SOUTHERN BANCSHARES (N.C.), INC.

2022 Consolidated Financial Statements

SOUTHERN BANCSHARES (N.C.), INC. AND SUBSIDIARY

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Independent Auditor's Report

Southern BancShares (N.C.), Inc.
Board of Directors
Mount Olive, NC

Opinion

We have audited the consolidated financial statements of Southern BancShares, (N.C.), Inc. and Subsidiary (the "Company"), which comprise the consolidated balance sheets as of December 31, 2022 and 2021, and the related consolidated statements of income and comprehensive (loss) 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 accompanying consolidated financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2022 and 2021, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

We have also audited in accordance with auditing standards generally accepted in the United States of America (GAAS), the Company's internal control over financial reporting as of December 31, 2022, based on the criteria established in *Internal Control—Integrated Framework (2013),* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) and our report dated March 27, 2023 expressed an unmodified opinion thereon.

Basis for Opinion

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

Responsibilities of Management for the Consolidated Financial Statements

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

In preparing the consolidated financial statements, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the Company's ability to continue as a going concern within one year after the date that these consolidated financial statements are available to be issued.

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

In performing an audit in accordance with GAAS, we:

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

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

FORVIS, LLP

Greenville, NC
March 27, 2023

SOUTHERN BANCSHARES (N.C.), INC. AND SUBSIDIARY
CONSOLIDATED BALANCE SHEETS
(Dollars in Thousands Except Share and Per Share Data)

	December 31, 2022	December 31, 2021
ASSETS		
Cash and cash equivalents:		
Cash and due from banks	$ 21,253	$ 35,106
Interest-bearing deposits with banks	115,986	138,469
Certificates of deposit with banks	2,600	11,946
Total cash and cash equivalents	139,839	185,521
Investment in marketable equity securities at fair value (cost of $26,946 and $25,973, respectively)	173,187	188,420
Investment securities available for sale, at fair value (amortized cost of $1,647,993 and $1,617,009 respectively)	1,380,120	1,613,292
Loans held for sale	2,978	15,126
Loans:		
Acquired loans	74,503	93,315
Non-acquired loans	2,775,864	2,346,234
Less allowance for loan losses:		
Acquired loans	(1,726)	(1,860)
Non-acquired loans	(34,108)	(27,449)
Net loans	2,814,533	2,410,240
Premises and equipment, net	64,211	65,524
Operating lease right of use assets	3,493	4,035
Accrued interest receivable	14,688	12,034
Stock in Federal Home Loan Bank of Atlanta	8,796	1,855
Other real estate owned	-	86
Goodwill	26,649	26,649
Intangible assets	6,693	6,425
Bank owned life insurance	29,606	28,919
Other assets	61,764	32,854
Total assets	$ 4,726,557	$4,590,980
LIABILITIES		
Deposits:		
Noninterest-bearing	$ 1,445,626	$1,386,132
Interest-bearing	2,680,356	2,533,051
Total deposits	4,125,982	3,919,183
Short-term borrowings	208,061	63,670
Long-term borrowings	88,993	88,874
Operating lease liabilities	3,704	4,231
Other liabilities	15,534	48,083
Total liabilities	4,442,274	4,124,041
SHAREHOLDERS' EQUITY		
Preferred stock	1,736	1,802
Common stock, $5 par value; 158,485 shares authorized; 78,043 and 79,357 shares issued and outstanding at December 31, 2022 and 2021, respectively	390	397
Surplus	27,043	27,043
Retained earnings	461,326	440,622
Accumulated other comprehensive loss	(206,212)	(2,925)
Total shareholders' equity	284,283	466,939
Total liabilities and shareholders' equity	$ 4,726,557	$4,590,980

See Notes to Consolidated Financial Statements

SOUTHERN BANCSHARES (N.C.), INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE (LOSS) INCOME
(Dollars in Thousands Except Share and Per Share Data)

	Year Ended December 31, 2022	2021
Interest income:		
Loans	$ 106,536	$ 100,646
Investment securities	32,263	21,945
Federal funds sold and deposits with banks	2,162	447
Total interest income	140,961	123,038
Interest expense:		
Deposits	6,563	2,263
Short-term borrowings	1,735	60
Long-term borrowings	2,881	2,796
Total interest expense	11,179	5,119
Net interest income	129,782	117,919
Provision (recovery) for loan losses	6,279	(815)
Net interest income after provision (recovery) for loan losses	123,503	118,734
Noninterest income:		
Service charges on deposit accounts	7,996	6,859
Other service charges and fees	7,767	6,261
Realized gains (losses) on investments:		
Marketable equity securities	934	-
Investment securities available for sale	(122)	514
Unrealized (losses) gains on marketable equity securities	(16,872)	54,749
Gain on sale of loans	1,554	4,931
Gain on sale of other real estate owned, net of writedowns	50	2
Investment services revenue	3,379	3,600
Other	6,730	7,933
Total noninterest income	11,416	84,849
Noninterest expense:		
Personnel	57,839	54,329
Data processing	9,752	8,344
Occupancy	7,310	7,189
Furniture and equipment	5,888	6,146
FDIC assessments	1,422	1,226
Professional fees	2,860	2,590
Amortization of intangibles and mortgage servicing rights	1,108	1,668
Other	9,298	6,942
Total noninterest expense	95,477	88,434
Income before income taxes	39,442	115,149
Income taxes	9,523	21,603
Net income	29,919	93,546
Other comprehensive income (loss):		
Unrealized losses arising during period on investment securities available for sale	(264,279)	(27,526)
Tax effect	59,746	6,239
Reclassification adjustment from investment security transactions	122	(514)
Tax effect	(28)	116
Net of tax amount	(204,439)	(21,685)
Pension obligation	380	7,564
Tax effect	(14)	(1,715)
Amortization of actuarial losses	1,021	2,149
Tax effect	(235)	(485)
Net of tax amount	1,152	7,513
Total other comprehensive loss	(203,287)	(14,172)
Comprehensive (loss) income	$ (173,368)	$ 79,374
Per share information:		
Net income available to common shareholders per common share, basic and diluted	$ 377.64	$ 1,168.54
Cash dividends declared on common shares	25.00	20.00
Weighted average common shares outstanding	78,519	79,823

See Notes to Consolidated Financial Statements

SOUTHERN BANCSHARES (N.C.), INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
(Dollars in Thousands Except Share and Per Share Data)

	Preferred Series B	Preferred Series C	Common Stock	Surplus	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Shareholders' Equity
Balance, December 31, 2020	$ 1,316	$ 489	$ 400	$ 27,043	$ 352,670	$ 11,247	$ 393,165
Net income	-	-	-	-	93,546	-	93,546
Other comprehensive loss	-	-	-	-	-	(14,172)	(14,172)
Comprehensive income	-	-	-	-	93,546	(14,172)	79,374
Purchase and retirement of stock	(3)	-	(3)	-	(3,728)	-	(3,734)
Cash dividends:							
Common stock	-	-	-	-	(1,596)	-	(1,596)
Preferred B	-	-	-	-	(237)	-	(237)
Preferred C	-	-	-	-	(33)	-	(33)
Balance, December 31, 2021	1,313	489	397	27,043	440,622	(2,925)	466,939
Net income	-	-	-	-	29,919	-	29,919
Other comprehensive loss	-	-	-	-	-	(203,287)	(203,287)
Comprehensive loss	-	-	-	-	29,919	(203,287)	(173,368)
Purchase and retirement of stock	(50)	(16)	(7)	-	(6,986)	-	(7,059)
Cash dividends:							
Common stock	-	-	-	-	(1,962)	-	(1,962)
Preferred B	-	-	-	-	(235)	-	(235)
Preferred C	-	-	-	-	(32)	-	(32)
Balance, December 31, 2022	$ 1,263	$ 473	$ 390	$ 27,043	$ 461,326	$ (206,212)	$ 284,283

See Notes to Consolidated Financial Statements

SOUTHERN BANCSHARES (N.C.), INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Dollars in Thousands Except Share and Per Share Data)

	Year Ended December 31, 2022	2021
OPERATING ACTIVITIES:		
Net income	$ 29,919	$ 93,546
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision (recovery) for loan losses	6,279	(815)
Deferred income tax (benefit) expense	(5,121)	9,384
(Loss) gain on marketable equity securities	15,938	(54,749)
Loss (gain) on sales and issuer calls of investment securities available for sale	122	(514)
Loss on disposal of premises and equipment	-	24
Gain on sale of other real estate owned, net of writedowns	(50)	(2)
Gain on sale of loans	(1,554)	(4,931)
Net amortization on investment securities available for sale	3,260	5,242
Accretion on acquired loans	(4,588)	(5,339)
Amortization of intangibles and mortgage servicing rights	1,108	1,520
Depreciation	4,385	4,892
Amortization of long-term borrowings issuance costs	119	59
Proceeds from sales of loans held for sale	398,457	222,216
Origination of loans held for sale	(384,755)	(214,310)
Amortization of operating lease right of use assets	542	970
Payments on operating lease liabilities	(527)	(691)
Net increase in intangible assets	(1,376)	(2,785)
Net change in accrued interest receivable	(2,654)	179
Net increase in cash surrender value of bank owned life insurance	(687)	(728)
Net change in other assets	36,054	(8,983)
Net change in other liabilities	(31,148)	11,765
NET CASH PROVIDED BY OPERATING ACTIVITIES	63,723	55,950
INVESTING ACTIVITIES:		
Purchases of marketable equity securities	(1,109)	(2,916)
Proceeds from sales of marketable equity securities	404	-
Proceeds from maturities, paydowns, and issuer calls of investment securities available for sale	148,132	277,017
Proceeds from sales of investment securities available for sale	131,756	41,609
Purchases of investment securities available for sale	(314,254)	(989,873)
Net increase in loans	(406,300)	(134,712)
Net (increase) decrease in FHLB stock	(6,941)	778
Purchases of premises and equipment	(3,612)	(7,397)
Proceeds from sale of premises and equipment	165	391
Proceeds from the sale of other real estate owned	452	463
NET CASH USED BY INVESTING ACTIVITIES	(451,307)	(814,640)
FINANCING ACTIVITIES:		
Net increase in noninterest-bearing demand deposits	59,494	207,396
Net increase in interest-bearing deposits	147,305	395,987
Net increase in short-term borrowed funds	144,391	8,407
Proceeds from issuance of long-term debt	-	88,815
Payments on junior subordinated debentures	-	(23,711)
Cash dividends paid	(2,229)	(1,866)
Purchase and retirement of stock	(7,059)	(3,734)
NET CASH PROVIDED BY FINANCING ACTIVITIES	341,902	671,294
NET DECREASE IN CASH AND CASH EQUIVALENTS	(45,682)	(87,396)
CASH AND CASH EQUIVALENTS AT THE BEGINNING OF YEAR	185,521	272,917
CASH AND CASH EQUIVALENTS AT THE END OF YEAR	$ 139,839	$ 185,521

See Notes to Consolidated Financial Statements

SOUTHERN BANCSHARES (N.C.), INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS (Continued)
(Dollars in Thousands Except Share and Per Share Data)

	Year Ended December 31,	
	2022	2021
SUPPLEMENTAL DISCLOSURES OF CASH PAID DURING THE YEAR FOR:		
Interest	$ 11,735	$ 4,976
Income taxes	11,511	12,705
SUPPLEMENTAL DISCLOSURES OF NONCASH FINANCING AND INVESTING ACTIVITIES:		
Unrealized losses on available-for-sale securities, net of tax	$ (203,653)	$ (21,685)
Investment securities transferred to other assets	-	1,802
Change in pension obligation, net of tax	366	7,513
Non-acquired foreclosed loans transferred to other real estate	316	105
Premises and equipment transferred to other assets	375	-
Recognition of new and modified operating lease right of use assets	(227)	(714)

See Notes to Consolidated Financial Statements

Note 1. Nature of Operations and Summary of Significant Accounting Policies

BancShares

Southern BancShares (N.C.), Inc. ("BancShares") is the holding company for Southern Bank and Trust Company ("Southern"), which operates 47 banking offices in eastern North Carolina and 10 banking offices in southeastern Virginia. In addition to the full-service banking offices, Southern also maintains a loan production office in North Carolina and a loan production office in Virginia.

Southern, which began operations January 29, 1901, has a wholly-owned subsidiary, Goshen, Inc., whose primary operations include holding certain investments. Southern also has a wholly owned subsidiary, Tuscarora Properties, LLC, that was created to hold, manage and ultimately dispose of select other real estate owned ("OREO") properties. BancShares and Southern are headquartered in Mount Olive, North Carolina.

BancShares has no foreign operations and BancShares' customers are principally located in eastern North Carolina and southeastern Virginia.

BancShares and Southern are subject to extensive federal and state banking laws and regulations. These laws and regulations focus on the protection of depositors, federal deposit insurance funds, and the banking system as a whole rather than the protection of security holders. Federal and state banking regulators possess broad powers to take supervisory actions as they deem appropriate. These supervisory actions may result in higher capital requirements, higher insurance premiums, increased expenses, reductions in fee income and limitations on activities that could have a materially adverse effect on our results of operations.

Principles of Consolidation

The consolidated financial statements include the accounts of BancShares and other entities in which BancShares has a controlling interest. All significant intercompany balances have been eliminated in consolidation.

Basis of Financial Statement Presentation

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 liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. The most significant estimates made by BancShares in the preparation of its consolidated financial statements are:

- Investment security valuation
- Determination of the allowance for loan losses
- Goodwill impairment
- Pension plan assumptions
- Mortgage servicing rights
- Income taxes

Cash and Cash Equivalents

For purposes of reporting cash flows, cash and cash equivalents include cash and due from banks, interest-bearing deposits with banks, and certificates of deposit with banks. Overnight and federal funds are purchased and sold for one day periods.

Note 1. Nature of Operations and Summary of Significant Accounting Policies (Continued)

Marketable Equity Securities

Equity securities are recorded on a trade date basis and measured at fair value with all changes recorded through income. Realized and unrealized gains and losses are determined by specific identification and are included in Noninterest income. Non-marketable equity securities are securities that do not have readily determinable fair values and are measured at cost. Equity securities with no recurring market value data available are reviewed periodically and any observable market value changes are adjusted through noninterest income. BancShares evaluates its non-marketable equity securities for impairment and recoverability of the recorded investment by considering positive and negative evidence, including the profitability and asset quality of the issuer, dividend payment history and recent redemption experience. Impairment is assessed at each reporting period and if identified, is recognized in Noninterest income.

For equity investments without a readily determinable fair value, BancShares has elected to measure the equity investments using the measurement alternative, which requires BancShares to make a qualitative assessment of whether the investment is impaired at each reporting period. Under the measurement alternative, these investments will be measured at cost, less any impairment, plus or minus changes resulting from observable price changes in orderly transactions for an identical or similar investment of the same issuer. If a qualitative assessment indicates that the investment is impaired, BancShares will estimate the investment's fair value in accordance with Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") Topic ASC 820, *Fair Value Measurements and Disclosure* and, if the fair value is less than the investment's carrying value, recognize an impairment loss in net income equal to the difference between carrying value and fair value. Equity investments without a readily determinable fair value totaling $4.0 million at December 31, 2022 and 2021, respectively are recorded within other assets in the Consolidated Balance Sheets.

Investment Securities Available for Sale

BancShares classifies debt securities as available for sale and they are reported at estimated fair value, with unrealized gains and losses, net of income taxes, reported in accumulated other comprehensive income (loss) (“AOCI”). Amortization of premiums and accretion of discounts for debt securities are included in interest income. Realized gains and losses from the sale of debt securities are determined by specific identification on a trade date basis and are included in noninterest income. BancShares evaluates each available for sale security in a loss position for other-than-temporary impairment (“OTTI”) at least quarterly. BancShares considers such factors as the length of time and the extent to which the market value has been below amortized cost, long-term expectations and recent experience regarding principal and interest payments, BancShares' intent to sell, and whether it is more likely than not that it would be required to sell those securities before the anticipated recovery of the amortized cost. The credit component of an OTTI loss is recognized in noninterest income and the non-credit component is recognized in AOCI in situations where BancShares does not intend to sell the security, and it is more likely than not that BancShares will not be required to sell the security prior to recovery.

Loans Held for Sale

Loans originated and intended for sale in the secondary market are carried at the lower of cost or estimated fair value in the aggregate. Estimated fair value is determined on the basis of existing forward commitments or the current market value of similar loans. Net unrealized losses, if any, are recognized through a valuation allowance by charges to Noninterest income. Prior to closing loans intended for sale in the secondary market, an interest rate lock commitment is entered into with the borrower. The interest rate lock is considered a derivative for Southern, whose estimated fair value is determined by current market rates for similar loans. Loans held-for-sale are normally sold to investors as part of a “mandatory” delivery program for mortgage loans. Under the mandatory delivery system, loans with interest rate locks are paired with the sale of a “to be announced” (“TBA”) mortgage-backed security bearing similar attributes. Under the mandatory delivery program, we commit to deliver loans to an investor at an agreed upon price prior to the close of such loans. Loans held-for-sale may also be sold to investors with the best efforts intent and ability to sell the loans as long as they meet the underwriting standards of the potential investor. A “best efforts” delivery sets the sale price with the investor on a loan-by-loan basis when each loan is locked. At December 31, 2022 and 2021, the estimated fair value of mortgage related derivatives was determined to be immaterial.

Note 1. Nature of Operations and Summary of Significant Accounting Policies (Continued)

Loans

Non-acquired loans that are held for investment purposes are carried at the principal amount outstanding reduced by unearned income and an allowance for loan losses.

Southern accounts for its acquisitions under FASB ASC Topic 805, *Business Combinations*, which requires the use of the acquisition method of accounting. All identifiable assets acquired, including loans, are recorded at fair value. No allowance for loan losses ("ALLL") related to acquired loans is recorded on the acquisition date because the fair value of the loans acquired incorporates assumptions regarding credit risk. Loans acquired are recorded at fair value in accordance with the fair value methodology prescribed in FASB ASC Topic 820. The fair value estimates associated with the loans include estimates related to expected prepayments and the amount and timing of expected principal, interest and other cash flows.

Acquired loans with evidence of credit deterioration since origination and for which it is probable that all contractually required payments will not be collected are considered to be credit-impaired. Evidence of credit quality deterioration as of the acquisition date may include information such as past due and nonaccrual status, borrower credit scores and recent loan to value percentages. Acquired credit-impaired loans are accounted for under the accounting guidance for loans and debt securities acquired with deteriorated credit quality, found in FASB ASC Topic 310-30, *Receivables—Loans and Debt Securities Acquired with Deteriorated Credit Quality*, and initially measured at fair value, which includes estimated future credit losses expected to be incurred over the life of the loans. Acquired credit-impaired loans accounted for in accordance with FASB ASC Topic 310-30 are recorded net of a nonaccretable difference and, if appropriate, an accretable yield. The difference between contractually required payments at acquisition and the cash flows expected to be collected at acquisition is the nonaccretable difference, which is included as a reduction to the carrying amount of acquired FASB ASC Topic 310-30 loans. Any excess of cash flows expected at acquisition over the estimated fair value is referred to as the accretable yield and is recognized in Interest income over the remaining life of the loan when there is a reasonable expectation regarding the amount and timing of such cash flows. In accordance with FASB ASC Topic 310-30, Southern has aggregated substantially all acquired credit-impaired loans that have common risk characteristics into pools and is accounting for these loans on a pool level basis. Certain large or non-homogeneous acquired credit-impaired loans are accounted for on an individual loan basis.

Cash flow analyses are performed on acquired FASB ASC Topic 310-30 loans in order to determine the cash flows expected to be collected. Subsequent decreases to expected cash flows will generally result in recognition of an allowance by a charge to provision for loan losses. Subsequent increases in expected cash flows result in either a reversal of the provision for loan losses to the extent of prior charges, or a reclassification of the difference from nonaccretable to accretable with a positive impact on the accretable yield.

Acquired loans that do not meet the specific criteria of FASB ASC Topic 310-30, but for which a discount is attributable at least in part to credit quality are generally accounted for under this guidance. As a result, related discounts are recognized subsequently through accretion based on the expected cash flow of the acquired loans. Certain acquired loans, such as lines of credit (consumer and commercial) and loans with no significant credit related discount are accounted for in accordance with FASB ASC Topic 310-20, where the discount is accreted through earnings based on contractual cash flows over the estimated life of the loan.

Interest income on non-acquired loans is recognized in a manner that approximates the level yield method when related to the principal amount outstanding. Accrual of interest is discontinued on a loan when management believes the borrower's financial condition is such that collection of principal or interest is doubtful. Loans are returned to the accrual status when the factors indicating doubtful collectability cease to exist and the loan has performed in accordance with its terms for a demonstrated period of time. Acquired credit-impaired loans that are accounted for in accordance with FASB ASC Topic 310-30, as well as acquired non-credit-impaired loans accounted for under FASB ASC Topic 310-20 are accruing interest under the accretion method and are thus not reported as nonaccrual. The past due status of loans is based on the contractual terms of the loan.

Note 1. Nature of Operations and Summary of Significant Accounting Policies (Continued)

Loans (Continued)

Management considers a non-acquired loan or an acquired loan accounted for in accordance with FASB ASC Topic 310-20 to be impaired when, based on current information or events, it is probable that a borrower will be unable to pay all amounts due according to the contractual terms of the loan agreement. Impaired loans are valued using either the discounted expected cash flow method or the collateral value. When the ultimate collectability of the non-acquired impaired loan's principal is doubtful, all cash receipts are applied to principal. Once the recorded principal balance has been reduced to zero, future cash receipts are applied to Interest income, to the extent that any interest has been foregone. Future cash receipts are recorded as recoveries of any amounts previously charged-off.

Southern provides an ALLL on non-acquired loans and acquired loans accounted for in accordance with FASB ASC Topic 310-20 on a reserve basis and includes in operating expenses a provision for loan losses determined by management. The allowance is reduced by charge-offs and increased by subsequent recoveries. Management's periodic evaluation of the adequacy of the allowance is based on Southern's past loan loss experience, known and inherent risks in the portfolio, adverse situations that may affect borrowers' experience, the estimated value of any underlying collateral, current economic conditions and other risk factors. Management believes it has established the allowance in accordance with accounting principles generally accepted in the United States of America and in consideration of the current economic environment. While management uses the best information available to make evaluations, future adjustments may be necessary.

The evaluation of the adequacy of the ALLL includes both loans evaluated collectively for impairment and loans evaluated individually for impairment. Impaired loans with a balance less than $100,000 are not evaluated individually for impairment, unless the loan is not performing and unsecured, or if the condition of the collateral has significantly deteriorated since the collateral was last appraised. For loans evaluated collectively for impairment, loans are grouped based on common risk characteristics which include call report code and risk grade. Call report codes segregate loans based on loan type and collateral type and helps to provide consistent reporting across accounting principles generally accepted in the United States ("GAAP") and regulatory reports. Historical loss rates are calculated based on the historical probability of default ("PD") and loss given default ("LGD") for each loan grouping. PDs represent the likelihood that a loan will default within a one year period of time, and LGDs represent the estimated magnitude of loss Southern will incur if a loan defaults. A loan is considered to be in default if it becomes 90 days or more past due, meets the criteria for nonaccrual status, or incurs a charge-off. Historical loss rates are developed with five years of trailing default and loss data. These historical loss rates are then combined with certain qualitative factors to determine the ALLL reserve rates for each loan grouping. Qualitative factors include consideration of certain internal and external factors, such as loan delinquency levels and trends, loan growth, loan portfolio composition and concentrations, local and national economic conditions, the loan review function, and other factors management deems relevant to the ALLL calculation.

In addition, various regulatory agencies, as an integral part of their examination process, periodically review Southern's allowance for loan losses and actual losses on OREO. Such agencies may require Southern to recognize adjustments to the allowance based on the examiners' judgments about information available to them at the time of their examinations.

Troubled Debt Restructurings ("TDRs")

Southern designates loan modifications as TDRs when, for economic or legal reasons related to the borrower's financial difficulties, it grants a concession to the borrower that it would not otherwise consider. Loans on nonaccrual status at the date of modification are initially classified as nonaccrual TDRs. Loans on accruing status at the date of modification are initially classified as accruing TDRs at the date of modification, if the note is reasonably assured of repayment and performance is in accordance with its modified terms. Such loans may be designated as nonaccrual loans subsequent to the modification date if reasonable doubt exists as to the collection of interest or principal under the restructuring agreement. Nonaccrual TDRs are returned to accruing status when there is economic substance to the restructuring, there is well documented credit evaluation of the borrower's financial condition, the remaining balance is reasonably assured of repayment in accordance with its modified terms, and the borrower has demonstrated sustained repayment performance in accordance with the modified terms for a reasonable period of time (generally a minimum of six months).

Note 1. Nature of Operations and Summary of Significant Accounting Policies (Continued)

Premises and Equipment

Premises and equipment are stated at cost less accumulated depreciation and amortization. Depreciation and amortization are computed using the straight-line method over the estimated lives of the assets, ranging from 15 to 39 years for buildings and improvements and 3 to 9 years for furniture and equipment.

Leases

Southern leases certain office facilities and office equipment under operating leases. Southern also subleases certain office facilities and owns certain office facilities that are leased to outside parties; however, such leases are not significant. For operating leases other than those considered to be short-term, Southern recognizes operating lease right of use assets and related operating lease liabilities which are reported in the consolidated balance sheets. Southern does not recognize short-term operating leases in the consolidated balance sheets. A lease is considered short-term if it has an original term of 12 months or less and does not have a purchase option that is likely to be exercised.

In recognizing operating lease right of use assets and related operating lease liabilities, Southern has elected the practical expedient that allows for lease and non-lease components to be accounted for as a single lease component. Lease payments over the expected term are discounted using Southern's incremental borrowing rate referenced to the Federal Home Loan Bank Secure Connect advance rates for borrowings of similar term. Management also considers renewal and termination options in the determination of the expected term of each lease. If it is reasonably certain that a renewal or termination option will be exercised, the effects of such options are included in the determination of the expected lease term. Most leases include one or more renewal options. At December 31, 2022 and 2021, leases for office facilities have terms, including renewal options that Management is reasonably certain will be exercised, that extend up to 10 years. Southern's leases do not contain material residual value guarantees or material restrictive covenants.

Stock in Federal Home Loan Bank of Atlanta

Stock in Federal Home Loan Bank of Atlanta ("FHLB") is acquired for regulatory purposes. This security does not have a readily determinable fair value because its ownership is restricted and lacks a market for trading. As a result, this security is carried at cost and is periodically evaluated for impairment.

OREO

OREO acquired through, or in lieu of, foreclosure is held for sale and is stated at estimated fair market value of the property, less estimated disposal costs at time of foreclosure then lower of cost or net realizable value throughout the remaining life. At least annually, current valuations in the form of internal or external appraisals are obtained for all OREO and carrying values are adjusted, if required, with a charge to current expenses for adjustments to reflect the current appraised values less the estimated cost to sell.

BancShares estimates fair value at the asset's fair market value less disposal costs using management's assumptions, which are based on current market trends and historical losses for similar assets. Any excess of cost over the estimated fair market value at the time of foreclosure is charged to the allowance for loan losses.

Goodwill and Intangible Assets

Intangible assets are composed of goodwill, core deposit premiums and mortgage servicing rights ("MSRs"). Core deposit premiums are generally amortized on an accelerated basis over a period of 5 to 10 years and the useful lives are periodically reviewed for reasonableness.

MSRs represent the estimated value of the right to service mortgage loans for others. Capitalization of MSRs occurs when the underlying loans are sold with servicing retained by Southern. Capitalized MSRs are amortized into income over the projected servicing life of the underlying loans.

(Dollars in Thousands for Tabular Presentations)

Note 1. Nature of Operations and Summary of Significant Accounting Policies (Continued)

Goodwill and Intangible Assets (continued)

As of December 31, 2022, BancShares had goodwill and intangible assets totaling $33.3 million. Management evaluated BancShares' existing intangible assets and goodwill for impairment as of September 30, 2022. Amortization expense associated with intangible assets was $1.1 million and $1.5 million for the years ended December 31, 2022 and 2021, respectively.

Goodwill arising from acquisitions is not amortized but is reviewed for potential impairment at least annually or if events or circumstances indicate a potential impairment. BancShares concluded that goodwill was not impaired as of December 31, 2022; however, future events impacting financial institutions could negatively impact BancShares' goodwill asset in the future.

The following is a summary of the gross carrying amounts, accumulated amortization and net carrying amounts of amortized intangible assets and the gross carrying amount of unamortized intangible assets as of December 31, 2022 and December 31, 2021:

	December 31, 2022		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Amortized intangible assets:			
Core deposits intangibles	$ 23,528	$ 23,528	$ -
Mortgage servicing rights	17,813	11,120	6,693
Total	$ 41,341	$ 34,648	$ 6,693
Unamortized intangible assets:			
Goodwill	$ 26,649		

	December 31, 2021		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Amortized intangible assets:			
Core deposits intangibles	$ 23,528	$ 23,520	$ 8
Mortgage servicing rights	16,437	10,020	6,417
Total	$ 39,965	$ 33,540	$ 6,425
Unamortized intangible assets:			
Goodwill	$ 26,649		

At December 31, 2022, the scheduled amortization expense for intangible assets is as follows:

2023	$ 327
2024	320
2025	283
2026	233
2027	199
Thereafter	5,331
Total	$ 6,693

The actual amortization expense in future periods may be subject to change based on changes in the useful life of the assets, expectations for loan prepayments, future acquisitions and future loan sales.

Bank-Owned Life Insurance

Southern has purchased life insurance policies on certain current and past key employees and directors where the insurance policy benefits and ownership are retained by the employer. These policies are recorded at their cash surrender value. Income from these policies and changes in the net cash surrender value are recorded in Noninterest income as earnings on bank-owned life insurance. The cash value accumulation is permanently tax deferred if the policy is held to the insured person's death and certain other conditions are met.

(Dollars in Thousands for Tabular Presentations)

Note 1. Nature of Operations and Summary of Significant Accounting Policies (Continued)

Income Taxes

BancShares uses the asset and liability method to account for deferred income taxes. The objective of the asset and liability method is to establish deferred tax assets and liabilities for the temporary differences between the financial reporting basis and the income tax basis of BancShares' assets and liabilities at enacted rates expected to be in effect when such amounts are realized or settled.

Recognition of deferred tax assets is based on management's belief that it is "more likely than not" that the tax benefit associated with certain temporary differences will be realized. A valuation allowance is recorded for deferred tax assets when the "more likely than not" standard is not met.

Shareholders' Equity

Common shareholders are entitled to one vote per share and preferred series B and C shareholders are entitled to one vote for each 38 shares owned of a class. Dividends on BancShares' common stock may be paid only after annual dividends of $.90 per share on both preferred series B and C shares have been paid. Share activity and other information for each of the preferred and common stock issues is presented below:

	Non-cumulative Preferred Series B	Non-cumulative Preferred Series C	Common
December 31, 2020	263,219	36,867	80,085
Purchase and retirement	(520)	-	(728)
December 31, 2021	262,699	36,867	79,357
Purchase and retirement	(10,047)	(1,210)	(1,314)
December 31, 2022	252,652	35,657	78,043
Shares authorized	408,728	43,631	158,485
Par value	None	None	$ 5.00
Liquidation value			
December 31, 2021	$ 2,627	$ 369	N/A
December 31, 2022	$ 2,527	$ 357	N/A

Although there were no shares outstanding or activity in any period presented, there were 500,000 shares of $0.01 par value preferred stock authorized as of December 31, 2022.

Earnings per common share are computed by dividing income applicable to common shares by the weighted average number of common shares outstanding during the period. Income applicable to common shares represents net income reduced by dividends paid to preferred shareholders. BancShares has no potentially dilutive securities.

Earnings per common share are calculated based on the following amounts for the years ended December 31:

	2022	2021
Net income	$ 29,919	$ 93,546
Less preferred dividends	(267)	(270)
Net income applicable to common shares	$ 29,652	$ 93,276
Weighted average common shares outstanding during the period	78,519	79,823

On January 18, 2022, BancShares' board of directors approved a stock repurchase program that expires on March 31, 2023, and authorizes the repurchase of up to 4,000 shares of common stock. The repurchase program stipulates that the aggregate dollar amount paid during any consecutive twelve-month period to repurchase shares of common and preferred stock may not equal or exceed three percent of consolidated shareholders' equity. As of December 31, 2022, BancShares had spent $7.1 million to repurchase shares of common and preferred stock pursuant to the repurchase program. The aggregate repurchase limit under the repurchase program is $8.5 million as of December 31, 2022.

Note 1. Nature of Operations and Summary of Significant Accounting Policies (Continued)

Comprehensive (Loss) Income

Comprehensive (loss) income is defined as the change in equity during a period for non-owner transactions and includes net income and other comprehensive (loss) income. Other comprehensive (loss) income includes revenues, expenses, gains, and losses that are excluded from earnings under current accounting standards. Components of other comprehensive (loss) income for BancShares consist of the unrealized gains and losses, net of taxes, in BancShares' available-for-sale securities portfolio and changes in the defined benefit pension plan obligation.

Revenue Recognition

BancShares generally acts in a principal capacity, on its own behalf, in its contracts with customers. In these transactions, BancShares recognizes revenues and the related costs to generate those revenues on a gross basis. In certain circumstances BancShares acts in an agent capacity on behalf of the customers with other entities and recognize revenues and the related costs to provide BancShares' services on a net basis. Business lines where BancShares acts as an agent include interchange and debit card income, merchant services and check sales. Descriptions of BancShares' noninterest revenue-generating activities are broadly segregated as follows:

Service Charges on deposit accounts - These deposit account-related fees represent monthly account maintenance and transaction-based service fees such as overdraft fees, stop payment fees and charges for issuing cashier's checks and money orders. For account maintenance services, revenue is recognized at the end of the statement period when BancShares' performance obligation has been satisfied. All other revenues from transaction-based services are recognized at a point in time when the performance obligation has been completed.

Other service charges and fees - These include, but are not limited to, check cashing fees, internet banking fees, wire transfer fees and safe deposit fees. The performance obligation is fulfilled, and revenue is recognized, at the point in time the requested service is provided to the customer.

Interchange and debit card revenue - These represent interchange fees, included in Other service charges and fees, from customer debit and credit card transactions that are earned at the time a cardholder engages in a transaction with a merchant. Revenue is recognized when the performance obligation has been satisfied, which is upon completion of the card transaction. Additionally, costs associated with interchange and debit card revenue are netted against the fee income from such transactions.

Sales of OREO - OREO property consists of foreclosed real estate used as collateral for loans. Revenue is generally recognized on the date of sale where the performance obligation of providing access and transferring control of the specified OREO property to the buyer in good faith and good title is satisfied.

Investment Services - These primarily represent annuity fees, sales commissions, management fees, insurance sales, and advisory fees. The performance obligation for investment services is the provision of services to place annuity products issued by the counterparty to investors, and the provision of services to manage the client's assets, including brokerage custodial and other management services. Revenue from investment services is recognized over the period in which services are performed, and is based on a percentage of the value of the assets under management/administration. This revenue is either fixed or variable based on account type, or transaction-based.

Merchant services- These represent fees charged to merchants, included in Other noninterest income, for providing them the ability to accept and process debit and credit card transactions. Revenue is recognized when the performance obligation has been satisfied, which is upon completion of the card transaction. Costs associated with merchant services transactions are netted against the fee income from such transactions.

Check sales – These represent the fees, included in Other noninterest income, charged for checks sold to customers. A contract has been established with a third party vendor to provide the checks to the customer. Southern receives a commission based upon contractual terms with the third party vendor and the volume of sales that occur over a period of time. Revenue is recognized when the performance obligation has been satisfied, which is upon completion of the sale of the checks. Additionally, costs associated check sales transactions are netted against the fee income from such transactions.

Note 1. Nature of Operations and Summary of Significant Accounting Policies (Continued)

Other - This consists of several forms of recurring revenue such as dividends on equity investments without a readily determinable fair value, FHLB dividends, and income earned on changes in the cash surrender value of bank-owned life insurance, all of which are outside the scope of FASB ASC Topic 606, *Revenue from Contracts with Customers*. The remaining miscellaneous income is the result of immaterial transactions where revenue is recognized when, or as, the performance obligation is satisfied.

Recent Accounting Pronouncements

The following is a summary of recent authoritative pronouncements that could impact the accounting, reporting, and/or disclosure of financial information by BancShares.

ASU 2016-13, "Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments." ASU 2016-13 requires the measurement of all expected credit losses for financial assets held at the reporting date based on historical experience, current conditions, and reasonable and supportable forecasts and requires enhanced disclosures related to the significant estimates and judgments used in estimating credit losses, as well as the credit quality and underwriting standards of an organization's portfolio. ASU 2016-13, as subsequently updated for certain clarifications, targeted relief and codification improvements, is effective for BancShares as of January 1, 2023.

ASU 2020-04, "Reference Rate Reform (Topic 848): Facilitation of the Effects of Reference Rate Reform on Financial Reporting." ASU 2020-04 provides optional expedients and exceptions for accounting related to contracts, hedging relationships and other transactions affected by reference rate reform if certain criteria are met. ASU 2020-04 applies only to contracts, hedging relationships, and other transactions that reference LIBOR or another reference rate expected to be discontinued because of reference rate reform and do not apply to contract modifications made and hedging relationships entered into or evaluated after December 31, 2022. During December 2022, the FASB issued *ASU 2022-06,* which deferred the sunset date from December 31, 2022, to December 31, 2024.

ASU 2022-02, "Financial Instruments – Credit Losses (Topic 326) – Troubled Debt Restructurings and Vintage Disclosures." ASU 2022-02 eliminates the prior recognition and measurement guidance for troubled debt restructurings and establishes new disclosures for loan modifications arising from a borrower experiencing financial difficulties. ASU 2022-02 also requires disclosures of current period gross charge-offs by year of origination. BancShares adopted the provisions of ASU 2022-02, concurrent with the effectiveness of ASU 2013-06, as of January 1, 2023.

From time to time, the FASB issues exposure drafts for proposed statements of financial accounting standards. Such exposure drafts are subject to comment from the public, to revisions by the FASB and to final issuance by the FASB as statements of financial accounting standards. Management considers the effect of the proposed statements in the consolidated financial statements of BancShares and monitors the status of changes to and proposed effective dates of exposure drafts.

(Dollars in Thousands for Tabular Presentations)

Note 2. Investment Securities

The amortized cost and estimated fair values of investment securities at December 31 were as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
December 31, 2022				
Investments in marketable equity securities	$ 26,946	$ 146,241	$ -	$ 173,187
Investment securities available for sale:				
U.S. Treasuries and government-sponsored entities debt*	$ 354,284	$ -	$ (55,286)	$ 298,998
Corporate debt securities	11,397	-	(505)	10,892
Obligations of states and political subdivisions	251,700	12	(48,112)	203,600
Government-sponsored mortgage-backed securities	1,030,612	-	(163,982)	866,630
Total investment securities available for sale	$ 1,647,993	$ 12	$ (267,885)	$ 1,380,120
December 31, 2021				
Investments in marketable equity securities	$ 25,973	$ 162,447	$ -	$ 188,420
Investment securities available for sale:				
U.S. Treasuries and government-sponsored entities debt*	$ 467,878	$ 257	$ (9,918)	$ 458,217
Corporate debt securities	11,396	192	(11)	11,577
Obligations of states and political subdivisions	275,161	10,123	(451)	284,833
Government-sponsored mortgage-backed securities	862,574	5,266	(9,175)	858,665
Total investment securities available for sale	$ 1,617,009	$ 15,838	$ (19,555)	$ 1,613,292

*Government-sponsored entities debt consists of debt securities offered by Federal Home Loan Mortgage Corporation, Federal National Mortgage Corporation, Federal Home Loan Bank, Small Business Administration ("SBA") and Federal Farm Credit Banks.

(Dollars in Thousands for Tabular Presentations)

Note 2. Investment Securities (Continued)

Investment securities available for sale with a carrying value of $697.3 million and $92.6 million were pledged at December 31, 2022 to secure public deposits and short-term borrowings, respectively.

Included in the following tables are all investments with unrealized loss positions. At December 31, 2022 and 2021, there were no securities with unrealized losses for which other-than-temporary impairment has been recognized.

Temporarily impaired securities at December 31 were as follows:

	Less Than 12 Months		12 Months or Longer		Total	
	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value
December 31, 2022						
U.S. Treasuries and government-sponsored entities debt	$ 9,299	$ 97,145	$ 45,987	$ 226,652	$ 55,286	$ 323,797
Corporate debt securities	440	7,460	65	435	505	7,895
Obligations of states and political subdivisions	34,619	163,186	13,493	39,386	48,112	202,572
Government-sponsored mortgage-backed securities	54,043	338,946	109,939	502,886	163,982	841,832
Total temporarily impaired securities	$ 98,401	$ 606,737	$ 169,484	$ 769,359	$ 267,885	$ 1,376,096
December 31, 2021						
U.S. Treasuries and government-sponsored entities debt	$ 6,832	$ 292,379	$ 3,086	$ 89,172	$ 9,918	$ 381,551
Corporate debt securities	11	489	-	-	11	489
Obligations of states and political subdivisions	431	50,295	20	2,325	451	52,620
Government-sponsored mortgage-backed securities	8,796	560,291	379	7,031	9,175	567,322
Total temporarily impaired securities	$ 16,070	$ 903,454	$ 3,485	$ 98,528	$ 19,555	$ 1,001,982

(Dollars in Thousands for Tabular Presentations)

Note 2. Investment Securities (Continued)

The above securities' losses were considered temporary losses at December 31, 2022 principally resulting from the increase in market interest rates since the securities were purchased. The following numbers of securities were in an unrealized loss position at:

	December 31, 2022	December 31, 2021
U.S. Treasuries and government-sponsored entities debt	60	42
Corporate debt securities	2	1
Obligations of states and political subdivision	279	64
Government-sponsored mortgage-backed securities	161	78
Total temporarily impaired securities	502	185

The unrealized losses are not likely to reverse unless and until market interest rates decline to the levels that existed when the securities were purchased or until the security matures or is called by the issuer. Since none of the unrealized losses relate to the marketability of the securities or the issuer's ability to honor redemption obligations, none of the securities are deemed to be other than temporarily impaired. As of December 31, 2022, there was no intent to sell any of the securities classified as available-for-sale. Furthermore, it is not likely that BancShares will have to sell any such securities before a recovery of the carrying value.

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 issuers may have the right to call or prepay obligations with or without call or prepayment penalties. Repayments of the government-sponsored mortgage-backed securities are dependent on the repayments of the underlying loan balances.

	Amortized Cost	Fair Value
Securities available-for-sale:		
U.S. Treasuries and government-sponsored entities debt		
Due after one year through five years	$ 45,272	$ 39,378
Due after five years through ten years	162,683	137,304
Due after ten years	146,329	122,316
	354,284	298,998
Corporate debt securities		
Due after one year through five years	2,997	2,997
Due after five years through ten years	8,400	7,895
	11,397	10,892
Obligations of states and political subdivisions		
Due after five years through ten years	6,592	6,003
Due after ten years	245,108	197,597
	251,700	203,600
Government-sponsored mortgage-backed securities	1,030,612	866,630
Total	$ 1,647,993	$ 1,380,120

Sales and issuer calls of securities available-for-sale having a cost basis of $52.9 million and $41.1 million in 2022 and 2021, respectively, resulted in gross realized gains of $683,000 and $514,000 for 2022 and 2021, respectively. The proceeds from such sales and issuer calls were $53.6 million and $41.6 million for the years ended December 31, 2022 and 2021, respectively. Sales and issuer calls of securities available-for-sale having a cost basis of $80.7 million resulted in gross realized losses of $805,000 in 2022. The proceeds from such sales and issuer calls were $78.2 million for the year ended December 31, 2022.

(Dollars in Thousands for Tabular Presentations)

Note 3. Loans and Allowance for Loan Losses

The following is a summary of non-acquired loans:

	December 31, 2022	December 31, 2021
Commercial:		
Construction and land development	$ 172,733	$ 110,373
Agricultural	233,233	221,896
Commercial mortgage	1,152,367	988,172
Commercial and industrial	218,068	204,240
Paycheck Protection Program	631	42,861
Other	32,685	28,829
Non-commercial:		
Residential mortgage	716,210	519,277
Revolving mortgage (HELOCS)	180,486	148,370
Construction and land development	45,846	56,403
Consumer	23,274	25,541
Demand overdrafts	331	272
Total non-acquired loans	$ 2,775,864	$ 2,346,234
Loans held for sale (excluded from total loans)	$ 2,978	$ 15,126
Loans serviced for others (excluded from total loans)	698,464	684,452

Net deferred fees included within the respective balances for each loan type presented above total $3.3 million and $2.9 million at December 31, 2022 and 2021, respectively.

Total loans to directors, executive officers and related individuals and organizations were $392,000 and $427,000 at December 31, 2022 and 2021, respectively. During 2022, there were $187,000 of advances of these loans made to this group and repayments totaling $222,000. There were no restructured or nonaccrual loans to directors, executive officers or related individuals and organizations. All extensions of credit to such persons have been made in the ordinary course of business.

Each portfolio segment and the classes within those segments are subject to risks that could have an adverse impact on the credit quality of the loan and lease portfolio. Management has identified the most significant risks as described below which are generally similar among the segments and classes. While the list is not exhaustive, it provides a description of the risks that management has determined are the most significant.

Commercial loans
Each commercial loan or lease is underwritten based primarily upon the customer's ability to generate the required cash flow to service the debt in accordance with the contractual terms and conditions of the loan agreement. A complete understanding of the borrower's businesses including the experience and background of the principals is obtained prior to approval. To the extent that the loan or lease is secured by collateral, which is true for the majority of commercial loans, the likely value of the collateral and what level of strength the collateral brings to the transaction is evaluated. To the extent that the principals or other parties provide personal guarantees, the relative financial strength and liquidity of each guarantor is assessed. Common risks to each class of commercial loans include general economic conditions within the markets BancShares serves, as well as risks that are specific to each transaction including demand for products and services, personal events such as disability or change in marital status, and reductions in the value of collateral.

Note 3. Loans and Allowance for Loan Losses (Continued)

In addition to these common risks for the majority of commercial loans, additional risks are inherent in certain classes of commercial loans, as follows:

Construction and land development
Construction and land development loans are highly dependent on the supply and demand for commercial real estate in the markets served by BancShares as well as the demand for newly constructed residential homes and lots that customers are developing. Continuing deterioration in demand could result in significant decreases in the underlying collateral values and make repayment of the outstanding loans more difficult for customers.

Agricultural, commercial mortgage, and commercial and industrial
Agricultural, commercial mortgage, and commercial and industrial loans are primarily dependent on the ability of borrowers to achieve business results consistent with those projected at loan origination resulting in cash flow sufficient to service the debt. To the extent that a customer's business results are significantly unfavorable versus the original projections, the ability for the loan to be serviced on a basis consistent with the contractual terms may be at risk. The performance of agricultural loans is highly dependent on favorable weather, reasonable costs for seed and fertilizer, and the ability to successfully market the product at a profitable margin. The demand for these products is also dependent on macroeconomic conditions that are beyond the control of the borrower. While these loans are generally secured by real property, personal property, or business assets such as inventory or accounts receivable, it is possible that the liquidation of the collateral will not fully satisfy the obligation.

Paycheck Protection Program ("PPP")
PPP loans include loans to businesses and other entities that would otherwise be reported as commercial and industrial loans originated under guidelines discussed above. PPP loans totaled $631,000 and $42.9 million at December 31, 2022 and 2021, respectively. During 2022 and 2021, we recognized $1.4 million and $8.1 million, respectively, in net deferred loan fees, which are included in loan interest income. As of December 31, 2022, remaining net deferred fees on PPP loans are not material to the consolidated financial statements.

Commercial other
Commercial other loans consist primarily of loans to municipalities and not for profit organizations, such as volunteer fire departments. Commercial other loans are dependent on the municipality or not for profit entity's ability to generate adequate cash flows to service the loan, primarily through tax revenues, fee revenues, federal and state grants, and donations by local citizens. As such, deterioration in the general economy could impact a borrower's ability to repay the loan due to declines in a municipality's tax base, available federal and state grants, and citizen's ability to provide donations. These loans are primarily secured by equipment used by the municipality or not for profit entity.

Non-commercial loans
Each non-commercial loan is underwritten based primarily upon the customer's ability to generate the required cash flow to service the debt in accordance with the contractual terms and conditions of the loan agreement. A complete understanding of the borrower's financial situation is obtained prior to loan approval. To the extent that the loan is secured by collateral we also evaluate the likely value of that collateral. Common risks to each class of non-commercial loans include risks that are not specific to individual transactions such as general economic conditions within the markets BancShares serves, particularly unemployment and potential declines in real estate values. Personal events such as disability or change in marital status also add risk to non-commercial loans.

(Dollars in Thousands for Tabular Presentations)

Note 3. Loans and Allowance for Loan Losses (Continued)

In addition to these common risks for the majority of non-commercial loans, additional risks are inherent in certain classes of non-commercial loans, as follows:

Revolving mortgage (“HELOCS”)
HELOC loans are often secured by second liens on residential real estate, thereby making such loans particularly susceptible to declining collateral values. A substantial decline in collateral value could render a second lien position to be effectively unsecured. Additional risks include lien perfection inaccuracies and disputes with first lien holders that may further weaken the collateral position. Further, the open-end structure of these loans creates the risk that customers may draw on the lines in excess of the collateral value if there have been significant declines since origination.

Consumer
The consumer loan portfolio includes loans secured by personal property such as automobiles, marketable securities, other titled recreational vehicles including boats and motorcycles, as well as unsecured consumer debt. The value of underlying collateral within this class is especially volatile due to potential rapid depreciation in values since the date of loan origination in excess of principal repayment.

Residential mortgage and non-commercial construction and land development
Residential mortgage and non-commercial construction and land development loans are made to individuals and are typically secured by 1-4 family residential property, undeveloped land, and partially developed land in anticipation of pending construction of a personal residence. Significant and rapid declines in real estate values can result in residential mortgage loan borrowers having debt levels in excess of the current market value of the collateral. Such a decline in values has led to unprecedented levels of foreclosures and losses within the banking industry. Non-commercial construction and land development projects can experience delays in completion and cost overruns that exceed the borrower’s financial ability to complete the project. Such cost overruns can routinely result in foreclosure of partially completed and unmarketable collateral.

Acquired loans
The risks associated with acquired loans are generally consistent with the risks identified for commercial and non-commercial loans and the classes of loans within those segments. Since these loans were not originally underwritten by Southern, there is a risk that these loans were not adequately supported by the paying capacity of the borrower or the value of underlying collateral at the time of origination.

During 2022 and 2021, (recovery) provision for loan losses on acquired loans totaled ($179,000) and ($1.0) million respectively.

In accordance with FASB guidance on accounting for acquired loans with deteriorated credit quality, BancShares aggregated the majority of acquired loans that have common risk characteristics into pools of loan categories as described in the tables that follow. Certain loans with unique characteristics or larger balances that did not conform to the pools are accounted for individually. These loans are identified as “Loans individually accounted for under FASB ASC Topic 310-30” in the tables that follow. The collectability of these loans is influenced by the continued stabilization of the local real estate market combined with borrower strength. The carrying value, which is net of specific reserves of $32,000 and $105,000 in 2022 and 2021, respectively and classification of these loans are as follows:

	December 31, 2022	December 31, 2021
Loans individually accounted for under FASB ASC Topic 310-30		
Non-farm, non-residential	$ 1,729	$ 1,936
1-4 family residential property	1,817	1,999
Commercial and industrial	576	700
1-4 family residential construction	-	5
Total loans individually accounted for under FASB ASC Topic 310-30	$ 4,122	$ 4,640

(Dollars in Thousands for Tabular Presentations)

Note 3. Loans and Allowance for Loan Losses (Continued)

Southern's acquired loan portfolio is comprised of the following balances, net of related discount:

	2022	2021
FASB ASC Topic 310-30 acquired loans:		
Commercial performing	$ 5	$ 9
Consumer performing	70	76
Consumer non-performing	561	574
Construction and development performing	574	692
Construction and development non-performing	537	495
Consumer real estate performing	1,543	2,509
Consumer real estate non-performing	922	1,825
Commercial real estate performing short term amortizing	520	687
Commercial real estate performing long term amortizing	1,738	2,317
Commercial real estate non-performing long term amortizing	10,431	11,936
Loans individually accounted for under FASB ASC Topic 310-30	4,155	4,745
Total FASB ASC Topic 310-30 acquired loans	21,056	25,865
FASB ASC Topic 310-20 acquired loans	53,447	67,450
Total acquired loans:	74,503	93,315
Less allowance for loan losses	(1,726)	(1,860)
Acquired loans, net	$ 72,777	$ 91,455

The total contractual principal balance for acquired loans at December 31, 2022 and 2021 was $86.1 million and $107.5 million, respectively.

The following are changes in the carrying value of acquired loans during the years ended December 31, 2022 and 2021.

	FASB ASC Topic 310-30
Balance at December 31, 2020	$ 29,798
Reductions for payments, foreclosures, and draws, net of accretion	(5,746)
Change in the allowance for loan losses	459
Balance at December 31, 2021	24,511
Reductions for payments, foreclosures, and draws, net of accretion	(4,812)
Change in the allowance for loan losses	75
Balance at December 31, 2022	$ 19,774

The total outstanding balance, which includes contractual principal and interest owed at the end of the reporting period, for loans accounted for under FASB ASC Topic 310-30 was $32.2 million and $39.5 million at December 31, 2022 and 2021, respectively.

The table above excludes $53.4 million ($336.0 million in fair value of acquired loans at acquisition date and $282.6 million in net decreases for payments, draws, and accretion) in acquired loans at carrying value as of December 31, 2022 that are accounted for under FASB ASC Topic 310-20. The table above excludes $67.5 million ($336.0 million in fair value of acquired loans at acquisition date and $268.5 million in net decreases for payments, draws, and accretion) in acquired loans at carrying value as of December 31, 2021 that are accounted for under FASB ASC Topic 310-20. At December 31, 2022 and 2021 there was an allowance for loan loss in the amount of $444,000 and $502,000, respectively which related to FASB ASC Topic 310-20 loans.

(Dollars in Thousands for Tabular Presentations)

Note 3. Loans and Allowance for Loan Losses (Continued)

The following are changes in the carrying amount of accretable yield for loans accounted for under FASB ASC Topic 310-30:

	Years Ended December 31, 2022	Years Ended December 31, 2021
Balance at beginning of period	$ 20,344	$ 24,489
Accretion recorded in interest income	(4,588)	(5,339)
Reclass of nonaccretable difference due to improvement in expected cash flows	444	28
Other changes, net	634	1,166
Balance at end of period	$ 16,834	$ 20,344

Allowance for loan losses
The allowance for loan losses is based upon estimates made by management. We maintain an allowance for loan losses at a level that we believe is appropriate to cover estimated credit losses on individually evaluated loans that are determined to be impaired as well as estimated credit losses inherent in the remainder of our loan portfolio. Arriving at the allowance involves a high degree of management judgment and results in a range of estimated losses. We regularly evaluate the adequacy of the allowance through our internal risk rating system, independent credit review, and regulatory agency examinations to assess the quality of the loan portfolio and identify problem loans. The evaluation process also includes our analysis of current economic conditions, composition of the loan portfolio, past due and nonaccrual loans, concentrations of credit, lending policies and procedures, and historical loan loss experience. While management uses available information to recognize losses on loans, future additions to the allowance may be necessary based on, among other factors, changes in economic conditions in our markets. In addition, regulatory agencies, as an integral part of their examination process, periodically review our allowances for losses on loans. These agencies may require management to recognize additions to the allowances based on their judgments about information available to them at the time of their examination. Because of these and other factors, it is possible that the allowances for losses on loans may change. The provision for loan losses is charged to expense in an amount necessary to maintain the allowance at an appropriate level.

The allowance for loan losses on non-acquired loans consists of general and specific reserves. The general reserves are determined by applying loss percentages to the portfolio that are based on the PD/LGD approach to calculating the historical loss rate for each call report code and risk grade. Additionally, the general economic and business conditions affecting key lending areas, credit quality trends, collateral values, loan volumes and concentrations, seasoning of the loan portfolio, the findings of internal and external credit reviews and results from external bank regulatory examinations are included in this evaluation. These adjustments are applied to the non-acquired loan portfolio when estimating the level of reserve required. The specific reserves are determined on a loan-by-loan basis based on management's evaluation of our exposure for each credit, given the current payment status of the loan and the value of any underlying collateral. These are loans classified by management as doubtful or substandard. For such loans that are also classified as impaired, an allowance is established when the discounted cash flows (or collateral value or observable market price) of the impaired loan is lower than the carrying value of that loan. Loans that are determined to be impaired are provided a specific reserve, if necessary, and are excluded from the calculation of the general reserves.

(Dollars in Thousands for Tabular Presentations)

Note 3. Loans and Allowance for Loan Losses (Continued)

In determining the acquisition date fair value of purchased loans, and in subsequent accounting, Southern generally aggregates purchased loans into pools of loans with common risk characteristics. Expected cash flows at the acquisition date in excess of the fair value of loans are recorded as interest income over the life of the loans using a level yield method if the timing and amount of the future cash flows of the pool is reasonably estimable. Subsequent to the acquisition date, increases in cash flows over those expected at the acquisition date reduce previously recorded allowance for loan losses and any remaining portion are reclassified from the nonaccretable difference to accretable yield and recognized as interest income prospectively. Decreases in expected cash flows after the acquisition date are recognized by recording an allowance for loan losses. Management analyzes the acquired loan pools and loans not accounted for in pools using various assessments of risk to determine an expected loss. The expected loss is derived based upon a loss given default based upon the collateral type and/or detailed review by loan officers and the probability of default that is determined based upon historical data at the loan level. Trends are reviewed in terms of accrual status, past due status, and weighted-average grade of the loans within each of the accounting pools. In addition, the relationship between the change in the unpaid principal balance and change in the mark is assessed to correlate the directional consistency of the expected loss for each pool.

An aggregated analysis of changes in allowance for loan losses is as follows:

	Non-acquired Loans	Acquired Loans	Total
Balance at December 31, 2020	$ 27,542	$ 2,608	$ 30,150
Loans charged-off	(983)	(7)	(990)
Recoveries of loans previously charged off	670	294	964
Net (charge-offs) recoveries	(313)	287	(26)
Provision (recovery) for loan losses	220	(1,035)	(815)
Balance at December 31, 2021	27,449	1,860	29,309
Loans charged-off	(700)	(1)	(701)
Recoveries of loans previously charged off	901	46	947
Net recoveries	201	45	246
Provision (recovery) for loan losses	6,458	(179)	6,279
Balance at December 31, 2022	$ 34,108	$ 1,726	$ 35,834

(Dollars in Thousands for Tabular Presentations)

Note 3. Loans and Allowance for Loan Losses (Continued)

The following tables present a disaggregated analysis of activity in the allowance for loan losses and loan balances for non-acquired loans:

	As of and for the Year Ended December 31, 2021											
	Commercial Construction and Land Development	Agricultural	Commercial Mortgage	Commercial and Industrial	Paycheck Protection Program	Commercial Other	Residential Mortgage	Revolving Mortgage (HELOCS)	Non-Commercial Construction and Land Development	Consumer	Demand Overdrafts	Total
Allowances for loan losses:												
December 31, 2020	$ 1,395	$ 3,059	$ 11,379	$ 2,601	$ -	$ 152	$ 5,667	$ 2,026	$ 578	$ 563	$ 122	$ 27,542
Charge offs	(39)	(66)	(2)	(444)	-	-	(55)	(26)	-	(85)	(266)	(983)
Recoveries	8	18	245	16	-	-	165	94	-	35	89	670
Provision charged to operating expense	(44)	(402)	(50)	355	-	38	325	(270)	68	(40)	240	220
December 31, 2021	$ 1,320	$ 2,609	$ 11,572	$ 2,528	$ -	$ 190	$ 6,102	$ 1,824	$ 646	$ 473	$ 185	$ 27,449
Allowance for loans individually evaluated for impairment	$ -	$ -	$ 7	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ 7
Allowance for loans collectively evaluated for impairment	1,320	2,609	11,565	2,528	-	190	6,102	1,824	646	473	185	27,442
Loans:												
Ending balance:												
Total	$ 110,373	$ 221,896	$ 988,172	$ 204,240	$ 42,861	$ 28,829	$ 519,277	$ 148,370	$ 56,403	$ 25,541	$ 272	$ 2,346,234
Individually evaluated for impairment	737	1,208	1,678	491	-	-	573	-	-	-	-	4,687
Collectively evaluated for impairment	109,636	220,688	986,494	203,749	42,861	28,829	518,704	148,370	56,403	25,541	272	2,341,547

(Dollars in Thousands for Tabular Presentations)

Note 3. Loans and Allowance for Loan Losses (Continued)

	As of and for the Year Ended December 31, 2022											
	Commercial Construction and Land Development	Agricultural	Commercial Mortgage	Commercial and Industrial	Paycheck Protection Program	Commercial Other	Residential Mortgage	Revolving Mortgage (HELOCS)	Non-Commercial Construction and Land Development	Consumer	Demand Overdrafts	Total
Allowance for loan losses:												
December 31, 2021	$ 1,320	$ 2,609	$ 11,572	$ 2,528	$ -	$ 190	$ 6,102	$ 1,824	$ 646	$ 473	$ 185	$ 27,449
Charge offs	-	(115)	(50)	(90)	-	-	(1)	(16)	-	(66)	(362)	(700)
Recoveries	8	48	315	304	-	-	38	102	-	25	61	901
Provision charged to operating expense	754	441	1,988	(63)	8	199	2,499	339	(95)	(30)	418	6,458
December 31, 2022	$ 2,082	$ 2,983	$ 13,825	$ 2,679	$ 8	$ 389	$ 8,638	$ 2,249	$ 551	$ 402	$ 302	$ 34,108
Allowance for loans individually evaluated for impairment	$ -	$ -	$ 5	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ 5
Allowance for loans collectively evaluated for impairment	2,082	2,983	13,820	2,679	8	389	8,638	2,249	551	402	302	34,103
Loans:												
Ending balance:												
Total	172,733	233,233	1,152,367	218,068	631	32,685	716,210	180,486	45,846	23,274	331	2,775,864
Individually evaluated for impairment	221	990	1,777	-	-	-	432	-	-	-	-	3,420
Collectively evaluated for impairment	172,512	232,243	1,150,590	218,068	631	32,685	715,778	180,486	45,846	23,274	331	2,772,444

(Dollars in Thousands for Tabular Presentations)

Note 3. Loans and Allowance for Loan Losses (Continued)

The following tables present a disaggregated analysis of activity in the allowance for loan losses and loan balances for acquired loans:

	Commercial Performing	Consumer Performing	Consumer Non-Performing	Construction and Development Performing	Construction and Development Non-Performing	Consumer Real Estate Performing	Consumer Real Estate Non-Performing	Commercial Real Estate Performing ST Amortizing
Allowances for loan losses:								
December 31, 2020	$ -	$ -	$ 549	$ -	$ -	$ -	$ -	$ -
Charge offs	-	-	-	-	-	-	-	-
Recoveries	-	-	-	-	-	-	-	-
Provision charged to operating expense	-	-	(4)	-	-	-	-	-
December 31, 2021	$ -	$ -	$ 545	$ -	$ -	$ -	$ -	$ -
Allowance for loans individually evaluated for impairment	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
Allowance for loans collectively evaluated for impairment	-	-	545	-	-	-	-	-
Loans:								
Total	9	76	574	692	495	2,509	1,825	687
Individually evaluated for impairment	-	-	-	-	-	-	-	-
Collectively evaluated for impairment	9	76	574	692	495	2,509	1,825	687
December 31, 2021	$ -	$ -	$ 545	$ -	$ -	$ -	$ -	$ -
Charge offs	-	-	-	-	-	-	-	-
Recoveries	-	-	-	-	-	-	-	-
Provision charged to operating expense	-	-	(3)	-	-	-	-	-
December 31, 2022	$ -	$ -	$ 542	$ -	$ -	$ -	$ -	$ -
Allowance for loans individually evaluated for impairment	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
Allowance for loans collectively evaluated for impairment	-	-	542	-	-	-	-	-
Loans:								
Total	5	70	561	574	537	1,543	922	520
Individually evaluated for impairment	-	-	-	-	-	-	-	-
Collectively evaluated for impairment	5	70	561	574	537	1,543	922	520

(Dollars in Thousands for Tabular Presentations)

Note 3. Loans and Allowance for Loan Losses (Continued)

	Commercial Real Estate Performing LT Amortizing	Commercial Real Estate Non-Performing LT Amortizing	Loans Individually Accounted For Under FASB ASC Topic 310-30	FASB ASC Topic 310-20 Loans	Total
Allowances for loan losses:					
December 31, 2020	$ -	$ 708	$ 560	$ 791	$ 2,608
Charge offs	-	-	(6)	(1)	(7)
Recoveries	-	-	-	294	294
Provision charged to operating expense	-	-	(449)	(582)	(1,035)
December 31, 2021	$ -	$ 708	$ 105	$ 502	$ 1,860
Allowance for loans individually evaluated for impairment	$ -	$ -	$ 105	$ -	$ 105
Allowance for loans collectively evaluated for impairment	-	708	-	502	1,755
Loans:					
Total	2,317	11,936	4,745	67,450	93,315
Individually evaluated for impairment	-	-	4,745	-	4,745
Collectively evaluated for impairment	2,317	11,936	-	67,450	88,570
December 31, 2021	$ -	$ 708	$ 105	$ 502	$ 1,860
Charge offs	-	-	-	(1)	(1)
Recoveries	-	-	-	46	46
Provision charged to operating expense	-	-	(73)	(103)	(179)
December 31, 2022	$ -	$ 708	$ 32	$ 444	$ 1,726
Allowance for loans individually evaluated for impairment	$ -	$ -	$ 32	$ -	$ 32
Allowance for loans collectively evaluated for impairment	-	708	-	444	1,694
Loans:					
Total	1,738	10,431	4,155	53,447	74,503
Individually evaluated for impairment	-	-	4,155	-	4,155
Collectively evaluated for impairment	1,738	10,431	-	53,447	70,348

Note 3. Loans and Allowance for Loan Losses (Continued)

Loans are closely monitored by management for changes in quality. This monitoring includes assessing the appropriateness of the credit quality indicator in relation to the risk of the loan. Southern utilizes a risk rating matrix to assign a risk rating to each of its loans. A description of the general characteristics of risk ratings is as follows:

- Superior - This grade includes loans to borrowers with excellent credit quality. These borrowers have exceptionally high net worth and cash flows to service existing debt and most have a significant or long term deposit relationship with Southern. If secured, the collateral for these loans is readily marketable and consists of savings accounts, life insurance assignments, etc.

- Above average - This grade includes loans to borrowers of adequate credit quality, sufficient net worth and cash flows to service existing debt. Borrowers in this grade have an existing long term deposit relationship with Southern and have made a reasonable investment in the loan. If secured, collateral for these loans is reasonably marketable such as listed stocks and bonds.

- Average - This grade includes loans to borrowers of acceptable credit quality and risk. Such borrowers have maintained an existing deposit relationship with Southern, but not for the time periods of those included in the above grades of average and superior. These borrowers also have sufficient net worth and cash flows to service existing debt, but not to the level of those included in grades above average and superior. There has been reasonable investment in the loan by the borrower.

- Below average - This grade includes loans to borrowers with credit history that reflects delinquencies with justifiable explanation or no credit history. Typically these borrowers do not have a deposit relationship with Southern and/or have made an insignificant investment in the loan. Included in this grade are loans to borrowers with marginal cash flows and net worth or who reside outside of the trade area. Also, loans for which repayment is dependent upon sales in unproven or unstable markets fall into this grade.

- Special mention - This grade is for loans which are “especially mentioned” in accordance with regulatory guidelines. This grade includes loans on management’s “watchlist”. This grade includes loans for which repayment terms exceed policy or with no significant principal reduction in the past 12 months, are in an industry that is deteriorating, or that repayment is based upon the sale of collateral, guarantors, or government guarantees. Also included are real estate under construction for speculative purposes and the borrower does not have a long history of sales. This grade is intended to be temporary and includes loans to borrowers whose credit quality has clearly deteriorated and are at risk of further decline unless active measures are taken to correct the situation.

- Substandard - This grade includes loans on management’s “watchlist”. Substandard loans are inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any. Loans so classified must have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. These loans are characterized by the distinct possibility that Southern will sustain some loss if the deficiency is not corrected.

- Doubtful - Loans classified as “doubtful” have all the weaknesses inherent in those classified as “substandard” with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently known facts, conditions, and values, highly questionable and improbable.

- Loss - Loans are considered uncollectible and of such little value that their continuance as bankable assets is not warranted. This classification does not mean that the loan has absolutely no recovery or salvage value, but rather it is not practical or desirable to defer writing off this basically worthless asset even though partial recovery may be affected in the future. Included in this category are loans that are covered under loss share agreements with the FDIC which have been partial charge-offs based on the terms of the loss share agreements.

- Ungradable - This represents loans that are HELOC and other consumer type loans with relatively small balances for which risk ratings are not assigned.

(Dollars in Thousands for Tabular Presentations)

Note 3. Loans and Allowance for Loan Losses (Continued)

The following presents the credit risk profile by risk grade for non-acquired loans:

	As of December 31, 2022								
	Superior	Above average	Average	Below average	Special mention	Substandard	Doubtful	Loss	Total
Commercial:									
Construction and land development	$ -	$ 3,334	$ 153,370	$ 15,919	$ 92	$ 18	$ -	$ -	$ 172,733
Agricultural	-	-	167,246	46,349	17,877	1,761	-	-	233,233
Commercial mortgage	-	1,301	995,395	153,356	517	1,798	-	-	1,152,367
Commercial and industrial	2	1	165,954	51,693	193	225	-	-	218,068
Payroll Protection Program	-	-	479	152	-	-	-	-	631
Other	-	-	32,685	-	-	-	-	-	32,685
Non-commercial:									
Residential mortgage	-	-	681,825	31,229	1,361	1,795	-	-	716,210
Revolving mortgage (HELOCS)	-	1,183	168,789	9,377	471	666	-	-	180,486
Construction and land development	-	-	43,119	2,694	-	33	-	-	45,846
Consumer	-	42	21,249	1,856	43	84	-	-	23,274
Demand overdrafts	-	-	331	-	-	-	-	-	331
Total non-acquired loans	$ 2	$ 5,861	$ 2,430,442	$ 312,625	$ 20,554	$ 6,380	$ -	$ -	$ 2,775,864

	As of December 31, 2021								
	Superior	Above average	Average	Below average	Special mention	Substandard	Doubtful	Loss	Total
Commercial:									
Construction and land development	$ -	$ -	$ 90,029	$ 19,125	$ 1,034	$ 185	$ -	$ -	$ 110,373
Agricultural	-	-	173,595	46,268	439	1,594	-	-	221,896
Commercial mortgage	403	5,596	810,106	165,187	5,136	1,744	-	-	988,172
Commercial and industrial	2	116	146,009	56,671	725	717	-	-	204,240
Paycheck Protection Program	-	-	42,861	-	-	-	-	-	42,861
Other	-	-	28,829	-	-	-	-	-	28,829
Non-commercial:									
Residential mortgage	-	3	481,169	34,946	1,484	1,675	-	-	519,277
Revolving mortgage (HELOCS)	-	1,185	137,874	8,525	121	665	-	-	148,370
Construction and land development	-	-	53,576	2,707	-	120	-	-	56,403
Consumer	-	125	23,164	2,126	48	78	-	-	25,541
Demand overdrafts	-	-	272	-	-	-	-	-	272
Total non-acquired loans	$ 405	$ 7,025	$ 1,987,484	$ 335,555	$ 8,987	$ 6,778	$ -	$ -	$ 2,346,234

(Dollars in Thousands for Tabular Presentations)

Note 3. Loans and Allowance for Loan Losses (Continued)

The following table presents the credit risk profile by risk grade of acquired loans, net of the related discount.

	As of December 31, 2022									
	Superior	Above average	Average	Below average	Special mention	Substandard	Doubtful	Loss	Ungradable	Total
FASB ASC Topic 310-30 acquired loans:										
Commercial performing	$ -	$ -	$ 5	$ -	$ -	$ -	$ -	$ -	$ -	$ 5
Consumer performing	-	-	70	-	-	-	-	-	-	70
Consumer non-performing	-	-	303	-	111	147	-	-	-	561
Construction and development performing	-	-	-	574	-	-	-	-	-	574
Construction and development non-performing	-	-	-	258	-	279	-	-	-	537
Consumer real estate performing	-	-	97	1,083	295	68	-	-	-	1,543
Consumer real estate non-performing	-	-	323	42	87	470	-	-	-	922
Commercial real estate performing ST amortizating	-	-	-	520	-	-	-	-	-	520
Commercial real estate performing LT amortizating	-	-	245	1,093	400	-	-	-	-	1,738
Commercial real estate non-performing LT amortizating	-	-	281	5,600	197	4,353	-	-	-	10,431
Loans individually accounted for under FASB ASC Topic 310-30	-	-	75	624	12	3,444	-	-	-	4,155
FASB ASC Topic 310-20 acquired loans	-	10	45,022	6,583	1,351	481	-	-	-	53,447
Total acquired loans	$ -	$ 10	$ 46,421	$ 16,377	$ 2,453	$ 9,242	$ -	$ -	$ -	$ 74,503

	As of December 31, 2021									
	Superior	Above average	Average	Below average	Special mention	Substandard	Doubtful	Loss	Ungradable	Total
FASB ASC Topic 310-30 acquired loans:										
Commercial performing	$ -	$ -	$ 9	$ -	$ -	$ -	$ -	$ -	$ -	$ 9
Consumer performing	-	-	76	-	-	-	-	-	-	76
Consumer non-performing	-	-	-	101	320	153	-	-	-	574
Construction and development performing	-	-	-	553	-	139	-	-	-	692
Construction and development non-performing	-	-	-	245	-	250	-	-	-	495
Consumer real estate performing	-	-	105	1,796	185	423	-	-	-	2,509
Consumer real estate non-performing	-	-	479	171	245	930	-	-	-	1,825
Commercial real estate performing ST amortizating	-	-	109	578	-	-	-	-	-	687
Commercial real estate performing LT amortizating	-	-	433	1,450	434	-	-	-	-	2,317
Commercial real estate non-performing LT amortizating	-	-	338	6,572	197	4,829	-	-	-	11,936
Loans individually accounted for under FASB ASC Topic 310-30	-	-	1,178	697	14	2,856	-	-	-	4,745
FASB ASC Topic 310-20 acquired loans	-	4	55,802	9,736	1,463	445	-	-	-	67,450
Total acquired loans	$ -	$ 4	$ 58,529	$ 21,899	$ 2,858	$ 10,025	$ -	$ -	$ -	$ 93,315

(Dollars in Thousands for Tabular Presentations)

Note 3. Loans and Allowance for Loan Losses (Continued)

The risk grading of acquired loans is determined utilizing a loan's contractual balance, while the amount recorded in the financial statements and reflected above is the carrying value.

The following is a summary of information pertaining to impaired non-acquired and acquired loans accounted for under FASB ASC Topic 310-10:

	As of December 31, 2022				
	Unpaid Contractual Principal Balance	Recorded Investment With No Allowance	Recorded Investment With Allowance	Total Recorded Investment	Related Allowance
Non-acquired:					
Commercial:					
Construction and land development	$ 221	$ 221	$ -	$ 221	$ -
Agricultural	1,353	990	-	990	-
Commercial mortgage	2,175	1,558	219	1,777	5
Commercial and industrial	-	-	-	-	-
Non-commercial:					
Residential mortgage	511	432	-	432	-
Total non-acquired loans	4,260	3,201	219	3,420	5
Acquired:					
FASB ASC Topic 310-20 acquired loans	-	-	-	-	-
Total acquired loans	-	-	-	-	-
Total impaired loans	$ 4,260	$ 3,201	$ 219	$ 3,420	$ 5

	As of December 31, 2021				
	Unpaid Contractual Principal Balance	Recorded Investment With No Allowance	Recorded Investment With Allowance	Total Recorded Investment	Related Allowance
Non-acquired:					
Commercial:					
Construction and land development	$ 737	$ 737	$ -	$ 737	$ -
Agricultural	1,410	1,208	-	1,208	-
Commercial mortgage	2,024	1,414	264	1,678	7
Commercial and industrial	776	491	-	491	-
Non-commercial:					
Residential mortgage	631	631	-	631	-
Total non-acquired loans	5,578	4,481	264	4,745	7
Acquired:					
FASB ASC Topic 310-20 acquired loans	149	116	-	116	-
Total acquired loans	149	116	-	116	-
Total impaired loans	$ 5,727	$ 4,597	$ 264	$ 4,861	$ 7

(Dollars in Thousands for Tabular Presentations)

Note 3. Loans and Allowance for Loan Losses (Continued)

The following table summarizes the average investment in impaired loans, non-acquired and acquired loans accounted for under FASB ASC Topic 310-10, and interest income recognized on these loans:

	Years Ended December 31,			
	2022		2021	
	Average Investment in Impaired Loans	Interest Income Recognized	Average Investment in Impaired Loans	Interest Income Recognized
Non-acquired:				
Commercial:				
Construction and land development	$ 568	$ 24	$ 746	$ 38
Agricultural	1,148	-	1,180	2
Commercial mortgage	1,691	32	1,986	27
Commercial and industrial	358	38	98	5
Non-commercial:				
Residential mortgage	527	2	1,168	29
Total non-acquired loans	4,292	96	5,178	101
Acquired:				
FASB ASC Topic 310-20 acquired loans	-	-	45	-
Total acquired loans	-	-	45	-
Total impaired loans	$ 4,292	$ 96	$ 5,223	$ 101

The amount of foregone interest on non-acquired and acquired loans accounted for under FASB ASC Topic 310-10 at December 31, 2022 and 2021 was not material for the periods presented.

The following is a summary of information pertaining to non-accrual loans accounted for under FASB ASC Topic 310-10 including restructured loans:

	As of December 31,	
	2022	2021
Non-acquired:		
Commercial:		
Agricultural	$ 990	$ 1,208
Commercial mortgage	1,294	1,158
Commercial and industrial	-	491
Non-commercial:		
Residential mortgage	432	-
Consumer	-	573
Total non-acquired	2,716	3,430
Acquired:		
FASB ASC Topic 310-20 acquired loans	-	-
Total acquired	-	-
Total non-accrual loans	$ 2,716	$ 3,430

(Dollars in Thousands for Tabular Presentations)

Note 3. Loans and Allowance for Loan Losses (Continued)

An aging analysis of past due loans, segregated by class for non-acquired loans, was as follows:

	As of December 31, 2022						
	30-59 Days Past Due	60-89 Days Past Due	Greater Than 90 Days Past Due	Total Past Due	Current	Total	Recorded Investment Greater Than 90 Days and Accruing
Commercial:							
Construction and land development	$ 10	$ -	$ -	$ 10	$ 172,723	$ 172,733	$ -
Agriculture	304	-	374	678	232,555	233,233	-
Commercial mortgage	226	137	-	363	1,152,004	1,152,367	-
Commercial and industrial	280	-	34	314	217,754	218,068	-
Paycheck Protection Program	152	-	-	152	479	631	-
Other	-	-	-	-	32,685	32,685	-
Non-commercial:							
Residential mortgage	926	300	-	1,226	714,984	716,210	-
Revolving mortgage (HELOCS)	800	10	-	810	179,676	180,486	-
Construction and land development	66	-	-	66	45,780	45,846	-
Consumer	57	-	-	57	23,217	23,274	-
Demand overdrafts	-	-	-	-	331	331	-
Total non-acquired loans	$ 2,821	$ 447	$ 408	$ 3,676	$ 2,772,188	$ 2,775,864	$ -

	As of December 31, 2021						
	30-59 Days Past Due	60-89 Days Past Due	Greater Than 90 Days Past Due	Total Past Due	Current	Total	Recorded Investment Greater Than 90 Days and Accruing
Commercial:							
Construction and land development	$ -	$ -	$ -	$ -	$ 110,373	$ 110,373	$ -
Agriculture	282	-	320	602	221,294	221,896	-
Commercial mortgage	628	-	146	774	987,398	988,172	-
Commercial and industrial	198	-	-	198	204,042	204,240	-
Paycheck Protection Program	-	-	-	-	42,861	42,861	-
Other	-	-	-	-	28,829	28,829	-
Non-commercial:							
Residential mortgage	955	87	170	1,212	518,065	519,277	-
Revolving mortgage (HELOCS)	39	-	-	39	148,331	148,370	-
Construction and land development	8	-	5	13	56,390	56,403	-
Consumer	26	7	34	67	25,474	25,541	-
Demand overdrafts	-	-	-	-	272	272	-
Total non-acquired loans	$ 2,136	$ 94	$ 675	$ 2,905	$ 2,343,329	$ 2,346,234	$ -

(Dollars in Thousands for Tabular Presentations)

Note 3. Loans and Allowance for Loan Losses (Continued)

An aging analysis of past due loans, segregated by class for acquired loans, was as follows:

	As of December 31, 2022					
	30-59 Days Past Due	60-89 Days Past Due	90 Days Past Due	Past Due	Current	Total
FASB ASC Topic 310-30 acquired loans:						
Commercial performing	$ -	$ -	$ -	$ -	$ 5	$ 5
Consumer performing	-	-	-	-	70	70
Consumer non-performing	-	-	-	-	561	561
Construction and development performing	-	-	-	-	574	574
Construction and development non-performing	-	-	-	-	537	537
Consumer real estate performing	-	6	-	6	1,537	1,543
Consumer real estate non-performing	-	37	-	37	885	922
Commercial real estate performing ST amortizing	-	-	-	-	520	520
Commercial real estate performing LT amortizing	-	-	-	-	1,738	1,738
Commercial real estate non-performing LT amortizing	-	32	1,125	1,157	9,274	10,431
Loans individually accounted for under FASB ASC Topic 310-30	-	-	-	-	4,155	4,155
Total FASB ASC Topic 310-30 acquired loans	-	75	1,125	1,200	19,856	21,056
FASB ASC Topic 310-20 acquired loans	319	43	80	443	53,004	53,447
Total acquired loans	$ 319	$ 118	$ 1,205	$ 1,643	$ 72,860	$ 74,503

	As of December 31, 2021					
	30-59 Days Past Due	60-89 Days Past Due	90 Days Past Due	Past Due	Current	Total
FASB ASC Topic 310-30 acquired loans:						
Commercial performing	$ -	$ -	$ -	$ -	$ 9	$ 9
Consumer performing	-	-	-	-	76	76
Consumer non-performing	-	-	-	-	574	574
Construction and development performing	-	-	-	-	692	692
Construction and development non-performing	-	-	-	-	495	495
Consumer real estate performing	105	12	-	117	2,392	2,509
Consumer real estate non-performing	51	44	-	95	1,730	1,825
Commercial real estate performing ST amortizing	-	-	-	-	687	687
Commercial real estate performing LT amortizing	-	-	-	-	2,317	2,317
Commercial real estate non-performing LT amortizing	-	-	1,135	1,135	10,801	11,936
Loans individually accounted for under FASB ASC Topic 310-30	-	-	-	-	4,745	4,745
Total FASB ASC Topic 310-30 acquired loans	156	56	1,135	1,347	24,518	25,865
FASB ASC Topic 310-20 acquired loans	16	-	177	193	67,257	67,450
Total acquired loans	$ 172	$ 56	$ 1,312	$ 1,540	$ 91,775	$ 93,315

In the course of resolving delinquent loans, Southern may choose to restructure the contractual terms of certain loans. A TDR is a restructuring of a loan in which a concession is granted to a borrower experiencing financial difficulty. A loan is accounted for as a TDR if Southern, for reasons related to the borrower's financial difficulties, grants a concession to the borrower that it would not otherwise grant. A TDR typically involves a modification of terms such as a reduction of the interest rate below the current market rate for a loan with similar risk characteristics or the waiving of certain financial loan covenants without corresponding offsetting compensation or additional support. BancShares measures the impairment loss of a TDR using the methodology for individually impaired loans. In accordance with FASB ASC Topic 310-30, a loan is not considered a TDR at the date of acquisition but may be classified as such if a modification is made subsequent to the acquisition.

(Dollars in Thousands for Tabular Presentations)

Note 3. Loans and Allowance for Loan Losses (Continued)

The following table presents a breakdown of the types of concessions made by loan class for the non-acquired loans that were modified as TDR's during 2022 and 2021. For the twelve month periods ended December 31, 2022 and 2021, the recorded investment in TDR's prior to modification was not materially impacted by the modification. Commitments to lend additional funds to TDR borrowers at December 31, 2022 and 2021 were not material.

	Years Ended December 31,					
	2022			2021		
	Number of Loans	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment	Number of Loans	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Extended payment terms:						
Commercial mortgage	2	$ 208	$ 208	-	$ -	$ -
Total restructured loans	2	$ 208	$ 208	-	$ -	$ -

Southern had $1.8 million and $2.6 million of non-acquired loans considered TDR's at December 31, 2022 and 2021, respectively. Included in TDR's are non-acquired loans totaling $769,000 and $964,000 at December 31, 2022 and 2021, respectively, which were also classified as nonaccrual loans. These loans were modified to extend maturity dates or permit interest only terms for a defined period of time with no material effect on interest income recognition.

These TDRs are evaluated on an individual basis along with all other TDRs based on underlying collateral value if asset dependent or the present value of future cash flows. In the event that there is a shortfall in the value of the collateral securing these loans or the present value of future cash flows, the calculated impairment is reserved for in the allowance for loan losses.

The following table presents non-acquired loans that were modified as TDRs during the 12 months indicated for which there was a payment default. A payment default is defined as a loan that is past due more than 30 days.

	December 31, 2022		December 31, 2021	
	Number of Loans	Recorded Investment	Number of Loans	Recorded Investment
Modifications with payment defaults				
Commercial mortgage	1	$ 45	-	$ -
Total defaults	1	$ 45	-	$ -

These TDRs are evaluated on an individual basis along with all other TDRs based on underlying collateral value. In the event that there is a shortfall in the value of the collateral securing these loans, the calculated impairment is included in the allowance for loan losses.

At December 31, 2021, BancShares had $86,000 of foreclosed residential real estate property in OREO. There was no OREO as of December 31, 2022. The recorded investment in residential mortgage loans in the process of foreclosure totaled $141,000 and $96,000 at December 31, 2022 and December 31, 2021, respectively.

(Dollars in Thousands for Tabular Presentations)

Note 4. Premises and Equipment

The components of premises and equipment were as follows:

	December 31, 2022	December 31, 2021
Land	$ 18,138	$ 18,313
Buildings and improvements	71,834	72,007
Furniture and equipment	25,457	26,432
Construction in progress	6,545	3,090
	121,974	119,842
Less: accumulated depreciation	(57,763)	(54,318)
Balance at the end of the year	$ 64,211	$ 65,524

Depreciation and amortization amounts of $4.4 million and $4.9 million in 2022 and 2021, respectively, are included in occupancy and furniture and equipment expenses. Construction in progress represents new facilities being built and other facilities currently undergoing renovations.

Premises and Equipment Lease Commitments

As of December 31, 2022 and 2021 BancShares had operating lease right of use assets of $3.5 million and $4.0 million, respectively and operating lease liabilities of $3.7 million and $4.2 million, respectively. BancShares maintains operating leases on land and buildings for some of the Southern's branch facilities. Most leases include renewal options, with renewal terms that management is reasonably certain to exercise extending up to 9 years. The exercise of renewal options is based on the judgment of management as to whether or not the renewal option is reasonably certain to be exercised. Factors in determining whether an option is reasonably certain of exercise include, but are not limited to, the value of leasehold improvements, the value of renewal rates compared to market rates, and the presence of factors that would cause a significant economic penalty to Southern if the option is not exercised. As allowed by the standard, leases with a term of 12 months or less are not recorded in the consolidated balance sheets and instead are recognized in lease expense on a straight-line basis over the lease term.

Operating lease expense, included in occupancy expense in the consolidated statements of income and other comprehensive (loss) income, totaled $889,000 and $857,000 during 2022 and 2021, respectively, all of which relates to fixed obligations. Short-term leases of equipment, included in furniture and equipment expense in the consolidated statements of income and other comprehensive income (loss), totaled $7,000 and $6,000, while leases of facilities owned or subleases of facilities leased, in which Southern is the lessor, included in other noninterest income in the consolidated statements of income and other comprehensive income (loss), totaled $158,000 and $210,000 during 2022 and 2021, respectively. Lease payments under operating leases that were applied to the operating lease liability totaled $754,000 and $691,000 during 2022 and 2021, respectively.

The following table reconciles future undiscounted lease payments to the operating lease liability as of December 31, 2022.

2023	$ 748
2024	751
2025	684
2026	471
2027	378
Thereafter	1,091
Total undiscounted operating lease liabilities	4,123
Imputed interest	419
Total operating lease liabilites	$ 3,704
Weighted average lease term in years	6.30
Weighted average discount rate	3.09%

As of December 31, 2022 and 2021, Southern did not maintain any finance leases or leases with related parties, and the number and dollar amount of equipment leases and short-term leases were determined to be immaterial. As of December 31, 2022, Southern had no additional leases that have not yet commenced.

(Dollars in Thousands for Tabular Presentations)

Note 5. Income Taxes

Allocation of federal and state income taxes between current and deferred portions for the years ended December 31 is as follows:

	2022	2021
Current:		
Federal	$ 11,394	$ 11,039
State	3,250	1,180
Total	14,644	12,219
Deferred:		
Federal	(5,103)	11,843
State	(18)	(2,459)
Total	(5,121)	9,384
Total tax expense	$ 9,523	$ 21,603

A reconciliation of income tax expense computed at the statutory federal income tax rate of 21 percent to income tax expense included in net income is as follows:

	2022	2021
Tax at statutory federal rate	$ 8,283	$ 24,181
State income tax expense (benefit), net of federal benefit	2,985	(1,011)
Tax exempt income	(1,545)	(1,432)
Dividends received deduction	(76)	(74)
Other	(124)	(61)
Total	$ 9,523	$ 21,603

The components of the net deferred tax asset (included in other assets) at December 31, 2022 and the net deferred tax liability (included in other liabilities) at December 31, 2021 are as follows:

	December 31, 2022	December 31, 2021
Deferred tax assets:		
Allowance for loan losses	$ 7,662	$ 6,305
Pension liability	-	16
Deferred compensation	743	823
Unrealized losses on available for sale securities	58,634	841
Operating lease liabilities	840	959
Other	687	714
Total deferred tax assets	68,566	9,658
Deferred tax liabilities:		
Depreciation	(1,080)	(1,255)
Intangibles	(1,571)	(1,573)
Pension funding commitment	(3,540)	(3,855)
Unrealized gains on marketable equity securities	(31,085)	(34,628)
Pension liability	(303)	-
FDIC acquisition	(1,533)	(1,310)
Operating lease right of use assets	(792)	(915)
Other	(900)	(955)
Total deferred tax liabilities	(40,804)	(44,491)
Net deferred tax asset (liability)	$ 27,762	$ (34,833)

(Dollars in Thousands for Tabular Presentations)

Note 5. Income Taxes (Continued)

In November 2021, North Carolina adopted a graduated reduction in its corporate income tax rate. Beginning in 2025 the corporate tax rates will be reduced from 2.50% to 0% in years subsequent to December 31, 2029. Accordingly, BancShares' deferred tax assets and liabilities were re-measured to reflect the reduction in the future North Carolina corporate income tax rate based on when the estimated deferred tax assets and liabilities will reverse. This resulted in a $2.1 million increase in income tax expense and a reduction in net deferred tax assets, and a $3.0 million decrease in income tax expense and net deferred tax liabilities for the years ended December 31, 2022 and 2021, respectively. The re-measurement of deferred tax assets related to net unrealized losses on investment securities available for sale recorded in accumulated other comprehensive (loss) income totaled $2.1 million at December 31, 2022. The re-measurement of deferred tax assets and liabilities related to all other components of accumulated other comprehensive (loss) income was immaterial at December 31, 2022 and 2021.

BancShares has invested in Qualified Affordable Housing Projects in the amount of $7.4 million at December 31, 2022 and 2021. The investment balance net of amortized tax benefits is $4.7 million and $5.2 million at December 31, 2022 and 2021, respectively and is shown in the consolidated balance sheets in other assets. BancShares also has commitments, which are shown in other liabilities in the consolidated balance sheets, to provide additional capital calls in the amount of $1.3 million and $2.0 million at December 31, 2022 and 2021, respectively. It is anticipated that these additional commitment amounts will be paid within the next three years.

Tax positions must meet a recognition threshold of more-likely-than-not in order for the benefit of those tax positions to be recognized in BancShares' consolidated financial statements. BancShares has determined that it does not have any material unrecognized tax benefits or obligations as of December 31, 2022. Interest and penalties related to income tax assessments, if any, are reflected in income tax expense in the consolidated statements of income and comprehensive (loss) income. Fiscal years ending on or after December 31, 2019 remain subject to examination by federal and state tax authorities.

Note 6. Deposits

Deposits at December 31 are summarized as follows:

		2022		2021
Noninterest-bearing demand	$	1,445,626	$	1,386,132
Time		305,370		278,326
Money market accounts		1,249,446		1,171,002
Checking with interest		798,266		787,656
Savings		327,274		296,067
Total deposits	$	4,125,982	$	3,919,183

Total time deposits with a denomination of $250,000 or more were $65.5 million and $81.5 million at December 31, 2022 and 2021, respectively.

At December 31, 2022, the scheduled maturities of all time deposits were:

2023	$	249,978
2024		32,588
2025		5,315
2026		5,041
2027		3,537
Thereafter		8,911
Total time deposits	$	305,370

Time deposits as of December 31, 2022, included $51.2 million of brokered deposits, all of which have scheduled maturities during 2023. There were no brokered deposits as of December 31, 2021.

(Dollars in Thousands for Tabular Presentations)

Note 7. Short and Long-Term Borrowings

Short-term borrowings at December 31 were:

	2022	2021
Repurchase agreements	$ 53,061	$ 63,670
FHLB advances	155,000	-
Total short-term borrowings	$ 208,061	$ 63,670

For the years ended December 31, 2022 and 2021, short-term borrowings outstanding averaged $117.1 million and $59.1 million, respectively, with weighted average rates of 1.48% and 0.26% as of December 31, 2022 and 2021, respectively.

Southern utilizes securities sold under agreements to repurchase to facilitate the needs of our customers. Repurchase agreements are transactions whereby Souhern offers to sell to a counterparty an undivided interest in an eligible security at an agreed upon purchase price, and which obligates Southern to repurchase the security on an agreed upon date at an agreed upon repurchase price plus interest at an agreed upon rate. Securities sold under agreements to repurchase are recorded at the amount of cash received in connection with the transaction and are reflected as Short-term borrowings in the consolidated balance sheets.

Southern monitors collateral levels on a continuous basis and maintain records of each transaction specifically describing the applicable security and the counterparty's fractional interest in that security, and segregates the security from its general assets in accordance with regulations governing custodial holdings of securities. The primary risk with Southern's repurchase agreements is market risk associated with the investments securing the transactions, as Southern may be required to provide additional collateral based on fair value changes of the underlying investments. Securities pledged as collateral under repurchase agreements are maintained with Southern's safekeeping agents.

At December 31, 2022 and 2021, investment securities with a carrying value of $72.2 million and $82.4 million, respectively were pledged for repurchase agreements. The securities collateralizing the repurchase agreements have been delivered to a third party custodian for safekeeping. In addition, loans totaling $937.7 million and $837.1 million are pledged as collateral for potential advances from the Federal Home Loan Bank at December 31, 2022 and 2021, respectively.

The remaining contractual maturity of the securities sold under agreements to repurchase by class of collateral pledged included in short-term borrowings as of December 31, 2022 and 2021 is as follows:

	Overnight and Continuous	
	2022	2021
U.S. Treasuries and government-sponsored entity debt	$ 34,052	$ 46,595
Obligations of states and political subdivisions	6,132	8,591
Government-sponsored mortgage backed securities	32,040	27,173
Total	$ 72,224	$ 82,359

Long-term borrowings at December 31 were:

	2022	2021
Subordinated notes payable	$ 80,000	$ 80,000
Senior notes payable	10,000	10,000
Unamortized issuance costs	(1,007)	(1,126)
Total long-term borrowings	$ 88,993	$ 88,874

On September 15, 2021, BancShares redeemed $23.7 million of 6.95% junior subordinated debentures payable to Southern Capital Trust II (the "Trust"). The Trust was a grantor trust established by BancShares for the purpose of issuing trust preferred securities. The obligations of BancShares with respect to the issuance of the capital securities constituted a full and unconditional guarantee by BancShares of the Trusts' obligations with respect to the capital securities. The Trust was not consolidated with BancShares. Accordingly, BancShares did not report the securities issued by the Trust as liabilities, but instead reported the junior subordinated debentures issued by BancShares and held by the Trust as liabilities. However, prior to their redemption, BancShares had fully and unconditionally guaranteed the repayment of the trust preferred securities. The trust preferred securities qualified as Tier 1 capital for regulatory capital requirements of BancShares.

(Dollars in Thousands for Tabular Presentations)

Note 7. Short and Long-Term Borrowings (Continued)

On June 23 2021, BancShares completed its private placement of $80 million aggregate principal amount of its 3.125% Fixed-to-Floating Rate Subordinated Notes due June 30, 2031 and redeemable at the option of BancShares starting with the interest payment due June 30, 2026. Redemption is subject to obtaining the prior approval of the Federal Reserve to the extent such approval is then required under the rules of the Federal Reserve, or earlier upon the occurrence of certain events. After the initial 5 year fixed rate period the note will revert to the three month Secured Overnight Financing Rate ("SOFR") plus 241 basis points.

Also on June 23, 2021, BancShares completed its private placement of $10 million aggregate principal amount of its 2.625% Fixed-Rate Senior Notes due June 30, 2026 to an affiliated institution.

Total long-term borrowings averaged $88.9 million and $63.1 million for 2022 and 2021, respectively and the average cost was 3.24% and 4.28% for 2022 and 2021, respectively.

Note 8. Retirement Plans

Southern has a noncontributory, defined benefit pension plan which covers a substantial number of full-time employees. Southern discontinued offering benefits under the defined benefit plan to employees hired after June 30, 2012. Employees hired who met eligibility requirements on or before June 30, 2012 were allowed the option of continued participation in the defined benefit plan and the existing 401(k) plan or enrollment in an enhanced 401(k) plan, discussed further below. Employees who elected to enroll in the enhanced plan discontinued the accrual of additional years of service under the defined benefit plan. Under the plan, retirement benefits are based on years of service and average earnings. The plan's assets consist primarily of investments in fixed income securities and listed common stocks. It is Southern's policy to determine the service cost and projected benefit obligation using the Projected Unit Credit Cost method.

The following sets forth pertinent information regarding the projected benefit obligation of the pension plan for the periods indicated:

	2022	2021
Projected benefit obligation, beginning of year	$ 93,950	$ 94,936
Service cost	2,050	2,278
Interest cost	2,841	2,627
Actuarial gain	(26,249)	(2,372)
Benefits paid	(3,873)	(3,519)
Projected benefit obligation, end of year	$ 68,719	$ 93,950

The accumulated benefit obligation for the pension plan at the end of 2022 and 2021 was $62.4 million and $82.4 million, respectively. Southern uses a measurement date of December 31 for its pension plan.

The weighted average assumptions used to determine benefit obligations, at the end of the year were as follows:

	2022	2021
Discount rate	5.50%	3.00%
Rate of compensation increase	4.00%	4.00%

The change in pension plan assets is as follows:

	2022	2021
Fair value of plan assets, beginning of year	$ 112,065	$ 105,554
Actual return on plan assets	(21,447)	10,030
Benefits paid	(3,872)	(3,519)
Fair value of plan assets, end of year	$ 86,746	$ 112,065

(Dollars in Thousands for Tabular Presentations)

Note 8. Retirement Plans (Continued)

Employer contributions and benefits paid in the above table include only those amounts contributed directly to, or paid directly from, plan assets.

		2022		2021
Funded status, end of year				
Fair value of plan assets	$	86,746	$	112,065
Projected benefit obligation		(68,719)		(93,950)
Funded status		18,027		18,115
Amounts not yet recognized:				
Unrecognized net loss		-		-
Net amount recognized	$	18,027	$	18,115

		2022		2021
Amounts recognized in the consolidated balance sheets:				
Other assets	$	18,027	$	18,115
Amounts recognized in accumulated other comprehensive (loss) income, excluding income taxes, consist of:				
Net actuarial loss	$	(1,335)	$	66
Prior service cost		-		-
Accumulated other comprehensive (loss) income	$	(1,335)	$	66

The following table discloses the components of periodic benefit cost related to the pension plan for the years ended December 31, 2022 and 2021:

		2022		2021
Service cost	$	2,050	$	2,278
Interest cost		2,841		2,627
Expected return on plan assets		(4,423)		(4,838)
Amortization of net actuarial loss		1,021		2,149
Net periodic benefit cost	$	1,489	$	2,216

(Dollars in Thousands for Tabular Presentations)

Note 8. Retirement Plans (Continued)

Investment decisions regarding the plan's assets seek to achieve a favorable annual return through a diversified portfolio that will provide needed capital appreciation and cash flow to allow both current and future benefit obligations to be paid. The target asset mix may change if the objectives for the plan's assets or risk tolerance change or if a major shift occurs in the expected long-term risk and reward characteristics of one or more asset classes.

The asset allocation for Southern's pension plan at the end of 2022 and 2021, and the target allocation for 2023, by asset category, is as follows:

Asset category	Target Allocation for 2023	Percentage of Plan Assets at December 31, 2022	2021
Cash and cash equivalents	2%	2%	1%
Equity securities	35%	33%	34%
Debt securities	63%	65%	65%
Total	100%	100%	100%

Southern's investment strategy calls for earning an adequate return on assets while not exposing the assets to unnecessary risk. The plan's assets are primarily invested in marketable, fixed rate U. S. Government and corporate securities and marketable equity securities. The plan's target allocation was modified in recent years to increase the exposure to debt securities, while decreasing the exposure to equity securities.

The fair values of pension plan assets at December 31, 2022 and 2021, by asset category are as follows:

Asset Category	Fair value as of December 31,	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Target Allocation	Actual % of Plan Assets
2022						
Cash and cash equivalents	$ 1,329	$ 1,329	$ -	$ -	1%	2%
Equity securities:					35%	33%
Individual equities	3,742	3,742	-	-		
Mutual funds	7,995	7,995	-	-		
Exchange traded funds	17,267	17,267	-	-		
Debt securities:					64%	65%
Bonds	20,968	8,445	12,523	-		
Mutual funds	35,445	35,445	-	-		
Total pension assets	$ 86,746	$ 74,223	$ 12,523	$ -	100%	100%
2021						
Cash and cash equivalents	$ 1,211	$ 1,211	$ -	$ -	1%	1%
Equity securities:					55%	34%
Individual equities	6,111	6,111	-	-		
Mutual funds	15,720	15,720	-	-		
Exchange traded funds	16,818	16,818	-	-		
Debt securities:					44%	65%
Bonds	72,205	57,078	15,127	-		
Total pension assets	$ 112,065	$ 96,938	$ 15,127	$ -	100%	100%

(Dollars in Thousands for Tabular Presentations)

Note 8. Retirement Plans (Continued)

BancShares does not anticipate making any contributions to the plan during 2023. Estimated payments to pension plan participants in the indicated periods are as follows:

2023	$ 3,699
2024	3,927
2025	4,136
2026	4,243
2027	4,376
2028 - 2032	23,806

The weighted-average assumptions used to determine the net periodic benefit cost for the years ended December 31, 2022 and 2021 are as follows:

	2022	2021
Discount rate	3.00%	2.70%
Rate of compensation increase	4.00%	4.00%
Expected return on plan assets	4.75%	5.50%

The discount rates above reflect the discount in effect at January 1 of the plan year.

Employees hired before July 1, 2012 are also eligible to participate in a 401(k) plan through deferral of portions of their salary. Based on the employee's contribution, BancShares will match up to 100% of the first 3% of the participant's contributions and 50% of the next 3%. In addition, BancShares also offers an enhanced 401(k) plan for certain employees. BancShares will match 100% of the first 6% of the participant's contributions. In addition, BancShares may make discretionary contributions. BancShares made participating contributions of $2.8 million and $2.6 million during 2022 and 2021, repectively.

Note 9. Regulatory Requirements and Restrictions

BancShares is subject to regulations with respect to certain risk-based capital ratios. These risk-based capital ratios measure the relationship of capital to a combination of balance sheet and off-balance sheet risks. The values of both balance sheet and off-balance sheet items are adjusted based on the rules to reflect categorical credit risk. In addition to the risk-based capital ratios, the regulatory agencies have also established a leverage ratio for assessing capital adequacy. The leverage ratio is equal to Tier 1 capital divided by total consolidated on-balance sheet assets (minus amounts deducted from Tier 1 capital). The leverage ratio does not involve assigning risk weights to assets.

In July 2013, the Federal Reserve announced its approval of a final rule to implement the regulatory capital reforms developed by the Basel Committee on Banking Supervision ("Basel III"), among other changes required by the Dodd-Frank Wall Street Reform and Consumer Protection Act. The new rules became effective January 1, 2015, subject to a phase-in period for certain aspects of the new rules.

As applied to BancShares and Southern, the new rules include a new minimum ratio of common equity Tier 1 capital ("CET1") to risk-weighted assets of 4.5%. The new rules also raise the minimum required ratio of Tier 1 capital to risk-weighted assets from 4% to 6%. The minimum required leverage ratio under the new rules is 4%. The minimum required ratio of total capital to risk-weighted assets remains at 8% under the new rules.

In order to avoid restrictions on capital distributions and discretionary bonus payments to executives, under the new rules a covered banking organization will also be required to maintain a "capital conservation buffer" in addition to its minimum risk-based capital requirements. This buffer will be required to consist solely of common equity Tier 1, and the buffer will apply to all three risk-based measurements (CET1, Tier 1 capital and total capital). The capital conservation buffer was phased in annually over four years beginning January 1, 2016, at 0.625% of risk-weighted assets and increasing each subsequent year by an additional 0.625%. As fully phased in on January 1, 2019, the capital conservation buffer is 2.5% of risk-weighted assets.

Note 9. Regulatory Requirements and Restrictions (Continued)

Southern is also subject to the regulatory framework for prompt corrective action, which identifies five capital categories for insured depository institutions (well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized, and critically undercapitalized) and is based on specified thresholds for each of the three risk-based regulatory capital ratios (CET1, Tier 1 capital and total capital) and for the leverage ratio.

The following table presents actual and required capital ratios as of December 31, 2022 and 2021 for BancShares and Southern under the Basel III capital rules. The minimum required capital amounts presented include the minimum required capital levels as of January 1, 2019 when the Basel III Capital Rules have been fully phased-in. Capital levels required to be considered well capitalized are based upon prompt corrective action regulations, as amended to reflect the changes under the Basel III Capital Rules.

In April 2020, Southern began originating loans to qualified small businesses under the PPP administered by the SBA. Federal bank regulatory agencies have issued an interim final rule that permits banks to neutralize the regulatory capital effects of participating in the Paycheck Protection Program Lending Facility (the "PPP Facility") and clarify that PPP loans have a zero percent risk weight under applicable risk-based capital rules. Specifically, a bank may exclude all PPP loans pledged as collateral to the PPP Facility from its average total consolidated assets for the purposes of calculating its leverage ratio, while PPP loans that are not pledged as collateral to the PPP Facility will be included. Southern's PPP loans are included in the calculation of the leverage ratio as of December 31, 2022 and 2021 as Southern did not utilize the PPP Facility for funding purposes.

	Actual		Minimum for capital adequacy purposes		Required to be considered well capitalized	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
			(Dollars in thousands)			
December 31, 2022:						
Common equity Tier 1 to risk-weighted assets:						
BancShares	$ 442,676	11.651%	$ 170,975	4.500%	$ 246,963	6.500%
Southern	402,336	11.654%	155,363	4.500%	224,413	6.500%
Tier 1 capital to risk-weighted assets						
BancShares	442,676	11.651%	227,966	6.000%	303,955	8.000%
Southern	402,336	11.654%	207,151	6.000%	276,201	8.000%
Total capital to risk-weighted assets						
BancShares	503,833	14.452%	278,896	8.000%	348,620	10.000%
Southern	438,170	12.691%	276,199	8.000%	345,249	10.000%
Tier 1 capital to average assets (leverage ratio):						
BancShares	442,676	8.973%	197,341	4.000%	246,677	5.000%
Southern	402,336	8.352%	192,683	4.000%	240,853	5.000%
December 31, 2021:						
Common equity Tier 1 to risk-weighted assets:						
BancShares	$ 404,050	12.098%	$ 150,291	4.500%	$ 217,088	6.500%
Southern	365,101	12.266%	133,944	4.500%	193,474	6.500%
Tier 1 capital to risk-weighted assets						
BancShares	404,050	12.098%	200,388	6.000%	267,185	8.000%
Southern	365,101	12.266%	178,592	6.000%	238,122	8.000%
Total capital to risk-weighted assets						
BancShares	503,833	15.085%	267,197	8.000%	333,996	10.000%
Southern	394,410	13.251%	238,116	8.000%	297,645	10.000%
Tier 1 capital to average assets (leverage ratio):						
BancShares	404,050	8.978%	180,018	4.000%	225,022	5.000%
Southern	365,101	8.358%	174,731	4.000%	218,414	5.000%

BancShares and Southern had capital conservation buffers of 5.65% and 4.69%, respectively, at December 31, 2022. These buffers exceed the 2.5% requirement, and therefore, result in no limit on distributions.

Note 9. Regulatory Requirements and Restrictions (Continued)

The primary source of funds for the dividends paid by BancShares to its shareholders is dividends received from its banking subsidiary. Southern is restricted as to dividend payout by state laws applicable to banks and may pay dividends only out of retained earnings. Should at any time its surplus be less than 50% of its paid-in capital stock, Southern may not declare a dividend until it has transferred from retained earnings to surplus 25% of its undivided profits or any lesser percentage that may be required to restore its surplus to an amount equal to 50% of its paid-in capital stock. Additionally, dividends paid by Southern may be limited by the need to retain sufficient earnings to satisfy minimum capital requirements imposed by the FDIC. Dividends on BancShares' common shares may be paid only after dividends on preferred series B and C shares have been paid. Common share dividends are based upon BancShares' profitability and are paid at the discretion of the Board of Directors.

Management does not expect any of the foregoing restrictions to materially limit its ability to pay dividends comparable to those paid in the past.

Note 10. Commitments, Contingencies and Concentration of Credit Risk

In the normal course of business there are various commitments and contingent liabilities outstanding, such as guarantees, commitments to extend credit, etc., which are not reflected in the accompanying financial statements. Southern is party to financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers and to reduce its own exposure to fluctuations in interest rates. These financial instruments include commitments to extend credit, standby letters of credit and undisbursed advances on customer lines of credit. These instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the Consolidated Balance Sheets.

Southern is exposed to credit loss for the contractual notional amount of commitments to extend credit and standby letters of credit in the event of nonperformance by the other party to the financial instrument. Southern uses the same credit policies in making these commitments and conditional obligations as it does for on-balance-sheet instruments.

Commitments to extend credit and undisbursed advances on customer lines of 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 commitments expire without being drawn, the total commitment amounts do not necessarily represent future cash requirements. Southern evaluates each customer's credit worthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by Southern, upon extension of credit is based on management's credit evaluation of the borrower. Collateral held varies but may include trade accounts receivable, property, plant, and equipment and income-producing commercial properties.

Standby letters of credit are commitments issued by Southern to guarantee the performance of a customer to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loans to customers. The maximum potential amount of undiscounted future payments related to standby letters of credit at December 31, 2022 is $8.5 million. At December 31, 2022, BancShares considered this amount to be immaterial and has recorded no liability for the current carrying amount of the obligation to perform as a guarantor and no liability is considered necessary. Substantially all standby letters of credit are secured by real estate and/or guaranteed by third parties in the event BancShares had to advance funds to fulfill the guarantee.

Outstanding commitments to lend at December 31, 2022 and December 31, 2021 were $859.6 million and $687.1 million. Outstanding standby letters of credit and commitments to lend at December 31, 2022 generally expire within one year, whereas commitments associated with undisbursed advances on customer lines of credit at December 31, 2022 generally expire within one to five years.

Non-recourse commitments to sell loans amounted to $5.2 million and $26.5 million at December 31, 2022 and 2021, respectively. BancShares utilized investor commitments to protect its mortgage loans held for sale from interest rate risk from the time of origination to the time of sale. These commitments are accounted for at fair market value. Unfunded residential mortgage loan commitments for loans to be sold are also accounted for at fair market value. These fair market value adjustments were insignificant as of and for the years ended December 31, 2022 and 2021.

Southern is also committed to leases for banking facilities. See Note 4 – Premises and Equipment for lease commitments at December 31, 2022.

(Dollars in Thousands for Tabular Presentations)

Note 10. Commitments, Contingencies and Concentration of Credit Risk (Continued)

BancShares does not have any special purpose entities or other similar forms of off-balance sheet financing arrangements.

Southern grants agribusiness, commercial and consumer loans to customers primarily in eastern North Carolina and southeastern Virginia.

BancShares is also involved in various legal actions arising in the normal course of business. Management is of the opinion that the outcome of such actions will not have a material adverse effect on the consolidated financial position of BancShares.

Note 11. Parent Company Financial Statements

Presented below are the condensed balance sheets (parent company only) of Southern BancShares (N.C.), Inc. as of December 31, 2022 and 2021 and condensed statements of income and cash flows for the years then ended.

CONDENSED BALANCE SHEETS

	December 31, 2022	December 31, 2021
ASSETS		
Cash and cash equivalents	$ 20,659	$ 27,319
Investment in marketable equity securities at fair value	147,782	160,621
Investment securities available for sale, at fair value	7,460	8,028
Other assets	2,540	2,511
Investment in subsidiary	221,540	387,159
Total assets	$ 399,981	$ 585,638
LIABILITIES AND SHAREHOLDERS' EQUITY		
Accrued liabilites	$ 26,705	$ 29,826
Notes payable	88,993	88,874
Total liabilities	115,698	118,700
Shareholders' equity	284,283	466,938
Total liabilities and shareholders' equity	$ 399,981	$ 585,638

CONDENSED STATEMENTS OF INCOME

	Year Ended December 31, 2022	Year Ended December 31, 2021
Interest and dividend income	$ 1,216	$ 1,243
Dividends from bank subsidiary	5,500	5,550
Unrealized (losses) gains on marketable equity securities	(13,910)	46,364
Unrealized (losses) gains on investment securities available for sale	(568)	(176)
Gain on sale of investment securities	213	17
Total income	(7,549)	52,998
Interest expense	2,881	2,832
Other expense	453	448
Total expense	3,334	3,280
(Loss) income before income tax	(10,883)	49,718
Income tax (benefit) expense	(3,572)	8,690
Net (loss) income before equity in undistributed earnings of subsidiary	(7,311)	41,028
Equity in undistributed income of subsidiary	37,230	52,518
Net income	$ 29,919	$ 93,546

(Dollars in Thousands for Tabular Presentations)

Note 11. Parent Company Financial Statements (Continued)

CONDENSED STATEMENTS OF CASH FLOWS

	Year Ended December 31, 2022	2021
OPERATING ACTIVITIES:		
Net income	$ 29,919	$ 93,546
Adjustments to reconcile net income to net cash provided by operating activities:		
Equity in undistributed net income of subsidiary	(37,230)	(52,518)
Unrealized loss (gain) on marketable equity securities	13,910	(46,364)
Unrealized loss on investment securities available for sale	568	176
Gain on sale of investment securities available for sale	(212)	(17)
Amorization of debt issuance costs	119	59
Change in other assets	29	1,116
Change in accrued liabilities	(3,049)	8,094
NET CASH PROVIDED BY OPERATING ACTIVITIES	4,054	4,092
INVESTING ACTIVITIES:		
Purchases of marketable equity securities	(1,829)	(2,916)
Proceeds from sale of marketable equity securities	403	-
Proceeds from sale of investment securities available for sale	-	173
Investment in subsidiary	-	(25,815)
Other	-	711
NET CASH USED BY INVESTING ACTIVITIES	(1,426)	(27,847)
FINANCING ACTIVITIES:		
Proceeds from borrowed money	-	88,815
Payoff of borrowed funds	-	(37,921)
Dividends paid	(2,229)	(1,866)
Purchase and retirement or redemption of stock	(7,059)	(3,734)
NET CASH PROVIDED (USED) BY FINANCING ACTIVITIES	(9,288)	45,294
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(6,660)	21,539
CASH AND CASH EQUIVALENTS AT THE BEGINNING OF YEAR	27,319	5,780
CASH AND CASH EQUIVALENTS AT THE END OF YEAR	$ 20,659	$ 27,319
SUPPLEMENTAL DISCLOSURES OF CASH PAID DURING THE YEAR FOR:		
Interest	$ 2,881	$ 2,825

Note 12. Fair Value of Financial Instruments

BancShares utilizes fair value measurements to record fair value adjustments to certain assets and to determine fair value disclosures. Fair value estimates are made by management at specific points in time based on relevant information about the financial instrument and the market. These estimates do not reflect any premium or discount that could result from offering for sale at one time BancShares' entire holdings of a particular financial instrument nor are potential taxes and other expenses that would be incurred in an actual sale considered. Because no market exists for a significant portion of BancShares' financial instruments, fair value estimates are based on judgments regarding future expected loss experience, current economic conditions, risk characteristics of various financial instruments and other factors. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and therefore cannot be determined with precision. Changes in assumptions and/or the methodology used could significantly affect the estimates disclosed. Similarly, the fair values disclosed could vary significantly from amounts realized in actual transactions.

Fair value estimates are based on existing on- and off-balance sheet financial instruments without attempting to estimate the value of anticipated future business and the value of assets and liabilities that are not considered financial instruments. For example, BancShares has premises and equipment which are not considered financial instruments. Accordingly, the value of these assets has not been incorporated into the fair value estimates. In addition, tax ramifications related to the realization of the unrealized gains and losses can have a significant effect on fair value estimates and have not been considered in any of the estimates.

BancShares reports fair value on a recurring basis for certain financial instruments, most notably for available-for-sale investment securities and certain derivative instruments. BancShares may be required, from time to time, to measure certain assets at fair value on a nonrecurring basis. These include assets that are measured at the lower of cost or market that were recognized at fair value which was below cost at the end of the period. Assets subject to nonrecurring use of fair value measurements could include impaired loans, loans held for sale, goodwill, and OREO.

BancShares groups financial assets and financial liabilities measured at fair value in three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value. These levels are:

Level 1 – Valuations for assets and liabilities traded in active exchange markets, such as the New York Stock Exchange. Level 1 also includes U.S. Treasury, other U.S. government and agency mortgage-backed securities that are traded by dealers or brokers in active markets. Valuations are obtained from readily available pricing sources for market transactions involving identical assets or liabilities.

Level 2 – Valuations for assets and liabilities traded in less active dealer or broker markets. Valuations are obtained from third party services for similar or comparable assets or liabilities.

Level 3 – Valuations for assets and liabilities that are derived from other valuation methodologies, including option pricing models, discounted cash flow models and similar techniques, and not based on market exchange, dealer, or brokered traded transactions. Level 3 valuations incorporate certain assumptions and projections in determining the fair value assigned to such assets or liabilities.

Marketable equity securities are measured at fair value using observable closing prices. The valuation also considers the amount of market activity by examining the trade volume of each security. Equity securities are classified as Level 1 since they are traded in an active market.

Securities available for sale are valued on a recurring basis at quoted market prices where available. If quoted market prices are not available, fair values are based on quoted market prices of comparable securities. Level 1 securities include those traded on an active exchange, such as the New York Stock Exchange, or U.S. Treasury and agency mortgage-backed securities issued by government sponsored entities that are traded by dealers or brokers in active over-the-counter markets and money market funds. Level 2 securities include mortgage-backed securities issued by government-sponsored entities, obligations of states and political subdivisions and corporate debt securities. Securities classified as Level 3 include asset-backed securities in less liquid markets given that there is an absence of observable inputs for these and similar securities in the debt markets. For these securities, a present value approach that maximizes the use of relevant observable inputs and minimizes the use of unobservable inputs provides representative fair values, and therefore, has been used rather than a market valuation approach. This income valuation approach requires numerous steps in determining fair value. These steps include estimating credit quality of the collateral, generating asset defaults, forecasting cash flows for underlying collateral, and determining losses given default assumptions.

(Dollars in Thousands for Tabular Presentations)

Note 12. Fair Value of Financial Instruments (Continued)

BancShares is allowed to make an irrevocable election to measure certain financial instruments at fair value. The changes in fair value from one reporting period to the next period must be reported in the income statement with additional disclosures to identify the effect on net income. BancShares continued to account for securities available-for-sale at fair value as reported in prior years. BancShares has no derivative activity. Securities available-for-sale are reported on a recurring basis.

Assets and Liabilities Recorded at Fair Value on a Recurring Basis

	Market Value	Markets for Identical (Level 1)	Observable Inputs (Level 2)	Unobservable Inputs (Level 3)
December 31, 2022				
Marketable equity securities	$ 173,187	$ 173,187	$ -	$ -
Investment securities available for sale:				
U.S. Treasuries and government sponsored entities debt	$ 298,998	$ 298,998	$ -	$ -
Corporate debt securities	10,892	-	10,892	-
Obligations of states and political subdivisions	203,600	-	203,600	-
Government-sponsored mortgage-backed securities	866,630	-	866,630	-
Total	$ 1,380,120	$ 298,998	$ 1,081,122	$ -
December 31, 2021				
Marketable equity securities	$ 188,420	$ 188,420	$ -	$ -
Investment securities available for sale:				
U.S. Treasuries and government sponsored entities debt	$ 458,217	$ 458,217	$ -	$ -
Corporate debt securities	11,577	-	11,513	64
Obligations of states and political subdivisions	284,833	-	284,833	-
Government-sponsored mortgage-backed securities	858,665	-	858,665	-
Total	$ 1,613,292	$ 458,217	$ 1,155,011	$ 64

(Dollars in Thousands for Tabular Presentations)

Note 12. Fair Value of Financial Instruments (Continued)

Changes in Level 3 Fair Value Measurements

For those investment securities available-for-sale with fair values that are determined by reliance on significant unobservable inputs, the following table identifies the factors causing the change in fair values for the years ended December 31, 2022 and 2021:

	Investment Securities Available-For-Sale With Fair Values Based on Significant Unobservable Inputs
Beginning balance, January 1, 2021	$ 106
Total losses realized or unrealized:	
Included in other comprehensive (loss) income	(2)
Maturities and calls, net	(40)
Ending balance, December 31, 2021	64
Total losses realized or unrealized:	
Included in other comprehensive (loss) income	-
Maturities and calls, net	(64)
Ending balance, December 31, 2022	$ -

Assets and Liabilities Recorded at Fair Value on a Nonrecurring Basis

As previously discussed, loans are considered impaired when it is determined to be probable that all amounts due under the contractual terms of the loan will not be collected when due. Loans considered individually impaired are evaluated and a specific allowance is established, if required, based on the most appropriate of the three measurement methods: present value of expected future cash flows, fair value of collateral, or the observable market price of a loan method. A specific allowance is required if the fair value of the expected repayments or the collateral is less than the recorded investment in the loan. At December 31, 2022, $219,000 of impaired loans required a specific allowance of $5,000 and an additional $888,000 of impaired loans had partial charge-offs for a total of $1.1 million of impaired loans measured at fair value. At December 31, 2021, $264,000 of impaired loans required a specific allowance of $7,000 and $2.5 million of impaired loans had partial charge-offs for a total of $2.8 million of impaired loans measured at fair value. BancShares relies on Level 3 inputs to determine the fair value of these loans.

OREO is measured and reported at fair value using Level 3 inputs for valuations based on non-observable criteria. There was no OREO at December 31, 2022. As of December 31, 2021, OREO totaled $86,000.

At December 31, 2022 and 2021, BancShares had certain equity securities without a readily determinable market value, which were measured using the measurement alternative. Under the measurement alternative, these investments will be measured at cost, less any impairment, plus or minus changes resulting from observable price changes in orderly transactions for an identical or similar investment of the same issuer. During the year ending December 31, 2021, certain equity securities without a readily determinable market value had observable prices changes in orderly transactions, and as a result, the carrying value of these investments was adjusted. As a result, these investments are valued using Level 2 inputs. No such adjustments were recorded during the year ending December 31, 2022.

At December 31, 2022 and December 31, 2021, BancShares had certain impaired loans and OREO that are measured at fair value on a nonrecurring basis. BancShares applies discounts ranging between 6% and 15% for expected liquidation and sales costs to fair value estimates for impaired loans and OREO.

(Dollars in Thousands for Tabular Presentations)

Note 12. Fair Value of Financial Instruments (Continued)

Assets and Liabilities Recorded at Fair Value on a Nonrecurring Basis (Continued)

The tables below present the balances of assets and liabilities measured at fair value on a nonrecurring basis.

	Fair value	Quoted Prices in Active Markets for Instrument (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
2022				
Impaired loans	1,102	-	-	1,102
2021				
Equity securities without a readily determinable market value	$ 2,463	$ -	$ 2,463	$ -
Impaired loans	2,838	-	-	2,838
OREO	86	-	-	86

Certain assets are carried at fair value on a nonrecurring basis. Loans held for sale are carried at the lower of aggregate cost or fair value and are therefore carried at fair value only when fair value is less than the asset cost. The values of loans held for sale are based on prices observed for similar pools of loans. There have been no fair value adjustments recorded for loans held for sale at December 31, 2022 and 2021. No financial liabilities were carried at fair value on a nonrecurring basis as of December 31, 2022 or December 31, 2021.

Fair Value of Financial Instruments

The following methods and assumptions were used to estimate the fair value of each class of financial instrument:

Cash and due from banks, Interest–bearing deposits with banks, Certificates of deposit with banks, Accrued interest receivable, Short-term borrowings, and Accrued interest payable - The carrying amounts for cash and due from banks, interest-bearing deposits with banks, certificates of deposits with banks, accrued interest receivable, short-term borrowings, and accrued interest payable are equal to their fair values due to the short-term nature of these financial instruments. These items are considered Level 1.

Marketable equity securities - Equity securities are measured at fair value using observable closing prices, and therefore are classified as Level 1.

Investment securities available for sale - Fair values of investment securities are based on quoted market prices. If a quoted market price is not available, fair value is estimated using quoted market prices for similar securities and as a result are classified as Level 2. Certain asset-backed securities in less liquid markets with no observable inputs or similar securities in the debt markets are valued using a present value approach that maximizes the use of relevant observable inputs and minimizes the use of unobservable inputs. These securities are considered Level 3.

Loans held for sale - Fair value for loans held for sale is generally based on market prices for loans with similar characteristics or external valuations. Loans held for sale are classified as Level 2.

Loans - Fair value of loans is an estimate of exit price. Exit price is estimated based on a discounted future cash flow analysis using estimated credit losses expected to be incurred over the remaining life of the loans and current interest rates offered on loans with similar terms and credit quality. The inputs used in the fair value measurements for loans and leases are considered Level 3 inputs.

Stock in Federal Home Loan Bank of Atlanta - The carrying amount for Federal Home Loan Bank of Atlanta stock is equal to the fair value due to the redemption provisions of the stock and no ready available market for such stock. Federal Home Loan Bank of Atlanta stock is considered Level 1.

Deposits **-** The fair value of demand deposits, savings accounts and money market deposits is the amount payable on demand at year end. The fair value of certificates of deposit is estimated by discounting the future cash flows using the current rates paid for similar deposits. Deposits are considered Level 2.

(Dollars in Thousands for Tabular Presentations)

Note 12. Fair Value of Financial Instruments (Continued)

Fair Value of Financial Instruments (Continued)

Long-term borrowings - The fair value of long-term borrowings reflects discounting future cash flows using the current interest rates for similar maturities. Long-term borrowings are considered Level 2.

Commitments - Southern's commitments to extend credit have no carrying value and are generally at variable rates and/or have relatively short terms to expiration. Accordingly, these financial instruments are deemed to have no material fair value.

The estimated fair values of BancShares' financial instruments at December 31 are as follows:

	2022		2021	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Financial assets:				
Cash and due from banks	$ 21,253	$ 21,253	$ 35,106	$ 35,106
Interest-bearing deposits with banks	115,986	115,986	138,469	138,469
Certificates of deposits with banks	2,600	2,600	11,946	11,946
Marketable equity securities	173,187	173,187	188,420	188,420
Investment securities available-for-sale	1,380,120	1,380,120	1,613,292	1,613,292
Loans held for sale	2,978	2,978	15,126	15,126
Loans, net of allowance	2,814,533	2,646,456	2,410,240	2,400,068
Stock in Federal Home Loan Bank of Atlanta	8,796	8,796	1,855	1,855
Accrued interest receivable	14,688	14,688	12,034	12,034
Financial liabilities:				
Deposits	$ 4,125,982	$ 4,122,712	$ 3,919,183	$ 3,918,139
Short-term borrowings	208,061	208,047	63,670	63,670
Long-term borrowings	88,993	74,945	88,874	88,311
Accrued interest payable	411	411	155	155

Note 13. Related Parties

One of BancShares' directors is an executive officer, a significant shareholder, and a director of First Citizens BancShares, Inc. At December 31, 2022 the director beneficially owned 8,094 shares, or 10.37%, of BancShares' outstanding common stock and 2,000 shares, or 0.79%, of BancShares' outstanding Series B preferred stock. A sibling of that director, who is also a director of BancShares, beneficially owns 6,881 shares, or 8.82%, of BancShares' outstanding common stock.

BancShares has entered into various service contracts with First Citizens BancShares, Inc. and its subsidiary, First-Citizens Bank & Trust Company (collectively "First Citizens"). The following table lists the various charges paid to and income received from First Citizens during the years ended December 31:

	2022	2021
Income from credit cards	$ 205	$ 171
Trustee for employee benefit plans	414	481

BancShares also has a correspondent relationship with First Citizens. Correspondent account balances with First Citizens included in cash and due from banks totaled $184,000 and $237,000 at December 31, 2022 and 2021, respectively. In addition, BancShares had sold to First Citizens loan participations of $2.7 million and $3.1 million as of December 31, 2022 and 2021, respectively.

Note 13. Related Parties (Continued)

BancShares also owns stock and debt securities in First Citizens as follows:

	2022			2021		
	Number of shares	Amortized Cost	Fair Value	Number of shares	Amortized Cost	Fair Value
	($ in thousands)					
First Citizens						
Class A	191,963	$ 15,322	$ 145,577	191,963	$ 15,322	$ 159,299
Class B	22,619	532	15,200	22,619	532	16,648
Preferred	198,945	4,480	3,875	198,945	4,480	5,202
Total equity securites	413,527	20,334	164,652	413,527	20,334	181,149
Investment securities available for sale at fair value	-	7,900	7,460	-	7,900	8,028
Total First Citizens securities	413,527	$ 28,234	$ 172,112	413,527	$ 28,234	$ 189,177

BancShares is also related through common ownership with Fidelity BancShares (N.C.), Inc., (“Fidelity”) in that the aforementioned significant shareholders of BancShares and certain of their related parties are also significant shareholders of Fidelity. At December 31, 2022 and 2021 BancShares had $7.5 million and $8.5 million, respectively in loan participations sold to Fidelity. Fidelity has also contracted with BancShares to service, on Fidelity’s behalf, $4,000 and $6,000 of Fidelity’s mortgage loans at December 31, 2022 and 2021, respectively. Also, as discussed further in Note 7, Fidelity purchased $10 million of senior notes issued by BancShares during 2021.

(Dollars in Thousands for Tabular Presentations)

Note 14. Accumulated Other Comprehensive Income (Loss)

Accumulated other comprehensive income (loss) included the following as of December 31:

	2022			2021		
	Accumulated other comprehensive loss	Deferred tax benefit (expense)	Accumulated other comprehensive loss net of tax	Accumulated other comprehensive loss	Deferred tax benefit (expense)	Accumulated other comprehensive loss net of tax
Unrealized gains (losses) on debt securities available for sale	$ (267,873)	$ 58,553	$ (209,320)	$ (3,716)	$ 841	$ (2,875)
Defined benefit pension plan	1,335	(284)	1,051	(66)	16	(50)
State tax rate adjustment	-	-	2,057	-	-	-
Total	$ (266,538)	$ 58,269	$ (206,212)	$ (3,782)	$ 857	$ (2,925)

	Unrealized gains and losses on available-for-sale securities	Defined benefit pension plan	Total
Balance at January 1, 2021	$ 18,810	$ (7,563)	$ 11,247
Other comprehensive income before reclassifications	(21,287)	5,849	(15,438)
Amounts reclassified from accumulated other comprehensive income (loss)	(398)	1,664	1,266
Net current period other comprehensive income	(21,685)	7,513	(14,172)
Balance at December 31, 2021	(2,875)	(50)	(2,925)
Other comprehensive income (loss) before reclassifications	(203,747)	(420)	(204,167)
Amounts reclassified from accumulated other comprehensive income (loss)	94	786	880
Net current period other comprehensive income (loss)	(203,653)	366	(203,287)
Balance at December 31, 2022	$ (206,528)	$ 316	$ (206,212)

During 2022, the net deferred tax benefit related to the change in net unrealized losses on debt securities available for sale was calculated by reference to state income tax rates that are projected to be in effect in the periods in which the related financial instrument either matures or is expected to be called by the issuer. The difference between the deferred tax benefit and the accumulated other comprehensive loss calculated by reference to the current state income tax rate is shown as the state tax rate adjustment within the preceeding table.

(Dollars in Thousands for Tabular Presentations)

Note 14. Accumulated Other Comprehensive Income (Loss) (Continued)

The following table represents the amounts reclassified from accumulated other comprehensive income (loss) and the line items affected in the statement where net income is presented for the twelve months ended December 31, 2022 and 2021:

	Year ended December 31, 2022	
Details about accumulated other comprehensive income	Amount reclassified from accumulated other comprehensive income	Affected line item in the statement where net income is presented
Unrealized gains and losses on available-for-sale debt securities	$ 122	Investment securities gains, net
	(28)	Income taxes
	$ 94	Net income
Amortization of defined benefit plan		
Actuarial losses	$ 1,021	Other noninterest expense
	(235)	Income taxes
	$ 786	Net income
Total reclassifications for the period	$ 880	

	Year ended December 31, 2021	
Details about accumulated other comprehensive income	Amount reclassified from accumulated other comprehensive income	Affected line item in the statement where net income is presented
Unrealized gains and losses on available-for-sale debt securities	$ (514)	Investment securities gains, net
	116	Income taxes
	$ (398)	Net income
Amortization of defined benefit plan		
Actuarial losses	$ 2,149	Other noninterest expense
	(485)	Income taxes
	$ 1,664	Net income
Total reclassifications for the period	$ 1,266	

Note 15. Subsequent Events

On March 20, 2023, Southern entered into a 3-year $100 million interest rate swap to synthetically convert a portfolio of fixed-rate municipal securities to a variable rate. This transaction seeks to minimize the interest rate risk on our consolidated balance sheet by protecting against rising interest rates. Management anticipates the interest rate swap will qualify for hedge accounting.

Management has evaluated subsequent events through March 27, 2023, the date the consolidated statements were available to be issued and, other than the event noted above, there have been no material subsequent events.