfinancial instruments from its disclosure requirements. Accordingly, the aggregate fair value amounts presented do not represent the underlying value of the Corporation.

Note 2 Summary of Significant Accounting Policies, continued

Fair Values of Financial Instruments, continued

The following methods and assumptions were used by the Corporation in estimating its fair value disclosures for financial instruments:

Cash and cash equivalents: The carrying amounts reported in the balance sheet for cash and cash equivalents approximate those assets' fair values.

Investment securities: Fair values for investment securities are based on quoted market prices, where available. If quoted market prices are not available, fair values are based on quoted market prices of comparable instruments.

FHLB stock and PCBB stock: These are restricted investments carried at cost which approximates their fair value.

Loans held-for-sale: The carrying amount reported in the balance sheet for loans held-for-sale approximates their fair values.

Loans: In accordance with ASU No. 2016-01, exit level pricing was utilized to determine the fair values for loans.

Bank-owned life insurance: The carrying amount of the bank-owned life insurance approximates its fair value.

SBA Servicing Asset: The carrying amount of the servicing asset approximates its fair value.

Deposits: In accordance with ASU No. 2016-01, exit level pricing was utilized to determine the fair values for deposits.

Long-Term Borrowings: The fair values of the Corporation's long-term borrowings are estimated using discounted cash flow analyses based on the Corporation's current incremental borrowing rates for similar types of borrowing arrangements.

Short-Term Borrowings: The carrying amount of short-term borrowings approximates their fair values.

Accrued Interest: The carrying amount of accrued interest approximates its fair value.

Reclassifications

Certain reclassifications have been made to the 2021 financial statements to conform to current year presentations. Such reclassifications have had no effect upon previously reported net income.

Note 2 Summary of Significant Accounting Policies, continued

Subsequent Events

Subsequent events are events or transactions that occur after the balance sheet date but before the financial statements are available to be issued. The Corporation recognizes in the financial statements the effects of all subsequent events that provide additional evidence about conditions that existed at the date of the balance sheet, including the estimates inherent in the process of preparing the financial statements. The Corporation's financial statements do not recognize subsequent events that provide evidence about conditions that did not exist at the date of the balance sheet but arose after the balance sheet date and before the financial statements are available to be issued. The Corporation has evaluated subsequent events from December 31, 2022 through April 27, 2023, the date the financial statements were available to be issued. Refer to Note 25 for information regarding subsequent events identified by the Corporation.

Accounting Standards Adopted in 2022 and 2021

In June 2016, the FASB issued ASU No. 2016-13, *Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments* which is intended to improve financial reporting by requiring timelier recording of credit losses on loans and other financial instruments held by financial institutions and other organizations. The standard requires an organization to measure 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 determine their credit loss estimates. The standard also requires enhanced disclosures to help investors and other financial statement users better understand significant estimates and judgments used in estimating credit losses, as well as the credit quality and underwriting standards of an organization's portfolio.

These disclosures include qualitative and quantitative requirements that provide additional information about the amounts recorded in the financial statements. Additionally, the standard amends the accounting for credit losses on available-for-sale debt securities and purchased financial assets with credit deterioration. For non-SEC filing entities, the amendments in this update are effective for fiscal years beginning after December 15, 2022, including interim periods within those fiscal years. An entity will apply the amendments in this update through a cumulative effect adjustment to retained earnings as of the beginning of the first reporting period in which the guidance is effective (that is, a modified-retrospective approach). The Corporation early adopted this ASU during 2022. A cumulative effect adjustment totaling $1,843,594 was recorded through retained earnings as a result of adoption of this ASU.

In July 2021, the FASB issued ASU No. 2021-05, *Leases (Topic 842)*, which affects lessors with lease contracts that (1) have variable lease payments that do not depend on a reference index or a rate and (2) would have resulted in the recognition of a selling loss at lease commencement if classified as sales-type or direct financing. The amendments in this update address concerns by amending the lease classification requirements for lessors to align them with practice under Topic 840. Lessors should classify and account for a lease with variable lease payments that do not depend on a reference index or a rate as an operating lease if both of the following criteria are met: (1) The lease would have been classified as a sales-type lease or a direct financing lease in accordance with the classification criteria in paragraphs 842-10-25-2 through 25-3 and (2) The lessor would have otherwise recognized a day-one loss. The amendments in this update are effective for fiscal years beginning after December 15, 2021 for all entities and interim periods within those fiscal years for public business entities and interim periods with fiscal years beginning after December 15, 2022 for all other entities. Early application is permitted. Implementation of this standard, which was effective as of January 1, 2022, did not have a significant

Note 2 Summary of Significant Accounting Policies, continued

Accounting Standards Adopted in 2022 and 2021, continued

impact on the Corporation's consolidated financial statements.

In October 2021, the FASB issued ASU No. 2021-07, *Compensation – Stock Compensation (Topic 718)*, which as a practical expedient allows nonpublic entities to determine the current price input of equity-based awards issued to both employees and nonemployees using a reasonable application of a reasonable valuation method. A reasonable application of a reasonable valuation method includes (1) the date on which a valuation's reasonableness is evaluated, (2) the factors that a reasonable valuation should consider, (3) the scope of information that a reasonable valuation should consider and (4) the criteria that should be met for the use of a previously calculated value to be considered reasonable. The amendments in this update are effective prospectively for all qualifying awards granted or modified during the fiscal years beginning after December 15, 2021 and interim periods within fiscal years beginning after December 15, 2022. Early application is permitted. Implementation of this standard, which was effective as of January 1, 2022, did not have a significant impact on the Corporation's consolidated financial statements.

In November 2021, the FASB issued ASU No. 2021-09, *Leases (Topic 842)*, which as a practical expedient allows nonpublic entities to elect, as an accounting policy, to use a risk-free rate as the discount rate for all leases. The amendments in this update allow those lessees to make the risk-free rate election by class of underlying asset, rather than at the entity-wide level. An entity that makes the risk-free rate election is required to disclose which asset classes it has elected to apply a risk-free rate. The amendments require that when the rate implicit in the lease is readily determinable for any individual lease, the lessee use that rate (rather than a risk-free rate or an incremental borrowing rate), regardless of whether it has made the risk-free rate election. For entities which have already adopted Topic 842, the amendments of this update were effective for fiscal years beginning after December 15, 2021, and interim periods within fiscal years beginning after December 15, 2022. Other entities are required to adopt the amendments of this update at the same time that they adopt Topic 842. Implementation of this standard, which was effective as of January 1, 2022, did not have a significant impact on the Corporation's consolidated financial statements.

Accounting Standards Pending Adoption

In March 2022, the FASB issued ASU No. 2022-02, *Financial Instruments – Credit Losses (Topic 326)*, which relates to Troubled Debt Restructurings (TDRs) for all entities after they have adopted ASU No. 2016-13, *Financial Instruments – Credit Losses (Topic 326): Measure of Credit Losses on Financial Instruments*. The amendments of this update eliminate the accounting guidance for TDRs by creditors in Subtopic 310-40, *Receivables – Troubled Debt Restructurings by Creditors*, while enhancing disclosure requirements for certain loan refinancings and restructurings by creditors when a borrower is experiencing financial difficulty. Specifically, rather than applying the recognition and measurement guidance in paragraphs 310-20-35-9 through 35-11 to determine whether a modification results in a new loan or a continuation of an existing loan. For public entities, the amendments of this update require that an entity disclose current-period gross writeoffs by year of origination for financing receivables and net investments in leases within the scope of Subtopic 326-20, *Financial Instruments – Credit Losses – Measured at Amortized Cost*. For entities that have adopted the amendments in ASU No. 2016-13, the amendments in this update are effective for fiscal years after December 15, 2022, including interim periods within those fiscal years. For entities that have not yet adopted the amendments in ASU No.

Note 2 Summary of Significant Accounting Policies, continued

Accounting Standards Pending Adoption, continued

2016-13, the effective date for the amendments in this update are the same as the effective dates in ASU No. 2016-13. An entity has the option to apply a modified retrospective transition method relating to the recognition and measurement of TDRs which will result in a cumulative-effect adjustment to retained earnings in the period of adoption. All other provisions of this update are applied prospectively. Implementation of this standard is not expected to have a significant impact on the Corporation's consolidated financial statements.

Note 3 Investment Securities

The amortized cost and fair values of investment securities at December 31, 2022 are as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available-for-Sale:				
U.S. Treasury bills	$ 2,004,028	$ -	$ (67,309)	$ 1,936,719
U. S. Government agency	502,104	-	(18,967)	483,137
Municipal bonds	3,261,584	-	(465,294)	2,796,290
U.S. Government agency mortgage-backed securities	16,014,017	-	(2,753,120)	13,260,897
Collateralized mortgage obligations (CMOs)	7,182,562	-	(965,437)	6,217,125
SBA pools	5,744,862	25,013	(34,164)	5,735,711
Corporate bonds	3,386,479	-	(263,779)	3,122,700
Total available-for-sale	38,095,636	25,013	(4,568,070)	33,552,579
Held-to-Maturity:				
Corporate bonds	5,050,000	-	(396,853)	4,653,147
Total held-to-maturity	5,050,000	-	(396,853)	4,653,147
Total investment securities	$ 43,145,636	$ 25,013	$ (4,964,923)	$ 38,205,726

The balance sheet as of December 31, 2022 reflects the fair value of available-for-sale securities of $33,552,579 and the amortized cost of held-to-maturity securities in the amount of $5,050,000, less the allowance for credit losses on held-to-maturity securities in the amount of $500,000, for a total of $38,102,579. A net unrealized loss of $4,543,057 is included in the available-for-sale investment securities balance. The unrealized loss, net of tax benefit, is included in shareholders' equity.

Note 3 Investment Securities, continued

The amortized cost and fair values of investment securities at December 31, 2021 are as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available-for-Sale:				
U.S. Government agency	$ 503,541	$ 13,791	$ -	$ 517,332
Municipal bonds	1,328,087	11,876	-	1,339,963
U.S. Government agency mortgage-backed securities	14,851,510	252	(305,412)	14,546,350
Collateralized mortgage obligations (CMOs)	6,601,495	145	(111,170)	6,490,470
SBA pools	4,860,650	68,873	(4,269)	4,925,254
Corporate bonds	3,449,175	4,275	(56,169)	3,397,281
Total available-for-sale	31,594,458	99,212	(477,020)	31,216,650
Held-to-Maturity:				
Corporate bonds	3,050,000	116	(19,830)	3,030,286
Total held-to-maturity	3,050,000	116	(19,830)	3,030,286
Total investment securities	$ 34,644,458	$ 99,328	$ (496,850)	$ 34,246,936

The balance sheet as of December 31, 2021 reflects the fair value of available-for-sale securities of $31,216,650 and the amortized cost of held-to-maturity securities in the amount of $3,050,000 for a total of $34,266,650. A net unrealized loss of $377,808 is included in the available-for-sale investment securities balance. The unrealized loss, net of tax benefit, is included in shareholders' equity.

The allowance for credit losses on held-to-maturity securities is a contra-asset valuation account that is deducted from the amortized cost basis of held-to-maturity securities to present the net amount expected to be collected. Management measures credit losses on held-to-maturity securities on a collective basis by major security type with each type sharing similar risk characteristics, and considers historical credit loss information that is adjusted for current conditions and reasonable and supportable forecasts. As noted on Page 21, an allowance for credit losses on held-to-maturity securities in the amount of $500,000 was recorded at December 31, 2022.

Note 3 Investment Securities, continued

The amortized cost and estimated fair value of debt securities at December 31, 2022, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties. Mortgage-backed securities, collateralized mortgage obligations and SBA pools are shown separately, since they are not due at a single maturity date.

	Available-for-Sale		Held-to-Maturity	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Amounts maturing in:				
One year or less	$ 250,410	$ 247,120	$ -	$ -
After one year through five years	6,703,580	6,290,106	-	-
After five years through ten years	1,024,942	924,470	5,050,000	4,653,147
After ten years	1,175,263	877,150	-	-
	9,154,195	8,338,846	5,050,000	4,653,147
U.S. Government agency mortgage-backed securities	16,014,017	13,260,897	-	-
Collateralized mortgage obligations	7,182,562	6,217,125	-	-
SBA pools	5,744,862	5,735,711	-	-
Totals	$ 38,095,636	$ 33,552,579	$ 5,050,000	$ 4,653,147

During 2022, sales proceeds totaling $72,841 were received for sales of available-for-sale investment securities. These sales resulted in gross unrealized losses totaling $3,442. There were no sales of investment securities during 2021. There were proceeds received from redemptions of FHLB stock totaling $700,400 and $800,400 in 2022 and 2021, respectively. The FHLB stock was redeemed at par value, so there were no realized gains or losses on these redemptions.

Securities with carrying amounts of $236,017 and $273,210 at December 31, 2022 and 2021, respectively, were pledged to secure public deposits and for other purposes as required or permitted by law.

Note 3 Investment Securities, continued

Information pertaining to securities with gross unrealized losses at December 31, 2022 and 2021, aggregated by investment category and length of time that individual securities have been in a continuous loss position, follows:

	Less Than 12 Months		12 Months or Greater		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
December 31, 2022:						
U.S. Treasury bills	$ 1,936,719	$ (67,309)	$ -	$ -	$ 1,936,719	$ (67,309)
U.S. Government agency	483,137	(18,967)	-	-	483,137	(18,967)
Municipal bonds	1,919,140	(167,181)	877,150	(298,113)	2,796,290	(465,294)
U.S. Government agency mortgage-backed securities	2,376,925	(172,490)	10,883,972	(2,580,630)	13,260,897	(2,753,120)
Collateralized mortgage obligations	2,149,464	(159,285)	4,067,661	(806,152)	6,217,125	(965,437)
SBA pools	1,801,458	(28,634)	203,659	(5,530)	2,005,117	(34,164)
Corporate bonds	1,115,813	(134,052)	4,510,034	(526,580)	5,625,847	(660,632)
Totals	$ 11,782,656	$ (747,918)	$ 20,542,476	$ (4,217,005)	$ 32,325,132	$ (4,964,923)
December 31, 2021:						
U.S. Government agency mortgage-backed securities	$ 14,493,305	$ (304,704)	$ 31,667	$ (708)	$ 14,524,972	$ (305,412)
Collateralized mortgage obligations	5,245,547	(110,456)	908,990	(714)	6,154,537	(111,170)
SBA pools	70,011	(3)	279,545	(4,266)	349,556	(4,269)
Corporate bonds	4,623,353	(75,999)	-	-	4,623,353	(75,999)
Totals	$ 24,432,216	$ (491,162)	$ 1,220,202	$ (5,688)	$ 25,652,418	$ (496,850)

Management evaluates securities for other-than-temporary impairment at least on a quarterly basis, and more frequently when economic or market concerns warrant such evaluation. Consideration is given to (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer and (3) the intent and ability of the Corporation to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value.

Note 3 Investment Securities, continued

At December 31, 2022, there are 57 investment securities with an unrealized loss of 13.31% from their amortized cost. The Corporation has evaluated these securities and has determined that these unrealized losses relate principally to the change in market interest rates since purchase. The decline in value is not related to any company or industry specific event. At December 31, 2022, the balance of held-to-maturity securities are reported on the balance sheet net of an allowance for credit losses totaling $500,000. At December 31, 2022, there was no allowance for credit losses on available-for-sale securities recorded. At December 31, 2021, management had the ability to hold debt securities until maturity, or for the foreseeable future if classified as available-for-sale, so no declines were deemed to be other-than-temporary.

Note 4 Loans Receivable and Allowance for Credit Losses

An analysis of loan categories at December 31, 2022 and 2021 is as follows:

	2022	2021
Commercial and agricultural loans	$ 66,167,051	$ 60,847,896
Real estate (RE) loans:		
Construction, land and land development	37,294,991	22,930,959
Residential 1-4 family	66,382,632	49,876,507
Commercial RE	193,865,988	174,118,671
Consumer and other loans	69,906,125	44,247,080
	433,616,787	352,021,113
Adjust: Net deferred loan costs	801,153	222,035
Allowance for credit losses	(5,829,255)	(4,237,004)
Loans, net	$ 428,588,685	$ 348,006,144

At December 31, 2022 and 2021, Residential 1-4 family loans shown above include mortgage loans held-for-sale totaling $1,523,000 and $2,838,911, respectively.

Included in total loans above are $31,536 and $21,504 in overdrawn accounts at December 31, 2022 and 2021, respectively.

On March 27, 2020, the Coronavirus Aid, Relief and Economic Security Act (CARES Act) was signed into law which introduced the Paycheck Protection Program (PPP). The goal of this program was to prevent job loss and failure of small businesses as a result of the COVID-19 pandemic. If the borrower met certain criteria, PPP loans were eligible for forgiveness under the Small Business Association's (SBA) forgiveness program. At December 31, 2022, there was one outstanding PPP loan with a balance of $141,667 included in Commercial and Agricultural loans shown above. At December 31, 2021, there were 15 outstanding PPP loans with balances totaling $5,228,300 included in Commercial and Agricultural loans shown above. These loans are 100% guaranteed by the SBA.

At December 31, 2022, there was one Residential 1-4 Family loan in process of foreclosure totaling $17,960. At December 31, 2021, there were no Residential 1-4 Family loans in process of foreclosure.

Note 4 Loans Receivable and Allowance for Credit Losses, continued

Transactions in the allowance for credit losses in 2022 are summarized as follows:

	Commercial and Agricultural	Construction, Land and Land Development	Residential 1-4 Family	Commercial Real Estate	Consumer and Other	Unallocated	2022 Total
Allowance for Credit Losses:							
Balance, beginning of year	$ 619,819	$ 239,068	$ 518,108	$ 1,814,304	$ 461,755	$ 583,950	$ 4,237,004
Provisions and cumulative effect adjustment, charged (credited) to income and/or retained earnings	253,757	575,578	477,148	56,055	841,966	(428,459)	1,776,045
	873,576	814,646	995,256	1,870,359	1,303,721	155,491	6,013,049
Loans charged-off	(165,626)	-	(891)	-	(97,227)	-	(263,744)
Recoveries of loans previously charged-off	60,234	-	891	-	18,825	-	79,950
Net charge-offs	(105,392)	-	-	-	(78,402)	-	(183,794)
Balance, end of year	$ 768,184	$ 814,646	$ 995,256	$ 1,870,359	$ 1,225,319	$ 155,491	$ 5,829,255
Amounts allocated to: Individually evaluated for impairment	$ 108,504	$ -	$ 2,676	$ 6,507	$ 33,153	$ -	$ 150,840
Amounts allocated to: Collectively evaluated for impairment	659,680	814,646	992,580	1,863,852	1,192,166	155,491	5,678,415
Balance, end of year	$ 768,184	$ 814,646	$ 995,256	$ 1,870,359	$ 1,225,319	$ 155,491	$ 5,829,255
Loans:							
Individually evaluated for impairment	$ 1,589,769	$ 176,421	$ 185,668	$ 1,280,985	$ 325,298		$ 3,558,141
Collectively evaluated for impairment	64,577,282	37,118,570	66,196,964	192,585,003	69,580,827		430,058,646
Ending balance total loans	$ 66,167,051	$ 37,294,991	$ 66,382,632	193,865,988	$ 69,906,125		$ 433,616,787

Note 4 Loans Receivable and Allowance for Credit Losses, continued

Transactions in the allowance for loan losses in 2021 are summarized as follows:

	Commercial and Agricultural	Construction, Land and Land Development	Residential 1-4 Family	Commercial Real Estate	Consumer and Other	Unallocated	2021 Total
Allowance for Loan Losses:							
Balance, beginning of year	$ 1,178,307	$ 270,755	$ 403,313	$ 1,501,421	$ 346,412	$ 787	$ 3,700,995
Provisions, charged (credited) to income	(287,419)	(31,687)	114,795	312,883	126,837	583,163	818,572
	890,888	239,068	518,108	1,814,304	473,249	583,950	4,519,567
Loans charged-off	(331,111)	(424)	-	-	(51,470)	-	(383,005)
Recoveries of loans previously charged-off	60,042	424	-	-	39,976	-	100,442
Net charge-offs	(271,069)	-	-	-	(11,494)	-	(282,563)
Balance, end of year	$ 619,819	$ 239,068	$ 518,108	$ 1,814,304	$ 461,755	$ 583,950	$ 4,237,004
Amounts allocated to: Individually evaluated for impairment	$ 148	$ -	$ -	$ 1,322	$ 468	$ -	$ 1,938
Amounts allocated to: Collectively evaluated for impairment	619,671	239,068	518,108	1,812,982	461,287	583,950	4,235,066
Balance, end of year	$ 619,819	$ 239,068	$ 518,108	$ 1,814,304	$ 461,755	$ 583,950	$ 4,237,004
Loans:							
Individually evaluated for impairment	$ 1,410,284	$ -	$ 180,611	$ 221,102	$ 1,417		$ 1,813,414
Collectively evaluated for impairment	59,437,612	22,930,959	49,695,896	173,897,569	44,245,663		350,207,699
Ending balance total loans	$ 60,847,896	$ 22,930,959	$ 49,876,507	$ 174,118,671	$ 44,247,080		$ 352,021,113

Note 4 Loans Receivable and Allowance for Credit Losses, continued

Federal regulations require that the Corporation periodically evaluate the risks inherent in its loan portfolio. In addition, the Corporation's regulatory agencies have authority to identify problem loans and, if appropriate, require them to be reclassified. There are three classifications for problem loans: Substandard, Doubtful and Loss. Substandard loans have one or more defined weaknesses and are characterized by the distinct possibility that the Corporation will sustain some loss if the deficiencies are not corrected. Doubtful loans have the weaknesses of loans classified as "Substandard," with additional characteristics that suggest the weaknesses make collection or recovery in full after liquidation of collateral questionable on the basis of currently existing facts, conditions and values. There is a high possibility of loss in loans classified as "Doubtful." A loan classified as "Loss" is considered uncollectible and of such little value that continued classification of the credit as a loan is not warranted. If a loan or a portion thereof is classified as "Loss," it must be charged-off, meaning the amount of the loss is charged against the allowance for credit losses, thereby reducing that reserve. The Corporation also classifies some loans as "Watch" or "Other Loans Especially Mentioned" ("OLEM"). Loans classified as Watch are performing assets and classified as pass credits but have elements of risk that require more monitoring than other performing loans. Loans classified as OLEM are assets that continue to perform but have shown deterioration in credit quality and require close monitoring.

Loans by credit quality risk rating at December 31, 2022 are as follows:

	Pass	Other Loans Especially Mentioned	Sub-Standard	Doubtful	Total
December 31, 2022:					
Commercial and agricultural loans	$ 65,286,667	$ 400,000	$ 480,384	$ -	$ 66,167,051
Real estate (RE) loans:					
Construction, land and land development	37,118,570	-	176,421	-	37,294,991
Residential 1-4 family	66,364,672	-	17,960	-	66,382,632
Commercial RE	192,585,003	-	1,280,985	-	193,865,988
Consumer and other loans	69,507,097	70,556	328,472	-	69,906,125
Subtotal	$ 430,862,009	$ 470,556	$ 2,284,222	$ -	433,616,787
Adjust: Net deferred loan costs					801,153
Total loans					$ 434,417,940

Note 4 Loans and Allowance for Credit Losses, continued

Loans by credit quality risk rating at December 31, 2021 are as follows:

	Pass	Other Loans Especially Mentioned	Sub-Standard	Doubtful	Total
December 31, 2021:					
Commercial and agricultural loans	$ 58,863,388	$ -	$ 1,984,508	$ -	$ 60,847,896
Real estate (RE) loans:					
Construction, land and land development	22,930,959	-	-	-	22,930,959
Residential 1-4 family	49,876,507	-	-	-	49,876,507
Commercial RE	172,518,510	-	1,600,161	-	174,118,671
Consumer and other loans	44,175,601	-	71,479	-	44,247,080
Subtotal	$ 348,364,965	$ -	$ 3,656,148	$ -	352,021,113
Adjust: Net deferred loan costs					222,035
Total loans					$ 352,243,148

An analysis of nonaccrual loans by category at December 31, 2022 and 2021 is as follows:

	2022	2021
Commercial and agricultural loans	$ 30,775	$ 1,410,284
Real estate (RE) loans:		
Commercial real estate	377,487	-
Consumer and other loans	54,808	417
Total nonaccrual loans	$ 463,070	$ 1,410,701

Note 4 Loans and Allowance for Credit Losses, continued

At December 31, 2022 and 2021, a summary of information pertaining to impaired loans is as follows:

	Unpaid Contractual Principal Balance	Recorded Investment with No Allowance	Recorded Investment with Allowance	Total Recorded Investment	Related Allowance	Average Recorded Investment	Interest Income Recognized
December 31, 2022:							
Commercial and agricultural loans	$ 1,937,550	$ 19,467	$ 1,570,302	$ 1,589,769	$ 108,504	$ 1,500,027	$ 102,729
Real estate (RE) loans:							
Construction, land and land development	176,421	176,421	-	176,421	-	88,210	11,263
Residential 1-4 family	185,668	17,960	167,708	185,668	2,676	183,140	11,817
Commercial RE	1,280,985	377,487	903,498	1,280,985	6,507	751,043	54,781
Consumer and other loans	325,298	257,133	68,165	325,298	33,153	163,358	9,969
Total	$ 3,905,922	$ 848,468	$ 2,709,673	$ 3,558,141	$ 150,840	$ 2,685,778	$ 190,559
December 31, 2021:							
Commercial and agricultural loans	$ 1,650,349	$ 1,391,752	$ 18,532	$ 1,410,284	$ 148	$ 1,899,078	$ -
Real estate (RE) loans:							
Construction, land and land development	-	-	-	-	-	454,964	-
Residential 1-4 family	180,611	180,611	-	180,611	-	373,031	12,359
Commercial RE	221,102	-	221,102	221,102	1,322	582,035	15,048
Consumer and other loans	1,919	-	1,417	1,417	468	10,436	119
Total	$ 2,053,981	$ 1,572,363	$ 241,051	$ 1,813,414	$ 1,938	$ 3,319,544	$ 27,526

The Corporation has no commitments to loan additional funds to borrowers whose loans are impaired.

Troubled Debt Restructurings – The restructuring of a loan is considered a "troubled debt restructuring" if both (i) the borrower is experiencing financial difficulties and (ii) the creditor has granted a concession. Concessions may include interest rate reductions or below market interest rates, principal forgiveness, restructuring amortization schedules and other actions intended to minimize potential losses.

There were no loans restructured during 2022. As of December 31, 2022, there were three commercial loans totaling $1,317,556 and one residential 1-4 family loan totaling $167,708 which were restructured prior to 2022. As of December 31, 2022, these loans were paying in accordance with their restructured terms.

Note 4 Loans and Allowance for Credit Losses, continued

There were no loans restructured during 2021. As of December 31, 2021, there were three commercial loans totaling $1,391,752, one residential 1-4 family loan totaling $180,611 and one consumer loan totaling $1,000 which were restructured prior to 2021. As of December 31, 2021, the residential 1-4 family and consumer loans were paying in accordance with their restructured terms. As of December 31, 2021, the commercial loans were on nonaccrual.

The following table illustrates an age analysis of past due loans as of December 31, 2022:

	30-89 Days Past Due	90 Days or More Past Due	Total Past Due	Current	Total Loans	Recorded Investment 90 Days or More Past Due and Still Accruing
December 31, 2022:						
Commercial and agricultural loans	$ 709,230	$ 30,774	$ 740,004	$ 65,427,047	$ 66,167,051	$ -
Real estate (RE) loans:						
Construction, land and land development	117,971	-	117,971	37,177,020	37,294,991	-
Residential 1-4 family	154,606	-	154,606	66,228,026	66,382,632	-
Commercial RE	-	377,487	377,487	193,488,501	193,865,988	-
Consumer and other loans	426,114	54,808	480,922	69,425,203	69,906,125	-
Subtotal	$ 1,407,921	$ 463,069	$ 1,870,990	$ 431,745,797	433,616,787	$ -
Adjust: Net deferred loan costs					801,153	
Total					$ 434,417,940	

Note 4 Loans and Allowance for Credit Losses, continued

The following table illustrates an age analysis of past due loans as of December 31, 2021:

	30-89 Days Past Due	90 Days or More Past Due	Total Past Due	Current	Total Loans	Recorded Investment 90 Days or More Past Due and Still Accruing
December 31, 2021:						
Commercial and agricultural loans	$ -	$ -	$ -	$ 60,847,896	$ 60,847,896	$ -
Real estate (RE) loans:						
Construction, land and land development	-	-	-	22,930,959	22,930,959	-
Residential 1-4 family	81,671	-	81,671	49,794,836	49,876,507	-
Commercial RE	927,621	-	927,621	173,191,050	174,118,671	-
Consumer and other loans	50,114	-	50,114	44,196,966	44,247,080	-
Subtotal	$ 1,059,406	$ -	$ 1,059,406	$ 350,961,707	352,021,113	$ -
Adjust: Net deferred loan costs					222,035	
Total					$ 352,243,148	

Loans totaling approximately $82,624,000 and $94,023,000 were pledged to secure borrowings at December 31, 2022 and 2021, respectively. Refer to Note 12 for additional information.

Note 5 SBA Servicing Asset

Loans serviced for others are not included in the accompanying balance sheets. The unpaid principal balances of loans serviced for others were $63,022,093 and $40,357,785 at December 31, 2022 and 2021, respectively. Servicing loans for others generally consists of collecting loan payments and disbursing payments to investors. The guaranteed portion of SBA loans are sold, and the Corporation recognized a net gain on sales of SBA loans of $3,254,216 and $2,758,063 in 2022 and 2021, respectively.

The Corporation accounts for servicing rights in accordance with provisions of authoritative guidance issued by the FASB. This authoritative guidance requires the Corporation to recognize servicing assets and/or liabilities and to amortize over the period of estimated servicing income or loss.

Note 5 SBA Servicing Asset, continued

The following summarizes the activity pertaining to SBA servicing rights measured using the amortization method, along with the aggregate activity in related valuation allowances, for the years ended December 31, 2022 and 2021:

	2022	2021
SBA servicing rights:		
Balance at beginning of year	$ 880,773	$ 616,322
Additions	686,843	423,095
Amortization	(189,584)	(158,644)
Balance at end of year	1,378,032	880,773
Valuation allowances:		
Balance at beginning of year	-	-
Additions	-	-
Reductions	-	-
Writedowns	-	-
Balance at end of year	-	-
SBA servicing assets, net	$ 1,378,032	$ 880,773

No allowance for impairment in the Corporation's SBA servicing rights was necessary during the years ended December 31, 2022 and 2021.

Note 6 Premises and Equipment

The components of premises and equipment at December 31 are as follows:

	2022	2021
Land	$ 4,267,266	$ 4,267,266
Buildings	9,290,998	9,249,445
Leasehold improvements	692,920	539,479
Equipment, furniture and fixtures	3,803,408	3,407,020
Construction in process	2,158,011	1,557,861
Lease right-of-use assets	132,037	266,200
Total cost	20,344,640	19,287,271
Less accumulated depreciation	(4,395,164)	(3,501,189)
Total	$ 15,949,476	$ 15,786,082

Depreciation and amortization charged against operations for the years ended December 31, 2022 and 2021 was $914,917 and $842,033, respectively.

Note 6 Premises and Equipment, continued

In May 2013, the Corporation opened a loan production center in Anacortes with a 12-month lease term at $1,050 per month. This lease has since been renewed for three additional two-year terms with current lease payment of $1,174 per month and a maturity of June 30, 2020. In May 2019, the Corporation entered into a new lease agreement which terminated the previous lease agreement when they opened a branch location in Anacortes. The new agreement is for a 36-month lease term, a maturity date of June 30, 2022 and provides for monthly lease payments of $8,000. During 2022, this lease was renewed for one year with a new maturity date of June 30, 2023 and provides for monthly lease payments of $8,600. There are two one-year renewals available as of December 31, 2022.

A loan production office was opened in Freeland in February 2016 with a 12-month lease term at $1,266 per month. This lease was extended until March 2021 at $2,394 base monthly rent. The Freeland branch opened at this location in April 2017. The branch moved to the Freeland branch included in the branch acquisition purchased during 2021; therefore, this lease was not renewed. In October 2021, the Corporation entered into a lease agreement for a loan production office in Friday Harbor, Washington. This location was converted into a branch location during 2022. The lease term is 36 months and provides for monthly lease payments of $3,996. During 2022, the Corporation entered into a lease agreement for a loan production office in Olympia, Washington through June 30, 2023. The monthly lease payments under this lease agreement are $2,281.

The Corporation also leases various equipment under operating leases. During 2019, the Corporation adopted ASU No. 2016-02 which required the recognition of certain operating leases on the balance sheet as lease right-of-use assets (reported as a component of premises and equipment) and related lease liabilities (report as a component of accrued expenses and other liabilities).

The weighted-average discount rate was 5.73%. The following table reconciles future undiscounted lease payments due under non-cancelable operating leases (those amounts subject to recognition) to the aggregate operating lease liability as of December 31, 2022:

2023	$ 125,528
2024	43,104
2025	2,090
2026	-
2027	-
Total undiscounted operating lease liability	170,722
Imputed interest	(38,685)
Total operating lease liability included in the balance sheet	$ 132,037

Rental expense was $248,238 and $220,564 for 2022 and 2021, respectively, which is included in occupancy and equipment expense.

Note 7 Other Intangible Assets

Effective April 30, 2021, the Corporation purchased certain assets and assumed certain liabilities of the Freeland branch from another financial institution. A premium of $1,249,316 was paid by the Corporation which was identified as core deposit intangibles. The core deposit intangibles are being amortized using a straight-line method over their estimated useful life of 10 years. The carrying amounts of $1,041,366 and $1,155,887 at December 31, 2022 and 2021, respectively, are net of accumulated amortization totaling $207,950 and $93,429, respectively. Amortization expense on the core deposit intangibles was $114,521 and $93,429 during 2022 and 2021, respectively. Refer to Note 24 for additional information regarding the acquisition.

As of December 31, 2022, amortization expense for the core deposit intangibles for the next five years and in the aggregate thereafter is as follows:

2023	$ 124,932
2024	124,932
2025	124,932
2026	124,931
2027	124,931
Thereafter	416,708
Total	$ 1,041,366

Note 8 Bank-Owned Life Insurance

During 2021, the Corporation purchased life insurance policies on select key officers. The Corporation is the beneficiary of these policies. In the event of death, the officer's designated beneficiary receives $50,000 of the death benefit if the officer is still employed by the Corporation at the time of death. The initial premium paid was $9,300,000. The carrying amount of bank-owned life insurance totaled $9,702,288 and $9,433,134 at December 31, 2022 and 2021, respectively. Net earnings on bank-owned life insurance totaling $269,154 and $133,134 was recorded through non-interest income during 2022 and 2021, respectively.

Note 9 Deposits

The composition of consolidated deposits at December 31 is as follows:

	2022	2021
Non-interest checking	$ 117,348,306	$ 120,056,929
Interest-bearing checking and money market	182,043,719	181,810,563
Savings deposits	69,370,544	52,910,834
Time deposits, less than $250,000	48,876,906	59,914,193
Time deposits, $250,000 or more	13,069,051	17,731,216
Total deposits	$ 430,708,526	$ 432,423,735

Note 9 Deposits, continued

The scheduled maturities of time deposits at December 31, 2022 are as follows:

2023	$ 30,332,346
2024	19,983,178
2025	10,982,745
2026	317,861
2027	329,827
Total	$ 61,945,957

Included in deposits are institutional deposits obtained from institutions outside of the Corporation's primary market area of $250,000 and $5,092,000 at December 31, 2022 and 2021, respectively. In addition, the Corporation held brokered deposits of $10,001,024 and $10,010,428 at December 31, 2022 and 2021, respectively.

Note 10 Federal Income Taxes

The principal factors causing a variation from the statutory tax rate of 21% are as follows:

	2022	2021
Income tax at statutory rate	$ 964,494	$ 947,059
Tax-exempt interest income	(58,710)	(21,890)
Earnings on bank-owned life insurance	(56,522)	(27,958)
Nondeductible expenses	13,355	9,609
Stock-based compensation	7,717	6,573
Other	(192)	12,823
Federal income tax expense	$ 870,142	$ 926,216

The components of the income tax expense were as follows:

	2022	2021
Current	$ 759,177	$ 362,554
Deferred	110,965	563,662
Federal income tax expense	$ 870,142	$ 926,216

Note 10 Federal Income Taxes, continued

The tax effects of temporary differences that give rise to significant portions of consolidated deferred tax assets and liabilities are:

	2022	2021
Deferred tax assets:		
Organization expenditures	$ 1,960	$ 1,960
Basis differences on other real estate owned	-	12,394
Off-balance-sheet liability	114,258	34,860
Allowance for credit losses on loans	998,797	625,828
Allowance for credit losses on HTM securities	105,000	-
Nonqualified stock options	42,731	33,907
Nonaccrual loan interest	473	27,183
Restricted stock	1,927	1,648
Amortization of core deposit intangibles	13,061	6,502
Unrealized loss on available-for-sale securities	954,042	79,340
Deferred compensation	26,555	-
Total deferred tax asset	2,258,804	823,622
Deferred tax liabilities:		
Accrual to cash adjustment	(209,539)	(16,869)
Depreciation	(300,516)	(313,536)
Other	(2,369)	(644)
Total deferred tax liability	(512,424)	(331,049)
Net deferred tax asset	$ 1,746,380	$ 492,573

During 2021, the Corporation fully utilized the net operating loss carryover from prior years.

Note 11 Related Party Transactions

During 2022 and 2021, the Corporation had transactions made in the ordinary course of business with related parties. All loans included in such transactions were made on substantially the same terms, including interest rate and collateral, as those prevailing at the time for comparable transactions with other persons, and did not, in the opinion of management, involve more than normal credit risk or present other unfavorable features.

Note 11 Related Party Transactions, continued

A summary of these transactions follows:

	Balance Beginning of Year	Additions	Amounts Collected	Balance End of Year
For the year ended: **December 31, 2022**	$ 5,369,907	$ 2,958,362	$ (342,453)	$ 7,985,816
For the year ended: **December 31, 2021**	$ 5,216,079	$ 488,023	$ (334,195)	$ 5,369,907

The Corporation also had unfunded commitments to related parties of approximately $706,000 and $877,000 at December 31, 2022 and 2021, respectively.

At December 31, 2022 and 2021, the Corporation held related party deposits of approximately $9,044,000 and $9,037,000, respectively.

During 2021, the Corporation borrowed $2,500,000 from a director. At December 31, 2022 and 2021, the total outstanding balance was $2,500,000. Total interest expense of $125,000 and $94,521 was recognized on this loan during 2022 and 2021, respectively. Refer to Note 15 for additional information.

Note 12 Federal Home Loan Bank Borrowings

The Bank is a member of the Federal Home Loan Bank (FHLB) of Des Moines which entitles it to certain benefits including a variety of borrowing options such as overnight advances or long-term advances at fixed or variable rates. Credit capacity is primarily determined by the value of assets collateralized at the FHLB, funds on deposit at the FHLB and stock owned by the Bank. Credit is limited to 45% of the Bank's total assets at December 31, 2022.

Advances on these lines at December 31 were as follows:

	2022	2021
Long-term advances	$ 25,000,000	$ 5,000,000
Overnight advances	10,000,000	-
Total	$ 35,000,000	$ 5,000,000

During 2020, a long-term advance was obtained in the amount of $5,000,000 which has a maturity date of March 4, 2025. The interest rate on this advance was 0.98%. During 2022, a long-term advance totaling $20,000,000 was obtained which has a maturity date of November 22, 2027. The interest rate on this long-term advance was 4.34%. At December 31, 2022 and 2021, the outstanding balance on this line of credit was $35,000,000 and $5,000,000, respectively. The overnight advances are due on January 3, 2023. Collateral pledged to the FHLB as of December 31, 2022 and 2021 included loans with outstanding balances of approximately $82,624,000 and $94,023,000, respectively. The Bank has available borrowing capacity of approximately $11,468,000 based on pledged collateral at December 31, 2022.

Note 13 Lines of Credit

At December 31, 2022 and 2021, the Corporation has a $10,000,000 unsecured line of credit with Pacific Coast Bankers' Bank (PCBB). There were no borrowings on this line at December 31, 2022 or 2021.

The Corporation also has a line of credit with Federal Home Loan Bank as discussed in Note 12.

Note 14 Subordinated Debt

On February 25, 2022, the Corporation received proceeds totaling $17,000,000 from issuance of subordinated debt. The maturity date of the subordinated debt is March 31, 2032. The initial interest rate is 4.25% computed on a 360-day year consisting of twelve 30-day months and payable semi-annually in arrears on September 30 and March 31 of each year beginning on September 30, 2022. The interest rate is fixed through March 31, 2027. After March 31, 2027, the interest rate is the higher of (a) the rate of 3.75% or (b) the rate reset quarterly based on the Three-Month Term SOFR Conventions. On or after the fifth anniversary date, the Corporation can redeem the debt in whole or in party at any time. The indebtedness is subordinate and junior in right to payment to the prior payment in full of all claims of creditors of the Corporation and depositors of SaviBank, whether now outstanding or subsequently created, assumed, guaranteed or incurred. The Corporation used $3,000,000 of these proceeds to inject capital into SaviBank during 2022. No principal payments are due on this debt for the next five years. The outstanding balance at December 31, 2022 is $17,000,000.

Note 15 Note Payable – Related Party

During 2021, the Corporation borrowed $2,500,000 from a director. The interest rate on this note is 5%. Interest only payments are due quarterly beginning June 30, 2021 and the remaining interest and principal are due at maturity on March, 31, 2023. At December 31, 2022 and 2021, the total outstanding balance was $2,500,000. This note is secured by the Bank stock held by the Corporation. Refer to Note 11 for additional information. This note was renewed as of March 31, 2023. Refer to Note 25 for additional information.

Note 16 Commitments and Contingent Liabilities

In the normal course of business, the Corporation has outstanding commitments and contingent liabilities, such as commitments to extend credit, which are not included in the accompanying financial statements. The Corporation's exposure to credit loss in the event of nonperformance by the other party to the financial instruments for commitments to extend credit is represented by the contractual or notional amount of those instruments. The Corporation uses the same credit policies in making such commitments as it does for instruments that are included in the balance sheet.

Commitments to extend credit and possible credit risk were approximately as follows:

	2022	2021
Commitments to extend credit	$ 70,591,000	$ 57,509,000
Standby letters of credit	5,338,000	5,346,000

Note 16 Commitments and Contingent Liabilities, continued

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Corporation evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Corporation upon extension of credit, is based on management's credit evaluation. Collateral held varies but may include accounts receivable, inventory, property and equipment, and income-producing commercial properties. The Corporation has not been required to perform on any financial guarantees nor incurred any losses on its commitments during 2022 or 2021.

The Corporation is subject to claims and lawsuits which arise primarily in the ordinary course of business. It is the opinion of management that the disposition or ultimate resolution of such claims and lawsuits will not have a material adverse effect on the financial position of the Corporation.

The Corporation issues various representations and warranties associated with the sale of loans. The Corporation has not experienced any significant losses in the years ended December 31, 2022 and 2021 regarding these representations and warranties.

The Corporation sells the guaranteed portion of SBA loans. In the event that the SBA guarantee is deemed invalid, the Corporation is liable to the purchaser of these guaranteed portions in the event that the loan is deemed uncollectible. At December 31, 2022 and 2021, the guaranteed portions totaled $63,022,093 and $40,357,785, respectively.

The Corporation participates in the Washington State Public Depository program which requires institutions to collateralize uninsured public deposits at 50% effective July 1, 2016 (previously 100%). At December 31, 2022 and 2021, the Corporation had pledged $236,017 and $273,210, respectively, to secure public deposits. Refer to Note 3 – Investment Securities for additional information.

Note 17 Concentrations of Credit Risk

The Corporation maintains its cash accounts with several correspondent banks. Generally, amounts placed or invested in bank accounts are insured by the Federal Deposit Insurance Corporation (FDIC) up to $250,000 per bank. There were uninsured deposits in bank accounts of $752,107 and $4,921,156 at December 31, 2022 and 2021, respectively. Furthermore, federal funds sold are essentially uncollateralized loans to other financial institutions. Management regularly evaluates the credit risk associated with the counterparties to these transactions and believes that the Corporation is not exposed to any significant credit risks on cash and cash equivalents.

The Corporation grants agribusiness, commercial, consumer and real estate loans to customers within Skagit, Island and Whatcom counties, Washington and the surrounding areas. Concentrations of credit by loan type are set forth in Note 4 – Loans Receivable and Allowance for Credit Losses.

Note 18 Regulatory Capital

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

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios (set forth in the table on the following page) of total Tier 1 capital (as defined in the regulations) to risk-weighted assets (as defined), and of Tier 1 capital (as defined) to average assets (as defined). Management believes, as of December 31, 2022 and 2021, that the Bank met all capital adequacy requirements to which it was subject.

Effective January 1, 2019, the Bank was required to establish a capital conservation buffer of 2.50%, increasing the minimum required total risk-based capital, Tier 1 risk-based and common equity Tier 1 capital to risk-weighted assets it must maintain to avoid limits on capital distributions and certain bonus payments to executive officers and similar employees.

The Bank's Tier 1 capital consists of shareholder's equity excluding unrealized gains and losses on securities available-for-sale and other intangible assets.

Note 18 Regulatory Capital, continued

To be categorized as well capitalized in 2022 and 2021, the Bank must maintain minimum common equity 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 category.

The Bank's actual and required capital amounts and ratios are as follows (dollars in thousands):

	Actual		Minimum Required for Capital Adequacy Purposes		Required to be Well Capitalized Under the Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2022:						
Total Risk-based Capital (to Risk-weighted Assets)	$ 49,504	10.38%	$ 38,144	8.00%	$ 47,681	10.00%
Tier 1 Capital (to Risk-weighted Assets)	$ 43,533	9.13%	$ 28,608	6.00%	$ 38,144	8.00%
Common Equity Tier 1 Capital (to Risk-weighted Assets)	$ 43,533	9.13%	$ 21,456	4.50%	$ 30,992	6.50%
Leverage Capital (to adjusted Total Average Assets)	$ 43,533	8.56%	$ 20,345	4.00%	$ 25,431	5.00%
As of December 31, 2021:						
Total Risk-based Capital (to Risk-weighted Assets)	$ 42,413	11.20%	$ 30,299	8.00%	$ 37,874	10.00%
Tier 1 Capital (to Risk-weighted Assets)	$ 38,010	10.04%	$ 22,725	6.00%	$ 30,299	8.00%
Common Equity Tier 1 Capital (to Risk-weighted Assets)	$ 38,010	10.04%	$ 17,043	4.50%	$ 24,618	6.50%
Leverage Capital (to adjusted Total Average Assets)	$ 38,010	7.90%	$ 19,242	4.00%	$ 24,052	5.00%

Note 19 Stock-Based Compensation

Long-Term Equity Incentive Plan

Effective May 23, 2019, the shareholders approved the adoption of the 2019 Long-Term Equity Incentive Plan (2019 Plan) which provides for the grant of stock awards to eligible employees, officers and non-employee directors. The 2019 Plan replaced the 2013 Long-Term Equity Incentive Plan (2013 Plan), which provided for the grant of up to 100,000 shares. Effective July 25, 2013, the shareholders approved the adoption of the 2013 Long-Term Equity Incentive Plan (2013 Plan) which provided for the grant of stock awards to eligible employees, officers and non-employee directors. The 2013 Plan replaced the 2005 Stock Option Plan (2005 Plan) which provided for the grant of up to 50,000 shares. The 2019 Plan permits the grant of Nonqualified Stock Options, Incentive Stock Options, Restricted Stock and Restricted Stock Unit Awards. The maximum number of shares of Common Stock which may be issued under all awards granted to participants under the 2019 Plan shall be 250,000 shares. No more than 50,000 shares of the 250,000 shares may be issued as Restricted Stock Grants or Restricted Stock Unit Awards. Shares of Common Stock issued under the Plan shall be authorized but unissued shares. At December 31, 2022, there were 162,200 shares available for future grants under the 2019 Plan.

During 2022, there were 300 and 40,000 stock options granted at an exercise price of $10.63 and $9.85, respectively. During 2021, there were 40,000, 2,000 and 1,000 stock options granted at an exercise price of $10.18, $11.10 and $10.12, respectively. These options vest over five years and have a term of 10 years. During 2022 and 2021, there were no restricted stock awards granted.

The compensation cost that has been charged against income for stock options under these Plans was $78,769 and $59,546 for the years ended December 31, 2022 and 2021, respectively.

The Corporation uses the Black-Scholes option pricing model to estimate the fair value of each option grant on the date of grant or modification. The Corporation amortizes the estimated fair value to stock compensation expense using the straight-line method over the vesting period of the option. Following is a description of the significant assumptions used in the option-pricing model:

***Expected Term*:** The expected term is the period of time that granted options are expected to be outstanding. The Corporation estimates the expected term based on historical patterns of option exercises, as well as potential future events that may increase liquidity. These factors are believed to reflect future exercise behavior.

Expected Volatility: Volatility is calculated based on trading of the Corporation's stock over the last three years, which is comparable to historical stock prices of similar banks going back over the estimated life of the option and averaging the volatilities of these banks.

***Risk-Free Interest Rate*:** The Corporation bases the risk-free interest rate used in the Black-Scholes option valuation model on the market yield in effect at the time of the option grant provided from the Federal Reserve Board's Statistical Releases and Historical publications from the Treasury constant maturities rates for the equivalent remaining terms.

***Dividends*:** The Corporation does not have plans to pay cash dividends in the future. Therefore, the Corporation uses an expected dividend yield of zero in the Black-Scholes option valuation model.

Note 19 Stock-Based Compensation, continued

Long-Term Equity Incentive Plan, continued

The following assumptions were used to estimate the value of options granted for the year ended December 31, 2022 and 2021:

	2022	2021
Weighted-average expected term	7.00 years	7.00 years
Expected stock price volatility	40.16-40.69%	41.33-42.98%
Risk-free interest rate	2.80-2.88%	1.20-1.46%
Weighted-average risk-free interest rate	2.80-2.88%	1.20-1.46%
Expected dividends	0%	0%

Option activity under the Plans for the years ended December 31, 2022 and 2021 is summarized as follows:

Options	Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term
Outstanding at January 1, 2021	125,996	$ 7.45	
Granted	43,000	10.22	
Exercised	(3,720)	6.85	
Forfeited or cancelled	(1,760)	9.77	
Outstanding at December 31, 2021	163,516	$ 8.17	4.94
Vested or expected to vest at December 31, 2021	163,516	$ 8.17	4.94
Exercisable at December 31, 2021	115,761	$ 7.36	3.32
Outstanding at January 1, 2022	163,516	$ 8.17	
Granted	40,300	9.86	
Exercised	(1,490)	8.87	
Forfeited or cancelled	(4,340)	9.43	
Outstanding at December 31, 2022	197,986	$ 8.48	4.94
Vested or expected to vest at December 31, 2022	197,986	$ 8.48	4.94
Exercisable at December 31, 2022	127,901	$ 7.64	2.81

There were 1,490 and 3,720 options exercised during the year ended December 31, 2022 and 2021, respectively, for total proceeds of $13,221 and $25,490.

Note 19 Stock-Based Compensation, continued

Long-Term Equity Incentive Plan, continued

A summary of the status of the Corporation's nonvested shares as of December 31, 2022, and changes during the year ended December 31, 2022, is presented below:

Nonvested Shares	Shares	Weighted-Average Grant-Date Fair Value
Nonvested at January 1, 2022	47,755	$ 4.43
Granted	40,300	4.58
Vested	(14,210)	4.43
Forfeited	(3,760)	4.50
Nonvested at December 31, 2022	70,085	$ 4.51

As of December 31, 2022, there was $252,959 of total unrecognized compensation cost related to nonvested stock options granted under the Plan. Total unrecognized compensation costs will be adjusted for future changes in estimated forfeitures. The Corporation expects to recognize that cost over a period of approximately 6.50 years.

During 2022 and 2021, there were no restricted stock awards granted. As of December 31, 2022, there were 2,000 nonvested restricted stock awards outstanding. Stock compensation totaling $12,709 and $12,894 was recorded during 2022 and 2021, respectively, relating to restricted stock awards. At December 31, 2022, there was unrecognized compensation expense relating to these awards totaling $14,446. The Corporation expects to recognize that cost over a period of three years.

Stock Warrants

On June 21, 2018, a stock warrant was issued which entitles the warrant holder to purchase 334,004 shares of the Corporation's common stock at a price of $8.00 per share on or before March 31, 2022. In July 2021, the expiration date was extended to March 31, 2027. This stock warrant remains outstanding as of December 31, 2022 and 2021.

On October 2, 2014, a stock warrant was issued which entitles the warrant holder to purchase 310,000 shares of common stock of the Corporation at a price of $6.25 per share on or before October 2, 2019. In December 2017, the expiration date was extended to March 31, 2022. In July 2021, the expiration date was extended to March 31, 2027. This stock warrant remains outstanding as of December 31, 2022 and 2021.

During 2012, a total of 115,553 stock warrants were issued in conjunction with the March 2012 Stock Offering. One stock warrant to purchase one share of common stock was issued to each person who purchased two shares of common stock through this offering. The warrants entitle the warrant holder the right to purchase Corporation stock at a price of $10.00 per share on or before June 29, 2015. On March 12, 2015, the expiration date was extended for three years to June 29, 2018. In December 2017, the expiration date was extended to March 31, 2022. In July 2021, the expiration date was extended to March 31, 2027. These warrants remain outstanding as of December 31, 2022 and 2021.

Note 19 Stock-Based Compensation, continued

Stock Warrants, continued

In June 2005, the Board of Directors authorized the granting of stock warrants to the Corporation's organizers in exchange for providing $700,000 in seed capital which funded the organizational expenses of the Corporation. Each Director (eight) received 1,750 warrants that entitles the holder to purchase one share of common stock at a price of $50.00 per share on or before May 31, 2015. On March 12, 2015, the existing warrants were allowed to expire and were replaced with new warrants for the same amount of shares, (1,750 per Director) to expire on October 2, 2019 at a price of $6.25 per share for those Directors (four) who are on the Board as of the date of this action and who provided seed capital which funded the organization expenses of the Corporation. In December 2017, the expiration date was extended to March 31, 2022. In July 2021, the expiration date was extended to March 31, 2027. At December 31, 2022 and 2021, there were 7,000 stock warrants outstanding for the Corporation's organizing Directors.

Note 20 Employee Benefit Plans

The Corporation has a 401(k) profit sharing plan (the "Plan") covering substantially all of its employees. Employees are eligible to participate in the Plan if they are 18 years of age and have completed three months of service. Eligible employees may contribute through payroll deductions and are 100% vested at all times in their deferral contributions account. The Corporation is allowed to make annual matching contributions and/or employer "non-elective" contributions at its discretion. Participants are 100% vested in employer contributions after five years of service. During 2022 and 2021, employer matching contributions to the 401(k) Plan totaled $373,584 and $223,847, respectively.

During 2021, the Corporation's Board of Directors approved a Supplemental Executive Retirement Plan (SERP) for the CEO which provides annual benefits of $60,000 paid in equal monthly payments upon retirement for a period of 10 years. At December 31, 2022 and 2021, accruals totaling $126,452 and $61,431, respectively, relating to the SERP were included in accrued expenses and other liabilities on the consolidated balance sheet. During 2022 and 2021, $65,021 and $61,431, respectively, was expensed relating to the SERP and is included in salaries and employee benefits on the consolidated income statement.

Note 21 Compensated Absences

Employees of the Corporation are entitled to paid time off (PTO), depending on job classification, length of service and other factors. The Corporation has determined that it was impracticable to estimate the amount of compensation for future absences, and, accordingly, no liability has been recorded in the accompanying financial statements. It is the Corporation's policy to recognize the costs of compensated absences when actually paid to employees.

Note 22 Fair Values of Financial Instruments

As discussed in Note 2, current accounting guidance (ASU 2016-01) requires that fair value disclosures use exit pricing. Fair values disclosed in the table below are based on the methods used in prior years and do not comply with current guidance, with the exception of the fair value for loans and deposits for 2022 and 2021 which were calculated in accordance with the current guidance. In addition, new guidance requires that financial assets and liabilities be presented by measurement category which has not been provided. The estimated fair values of the Corporation's financial instruments as of December 31, 2022 and 2021 are as follows (in thousands):

	2022		2021	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Financial assets:				
Cash and due from banks	$ 6,085	$ 6,085	$ 8,046	$ 8,046
Interest-bearing deposits with financial institutions	14,100	14,100	49,753	49,753
Federal funds sold	-	-	7,715	7,715
Investment securities	38,103	38,206	34,267	34,247
Federal Home Loan Bank stock	1,975	1,975	691	691
Pacific Coast Bankers' Bank stock	190	190	190	190
Loans held-for-sale	1,523	1,523	2,839	2,839
Loans, net	427,066	407,191	345,167	343,025
Bank-owned life insurance	9,702	9,702	9,433	9,433
Interest receivable	1,458	1,458	960	960
SBA servicing asset	1,378	1,378	881	881
Financial liabilities:				
Deposits	430,709	429,384	432,424	432,931
FHLB borrowings	35,000	34,580	5,000	4,942
Subordinated debt	17,000	17,000	-	-
Note payable	2,500	2,500	2,500	2,500
Interest payable	395	395	93	93

The carrying amounts in the preceding table are included in the consolidated balance sheets under the applicable captions.

Note 23 Fair Value Measurements

The Corporation previously adopted authoritative guidance issued by the FASB regarding fair value measurements for financial assets and financial liabilities. The authoritative guidance defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles and expands disclosures about fair value measurements. However, the Corporation has not fully adopted the most recent guidance issued by the FASB (ASU 2016-01). As discussed in Note 2, the new guidance requires that exit price notion be used when measuring the fair value of financial instruments for disclosure purposes. The Corporation has determined that the cost to fully implement exit pricing is prohibitive and there is no material impact to the financial statements.

The authoritative guidance issued by the FASB defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. A fair value measurement assumes that the transaction to sell the asset or transfer the liability occurs in the principal market for the asset or liability or, in the absence of a principal market, the most advantageous market for the asset or liability. The price in the principal (or most advantageous) market used to measure the fair value of the asset or liability shall not be adjusted for transaction costs. An orderly transaction is a transaction that assumes exposure to the market for a period prior to the measurement date to allow for marketing activities that are usual and customary for transactions involving such assets and liabilities; it is not a forced transaction. Market participants are buyers and sellers in the principal market that are (i) independent, (ii) knowledgeable, (iii) able to transact and (iv) willing to transact.

The authoritative guidance issued by the FASB requires the use of valuation techniques that are consistent with the market approach, the income approach and/or the cost approach. The market approach uses prices and other relevant information generated by market transactions involving identical or comparable assets and liabilities. The income approach uses valuation techniques to convert future amounts, such as cash flows or earnings, to a single present amount on a discounted basis. The cost approach is based on the amount that currently would be required to replace the service capacity of an asset (replacement cost). Valuation techniques should be consistently applied. Inputs to valuation techniques refer to the assumptions that market participants would use in pricing the asset or liability. Inputs may be observable, meaning those that reflect the assumptions market participants would use in pricing the asset or liability developed based on market data obtained from independent sources, or unobservable, meaning those that reflect the reporting entity's own assumptions about the assumptions market participants would use in pricing the asset or liability developed based on the best information available in the circumstances.

In that regard, the authoritative guidance establishes a fair value hierarchy for valuation inputs that gives the highest priority to quoted prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs. The fair value hierarchy is as follows:

- ***Level 1 Inputs:*** Unadjusted quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date.
- ***Level 2 Inputs:*** Inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. These might include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability (such as interest rates, volatilities, prepayment speeds, credit risks, etc.) or inputs that are derived principally from, or corroborated by, market data by correlation or other means.

Note 23 Fair Value Measurements, continued

- ***Level 3 Inputs:*** Unobservable inputs for determining the fair values of assets or liabilities that reflect an entity's own assumptions about the assumptions that market participants would use in pricing the assets or liabilities.

A description of the valuation methodologies used for instruments measured at fair value, as well as the general classification of such instruments pursuant to the valuation hierarchy, is set forth below.

In general, fair value is based upon quoted market prices, where available. If such quoted market prices are not available, fair value is based upon internally developed models that primarily use, as inputs, observable market-based parameters. Valuation adjustments may be made to ensure that financial instruments are recorded at fair value. These adjustments may include amounts to reflect counterparty credit quality and the Corporation's creditworthiness, among other things, as well as parameters. Any such valuation adjustments are applied consistently over time. The Corporation's valuation methodologies may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. While management believes the Corporation's valuation methodologies are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different estimate of fair value at the reporting date.

Securities Available-for-Sale: U.S. Treasury securities are reported at fair value utilizing Level 1 inputs. Other securities classified as available-for-sale are reported at fair value utilizing Level 2 inputs. For these securities, the Corporation obtains fair value measurements from an independent pricing service. The fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, live trading levels, trade execution data, market consensus prepayment speeds, credit information and the bond's terms and conditions, among other things.

Impaired Loans: Certain impaired loans are reported at the fair value of the underlying collateral if repayment is expected solely from the collateral. Collateral values are estimated using Level 2 inputs based on observable market data or Level 3 inputs based on customized discounting criteria.

Other Real Estate Owned: Other real estate owned represents foreclosed assets that are reported at the fair value less estimated selling costs of the underlying property. The fair values are estimated using Level 2 inputs based on observable market data or Level 3 inputs based on information obtained from customized discounting criteria.

Note 23 Fair Value Measurements, continued

The following table summarizes financial assets measured at fair value on a recurring basis as of December 31, 2022 and 2021, segregated by the level of the valuation inputs within the fair value hierarchy utilized to measure the fair value. At December 31, 2022 and 2021, there were no financial liabilities measured at fair value on a recurring basis.

	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs	Total Fair Value
December 31, 2022				
Available-for-Sale				
U.S. Treasury bills	$ 1,936,719	$ -	$ -	$ 1,936,719
U. S. Government agency	-	483,137	-	483,137
Municipal bonds	-	2,796,290	-	2,796,290
U.S. Government agency mortgage-backed securities	-	13,260,897	-	13,260,897
Collateralized mortgage obligations	-	6,217,125	-	6,217,125
SBA pools	-	5,735,711	-	5,735,711
Corporate bonds	-	3,122,700	-	3,122,700
Totals	$ 1,936,719	$ 31,615,860	$ -	$ 33,552,579
December 31, 2021				
Available-for-Sale				
U.S. Government agency	$ -	$ 517,332	$ -	$ 517,332
Municipal bonds	-	1,339,963	-	1,339,963
U.S. Government agency mortgage-backed securities	-	14,546,350	-	14,546,350
Collateralized mortgage obligations	-	6,490,470	-	6,490,470
SBA pools	-	4,925,254	-	4,925,254
Corporate bonds	-	3,397,281	-	3,397,281
Totals	$ -	$ 31,216,650	$ -	$ 31,216,650

Certain financial assets are measured at fair value on a non-recurring basis; that is, the instruments are not measured at fair value on an ongoing basis but are subject to fair value adjustments in certain circumstances (for example, when there is evidence of impairment). Financial assets measured at fair value on a non-recurring basis include certain impaired loans reported at the fair value of the underlying collateral if repayment is expected solely from the collateral. Collateral values are estimated using Level 2 inputs based on observable market data (current appraisals) or Level 3 inputs based on customized discounting criteria.

Note 23 Fair Value Measurements, continued

The following table summarizes financial assets measured at fair value on a non-recurring basis as of December 31, 2022 and 2021, segregated by the level of the valuation inputs within the fair value hierarchy utilized to measure the fair value:

	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs	Total Fair Value
December 31, 2022:				
Impaired loans	$ -	$ 1,061,816	$ 2,496,325	$ 3,558,141
Less specific valuation allowance for possible loan losses	-	(59,195)	(91,645)	(150,840)
Impaired loans, net	$ -	$ 1,002,621	$ 2,404,680	$ 3,407,301
December 31, 2021:				
Impaired loans	$ -	$ -	$ 1,813,414	$ 1,813,414
Less specific valuation allowance for possible loan losses	-	-	(1,938)	(1,938)
Impaired loans, net	$ -	$ -	$ 1,811,476	$ 1,811,476

A reconciliation of assets measured using Level 3 inputs for the years ended December 31, 2022 and 2021 is provided below:

		December 31, 2022	December 31, 2021
	Opening Balance	$ 1,813,414	$ 3,498,725
(a)	Transfers into Level 3	1,011,061	239,634
(b)	Transfers out of Level 3	-	-
	Settlements/payments	(328,150)	(1,924,945)
	Ending Balance	$ 2,496,325	$ 1,813,414

(a) Transfer from Level 2 to Level 3; loans are no longer collateral dependent, and impairment is based on discounted cash flows.

(b) Transferred from Level 3 to Level 2 because loan is now considered to be collateral dependent. Impairment based on current appraisal.

Note 23 Fair Value Measurements, continued

Certain nonfinancial assets are measured at fair value on a non-recurring basis. Nonfinancial assets measured at fair value on a non-recurring basis include other real estate owned which, upon initial recognition, were remeasured and reported at fair value through a charge-off to the allowance for credit losses and certain other real estate owned, which subsequent to their initial recognition, were remeasured at fair value through a writedown included in other non-interest expense. The fair value of other real estate owned is estimated using Level 2 inputs based on observable market data or Level 3 inputs based on customized discounting criteria. At December 31, 2022 and 2021, the Corporation had other real estate owned totaling $654,495 and $921,748, respectively. Fair values were determined using Level 2 measurements.

The following tables presents foreclosed assets that were remeasured and reported at fair value:

	2022	2021
Foreclosed assets remeasured at initial recognition:		
Carrying value of foreclosed assets prior to remeasurement	$ -	$ 654,495
Charge-offs recognized in the allowance for credit losses	-	-
Fair Value	$ -	$ 654,495
Foreclosed assets remeasured subsequent to initial recognition:		
Carrying value of foreclosed assets prior to remeasurement	$ -	$ 426,275
Writedowns included in other non-interest expense	-	(78,406)
Fair Value	$ -	$ 347,869

Charge-offs recognized upon loan foreclosures are generally offset by general or specific allocations of the allowance for credit losses and generally do not significantly impact the Corporation's provision for loan losses. Regulatory guidelines require the Corporation to reevaluate the fair value of other real estate owned on at least an annual basis.

Note 24 Acquisition

Effective April 30, 2021, the Bank purchased and assumed certain assets and liabilities of the Freeland branch from another financial institution for a premium of $1,249,316 which has been identified as core deposit intangibles. Refer to Note 7 for additional information on the core deposit intangibles. The estimated fair values of the assets acquired and liabilities assumed are set forth below:

	2021
Cash and cash equivalents	$ 103,811
Loans	1,925,440
Premises and equipment	910,591
Core deposit intangibles	1,249,316
Other assets	1,697
Deposits	(24,062.892)
Other liabilities	(2,533)
Total cash paid by seller	$ (19,874,570)

Note 25 Subsequent Events

On March 31, 2023, the note payable – related party was renewed for three years with a fixed interest rate of 7.00%. Refer to Note 15 for additional information on this note.

OTHER FINANCIAL INFORMATION

SAVI FINANCIAL CORPORATION, INC. AND SUBSIDIARY
CONSOLIDATING BALANCE SHEET
DECEMBER 31, 2022

	SAVI FINANCIAL	SAVI BANK	ELIMINATIONS	CONSOLIDATED BALANCES 2022
ASSETS				
Cash and due from banks	$ 2,486,718	$ 6,084,792	$ (2,486,718)	$ 6,084,792
Interest-bearing deposits in other financial institutions maturing in less than three months	10,177,407	3,922,266	-	14,099,673
Investment securities	-	38,102,579	-	38,102,579
Federal Home Loan Bank stock	-	1,975,100	-	1,975,100
Pacific Coast Bankers' Bank stock	-	190,000	-	190,000
Investment in subsidiary	42,362,668	-	(42,362,668)	-
Loans held-for-sale	-	1,523,000	-	1,523,000
Loans receivable, net of allowance for credit losses and deferred loan fees and costs	-	427,065,685	-	427,065,685
Premises and equipment, net	-	15,949,476	-	15,949,476
Foreclosed and repossessed assets	-	669,022	-	669,022
Accrued interest receivable	-	1,458,376	-	1,458,376
Core deposit intangibles, net	-	1,041,366	-	1,041,366
Bank-owned life insurance	-	9,702,288	-	9,702,288
Deferred tax asset	63,916	1,682,464	-	1,746,380
SBA servicing asset	-	1,378,032	-	1,378,032
Other assets	1,027,561	1,502,451	(184,229)	2,345,783
Total Assets	$ 56,118,270	$ 512,246,897	$ (45,033,615)	$ 523,331,552
LIABILITIES				
Deposits	$ -	$ 433,195,244	$ (2,486,718)	$ 430,708,526
Federal Home Loan Bank borrowings	-	35,000,000	-	35,000,000
Subordinated debt	17,000,000	-	-	17,000,000
Note payable - related party	2,500,000	-	-	2,500,000
Accrued interest payable	214,481	180,443	-	394,924
Accrued expenses and other liabilities	127,052	1,508,542	(184,229)	1,451,365
Total Liabilities	19,841,533	469,884,229	(2,670,947)	487,054,815
Shareholders' Equity				
Common stock-voting, No par value 10,000,000 shares authorized; 3,441,882 issued and outstanding	28,271,839	37,465,527	(37,465,527)	28,271,839
Additional paid in capital	668,814	5,668,814	(5,668,814)	668,814
Retained earnings	10,925,100	2,817,343	(2,817,343)	10,925,100
Accumulated other comprehensive loss	(3,589,016)	(3,589,016)	3,589,016	(3,589,016)
Total Shareholders' Equity	36,276,737	42,362,668	(42,362,668)	36,276,737
Total Liabilities and Shareholders' Equity	$ 56,118,270	$ 512,246,897	$ (45,033,615)	$ 523,331,552

Refer to Report of Independent Registered Public Accounting Firm.

SAVI FINANCIAL CORPORATION, INC. AND SUBSIDIARY
CONSOLIDATING INCOME STATEMENT
FOR THE YEAR ENDED DECEMBER 31, 2022

	SAVI FINANCIAL	SAVI BANK	ELIMINATIONS	CONSOLIDATED BALANCES 2022
Interest income				
Interest and fees on loans	$ -	$ 18,917,262	$ -	$ 18,917,262
Interest on investment securities	105,852	806,361	-	912,213
Interest on federal funds sold and interest-bearing deposits with financial institutions	76,702	309,515	-	386,217
Total interest income	182,554	20,033,138	-	20,215,692
Interest expense				
On deposits	-	740,859	-	740,859
On borrowed funds	739,125	164,248	-	903,373
Total interest expense	739,125	905,107	-	1,644,232
Net interest income (expense)	(556,571)	19,128,031	-	18,571,460
			-	
Provision for credit losses	-	413,865	-	413,865
Net interest income (expense) after provision for credit losses	(556,571)	18,714,166	-	18,157,595
Non-interest income				
Service charges on deposit accounts	-	871,867	-	871,867
Undistributed income of subsidiary	4,585,759	-	(4,585,759)	-
Loss on sales of investment securities	-	(3,442)	-	(3,442)
Gain on sales of loans	-	4,928,326	-	4,928,326
Loss on sales of other real estate owned	-	(167,118)	-	(167,118)
Earnings on bank-owned life insurance	-	269,154	-	269,154
Other	125,000	631,045	-	756,045
Total non-interest income	4,710,759	6,529,832	(4,585,759)	6,654,832
Non-interest expense				
Salaries and employee benefits	324,481	13,246,206	-	13,570,687
Occupancy and equipment	52,828	2,316,158	-	2,368,986
Amortization of core deposit intangibles	-	114,521	-	114,521
Data processing fees	-	707,289	-	707,289
Professional fees	89,046	350,492	-	439,538
FDIC assessment	-	380,235	-	380,235
OREO expense and writedowns	-	28,345	-	28,345
Directors and officers insurance	-	113,897	-	113,897
Director fees	90,625	146,579	-	237,204
Regulatory examination fees	-	53,048	-	53,048
B & O taxes	2,247	486,709	-	488,956
Other expense	101,937	1,614,954	-	1,716,891
Total non-interest expense	661,164	19,558,433	-	20,219,597
Income before federal income tax (benefit)	3,493,024	5,685,565	(4,585,759)	4,592,830
Federal income tax (benefit)	(229,664)	1,099,806	-	870,142
Net Income	$ 3,722,688	$ 4,585,759	$ (4,585,759)	$ 3,722,688

Refer to Report of Independent Registered Public Accounting Firm.