Report of Independent Auditors
and Consolidated Financial Statements

U & I Financial Corp. and Subsidiary

December 31, 2022 and 2021

MOSSADAMS

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Report of Independent Auditors

The Board of Directors and Shareholders of
U & I Financial Corp. and Subsidiary

Report on the Audit of the Financial Statements

Opinion

We have audited the consolidated financial statements of U & I Financial Corp. and Subsidiary, which comprise the consolidated statements of financial condition as of December 31, 2022 and 2021, and the related consolidated statements of income, comprehensive income, changes in shareholders' equity, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

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

Basis for Opinion

We conducted our audits in accordance with auditing standards generally accepted in the United States of America (GAAS). Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report. We are required to be independent of U & I Financial Corp. and Subsidiary 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 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 financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about U & I Financial Corp. and Subsidiary's ability to continue as a going concern within one year after the date that the financial statements are issued.

Auditor's Responsibilities for the Audit of the 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 financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of U & I Financial Corp. and Subsidiary's internal control. Accordingly, no such opinion is expressed.
- Evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the financial statements.
- Conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about U & I Financial Corp. and Subsidiary'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.

Moss Adams LLP

Everett, Washington
March 30, 2023

Consolidated Financial Statements

U & I Financial Corp. and Subsidiary
Consolidated Statements of Financial Condition
(dollars in thousands)
December 31, 2022 and 2021

	2022	2021
ASSETS		
ASSETS		
Cash and cash equivalents	$ 42,003	$ 31,096
Securities available-for-sale, at fair value	48,527	55,024
Loans receivable, net of allowance for loan losses of $4,580 and $4,575 at December 31, 2022 and 2021, respectively	454,441	321,765
Loans held for sale	12,527	20,783
Other investments	2,432	1,800
Premises and equipment, net	5,576	5,466
Right-of-use asset	1,406	1,724
Bank-owned life insurance	13,996	13,679
Accrued interest receivable	1,755	1,123
Servicing asset, net	2,385	2,400
Deferred tax asset	1,198	287
Other assets	484	536
Total assets	$ 586,730	$ 455,683
LIABILITIES AND SHAREHOLDERS' EQUITY		
LIABILITIES		
Deposits		
Noninterest-bearing	$ 117,491	$ 98,487
Interest-bearing		
Savings	14,042	16,348
Money market accounts and NOW	213,272	182,612
Time deposits	143,449	76,933
Total deposits	488,254	374,380
Borrowings	22,000	10,000
Lease liability	1,406	1,724
Accrued interest payable	316	24
Other liabilities	2,731	2,438
Total liabilities	514,707	388,566
SHAREHOLDERS' EQUITY		
Preferred stock, $1,000 par value; 5,500 shares authorized; no shares issued and outstanding at December 31, 2022 and 2021	-	-
Common stock - no par value; 10,000,000 shares authorized; 5,441,343 and 5,562,025 shares issued and outstanding at December 31, 2022 and 2021, respectively	30,955	30,016
Retained earnings	42,725	35,331
Accumulated other comprehensive (loss) income, net of tax	(1,657)	1,770
Total shareholders' equity	72,023	67,117
Total liabilities and shareholders' equity	$ 586,730	$ 455,683

See accompanying notes.

U & I Financial Corp. and Subsidiary
Consolidated Statements of Income
(dollars in thousands, except per share amounts)
Years Ended December 31, 2022 and 2021

	2022	2021
INTEREST INCOME		
Interest and fees on loans	$ 23,949	$ 16,445
Interest on securities	1,404	1,300
Interest on interest earning deposits with other banks	447	30
Interest on other investments	114	89
Total interest income	25,914	17,864
INTEREST EXPENSE		
Interest on deposits	2,750	723
Interest on borrowings	236	24
Total interest expense	2,986	747
Net interest income before provision for loan losses	22,928	17,117
PROVISION FOR LOAN LOSSES	-	-
Net interest income after provision for loan losses	22,928	17,117
NONINTEREST INCOME		
Service charges on deposit accounts	268	175
Gain on sale of loans	2,512	3,656
Other income	913	1,323
Total noninterest income	3,693	5,154
NONINTEREST EXPENSES		
Salaries and employee benefits	8,447	8,265
Occupancy and equipment	1,113	1,026
Professional fees, net	784	453
Data processing and communication	453	381
State B&O tax	416	412
Directors' expenses	197	225
Other	1,378	1,013
Total noninterest expenses	12,788	11,775
Income before income tax provision	13,833	10,496
INCOME TAX PROVISION	2,704	1,994
NET INCOME	$ 11,129	$ 8,502
Earnings per common share		
Basic	$ 2.03	$ 1.53
Diluted	$ 1.97	$ 1.49

See accompanying notes.

U & I Financial Corp. and Subsidiary
Consolidated Statements of Comprehensive Income
(dollars in thousands)
Years Ended December 31, 2022 and 2021

	2022	2021
NET INCOME	$ 11,129	$ 8,502
Other comprehensive loss, net of tax		
Unrealized loss on securities available-for-sale		
Unrealized holding loss, net of tax expense benefit of $911 and $175, respectively	(3,427)	(659)
Other comprehensive loss, net of tax	(3,427)	(659)
COMPREHENSIVE INCOME	$ 7,702	$ 7,843

See accompanying notes.

U & I Financial Corp. and Subsidiary
Consolidated Statements of Changes in Shareholders' Equity
(dollars in thousands, except share amounts)
Years Ended December 31, 2022 and 2021

	Preferred Stock		Common Stock		Retained Earnings	Accumulated Other Comprehensive (Loss) Income	Total Shareholders' Equity
	Shares	Amount	Shares	Amount			
BALANCE, December 31, 2020	-	$ -	5,578,990	$ 29,464	$ 27,192	$ 2,429	$ 59,085
Share-based compensation	-	-	-	459	-	-	459
Stock options exercised	-	-	17,735	93	-	-	93
Common stock repurchased	-	-	(34,700)	-	(363)	-	(363)
Net income	-	-	-	-	8,502	-	8,502
Other comprehensive loss, net of tax	-	-	-	-	-	(659)	(659)
BALANCE, December 31, 2021	-	-	5,562,025	30,016	35,331	1,770	67,117
Share-based compensation	-	-	-	281	-	-	281
Stock options exercised	-	-	107,038	658	-	-	658
Cash dividends	-	-	-	-	(1,099)		(1,099)
Common stock repurchased	-	-	(227,720)	-	(2,636)	-	(2,636)
Net income	-	-	-	-	11,129	-	11,129
Other comprehensive loss, net of tax	-	-	-	-	-	(3,427)	(3,427)
BALANCE, December 31, 2022	-	$ -	5,441,343	$ 30,955	$ 42,725	$ (1,657)	$ 72,023

See accompanying notes.

U & I Financial Corp. and Subsidiary
Consolidated Statements of Cash Flows
(dollars in thousands)
Years Ended December 31, 2022 and 2021

	2022	2021
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	$ 11,129	$ 8,502
Adjustments to reconcile net income to net cash from operating activities		
Depreciation and amortization	267	257
Increase in cash surrender value of bank-owned life insurance	(317)	(316)
Accretion of premiums and discounts on investment securities	336	335
Stock compensation expense	281	459
Proceeds from sales of loans	31,242	34,367
Origination of loans held-for-sale	(20,474)	(44,804)
Gain on sale of loans	(2,512)	(3,656)
Deferred income tax provision (benefit)	11	(479)
Servicing asset capitalized	(846)	(1,151)
Servicing asset amortization	861	737
Changes in operating assets and liabilities		
Change in accrued interest receivable	(632)	593
Change in other assets	41	158
Change in accrued interest payable	292	(10)
Change in other liabilities	293	897
Net cash from operating activities	19,972	(4,111)
CASH FLOWS FROM INVESTING ACTIVITIES		
Net change in loans receivable	(132,676)	(31,717)
Change in interest-bearing deposits in other financial institutions	-	2,747
Proceeds from matured, called, and principal repayment of securities available for sale	2,323	1,763
Purchase of securities available for sale	(500)	-
Purchases of other investments	(632)	(1,183)
Purchases of premises and equipment, net	(377)	(133)
Net cash from investing activities	(131,862)	(28,523)
CASH FLOWS FROM FINANCING ACTIVITIES		
Net change in deposits	113,874	36,811
Proceeds from Federal Home Loan Bank advances, net	12,000	5,000
Proceeds from exercise of stock options	658	93
Cash divided paid on common stock	(1,099)	-
Repurchases of common stock	(2,636)	(363)
Net cash from financing activities	122,797	41,541
NET CHANGE IN CASH AND CASH EQUIVALENTS	10,907	8,907
CASH AND CASH EQUIVALENTS, beginning of year	31,096	22,189
CASH AND CASH EQUIVALENTS, end of year	$ 42,003	$ 31,096
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION		
Cash paid during the year for		
Interest paid	$ 2,694	$ 757
Income taxes paid	$ 2,620	$ 1,950
NONCASH INVESTING ACTIVITIES		
Unrealized loss on securities available for sale	$ (4,338)	$ (834)
Addition to right of use asset obtained from new operating lease liabilities	$ -	$ 1,638
Reclassification of loans held for sale to loans receivable	$ 15,788	$ -

See accompanying notes.

Note 1 – Summary of Significant Accounting Policies

UniBank (the Bank) is a Washington state–chartered commercial bank, which was incorporated on September 1, 2006, and opened for business on November 1, 2006. The Bank provides general business banking services, including deposits and loans, and specializes in government guaranteed lending programs with its market encompassing the Asian American Communities of King, Snohomish, and Pierce counties in Washington state and certain markets in the West Coast and Sun Belt states. The principal office and full-service branch is located at 19315 Hwy. 99, Lynnwood, Washington, 98036. In addition, the Bank has branches in Tacoma, Bellevue, and Federal Way, Washington, as well as a loan production office in Atlanta, Georgia.

U & I Financial Corp. was issued a certificate of incorporation in the state of Washington on August 19, 2010. On September 10, 2010, the Federal Reserve Board granted authority to U & I Financial Corp. to become a bank holding company through a reorganization of the ownership interests of UniBank. The Washington Department of Financial Institutions Divisions of Banks approved the articles of share exchange and plan of share exchange and issued a certificate of reorganization.

The consolidated financial statements include the transactions of U & I Financial Corp. and its wholly owned subsidiary, UniBank (collectively, the Company). All significant intercompany transactions have been eliminated in consolidation.

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

Operating segments – The Company is managed as a legal entity and not by lines of business. The operations include commercial banking services, such as lending activities, deposit products, and other cash management services.

Use of estimates in the preparation of financial statements – The preparation of the consolidated financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, and the reported amounts of revenues and expenses during the reporting period. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the valuation of the allowance for loan losses, fair value of financial instruments, and deferred income taxes. Actual results could differ from those estimates.

Concentration of credit risk – Assets and liabilities that subject the Company to concentration of credit risk consist of investments, loans and deposits. Most of the Company’s customers are located within Snohomish County, King County, Pierce County, and the surrounding areas. The types of securities that the Company invests in are discussed in Note 2 and the Company’s primary lending products are discussed in Note 3. The Company did not have any significant concentrations to any one customer. The Company obtains what it believes to be sufficient collateral to secure potential losses. The extent and value of the collateral varies depending on the details underlying each loan agreement.

At times, the Company has cash and interest-bearing deposits in other banks in excess of the Federal Deposit Insurance Corporation (FDIC)-insured limits. The Company places these deposits with major financial institutions and monitors the financial condition of these institutions.

Cash and cash equivalents – Cash and cash equivalents include cash and due from banks, and term and overnight federal funds sold, all of which have original maturities less than 90 days.

Restricted cash – Zions Bank required a minimum balance of $250,000 as of December 31, 2022 and 2021, respectively, related to a line of credit (Note 9). The Pacific Coast Banker's Bank required a minimum balance of $250,000 as of December 31, 2022 and 2021, related to a line of credit (Note 9). These balances are included in cash and cash equivalents.

Investment securities – Investment securities are classified into one of three categories: (1) held-to-maturity, (2) available-for-sale, or (3) trading. The Company had no trading securities or held-to-maturity securities as of December 31, 2022 and 2021. Investment securities are categorized as held-to-maturity when the Company has the positive intent and ability to hold those securities to maturity. Securities that are held-to-maturity are stated at cost and adjusted for amortization of premiums and accretion of discounts, which are recognized as adjustments to interest income.

Investment securities categorized as available-for-sale are generally held for investment purposes (to maturity), although unanticipated future events may result in the sale of some securities. Available-for-sale securities are recorded at estimated fair value, with the net unrealized gain or loss included in comprehensive income, net of the related tax effect. Realized gains or losses on dispositions are based on the net proceeds and the adjusted carrying amount of securities sold, using the specific identification method. Amortizations of premiums are recognized in interest income over the period to call date. Accretions of discounts are recognized in interest income over the period to maturity.

Management reviews investment securities on an ongoing basis for the presence of other-than-temporary impairment (OTTI) or permanent impairment, taking into consideration current market conditions; fair value in relationship to cost; extent and nature of the change in fair value; issuer rating changes and trends; whether to sell the security before recovery of the amortized cost basis of the investment, which may be maturity; and other factors. For debt securities, if management intends to sell the security or it is likely that the Company will be required to sell the security before recovering its cost basis, the entire impairment loss would be recognized in earnings as an OTTI. If management does not intend to sell the security and it is not likely that the Company will be required to sell the security, but management does not expect to recover the entire amortized cost basis of the security, only the portion of the impairment loss representing credit losses would be recognized in earnings. The credit loss on a security is measured as the difference between the amortized cost basis and the present value of the cash flows expected to be collected. Projected cash flows are discounted by the original or current effective interest rate depending on the nature of the security being measured for potential OTTI. The remaining impairment related to all other factors, i.e., the difference between the present value of the cash flows expected to be collected and fair value, is recognized as a charge to other comprehensive income. Impairment losses related to all other factors are presented as separate categories within other comprehensive income.

Other investments – Other investments on the balance sheet consists of direct equity investments in stock of the Federal Reserve Bank of San Francisco (FRB), the Federal Home Loan Bank of Des Moines (FHLB), and investment in an equity fund.

As a Federal Reserve member bank, the Company is required to subscribe to Federal Reserve Stock. The par value of the stock is $100 per share of which one-half will be subject to call when deemed necessary by the Board of Governors of the Federal Reserve System. The recorded amount of the FRB stock equals its fair value because the shares can be redeemed only by the FRB at the par value. The Company's investment in FRB stock totaled $950,000 and $916,000 as of December 31, 2022 and 2021, respectively.

The Company, as a member of the FHLB, is required to maintain an investment in capital stock of FHLB in an amount equal to 4% of advances outstanding. The Company's investment in FHLB stock totaled $1,427,000 and $885,000 as of December 31, 2022 and 2021, respectively. FHLB stock is carried at cost and classified as a restricted security. Both cash and stock dividends received are reported as dividend income. The Company evaluates FHLB stock for impairment. The determination of whether these investments are impaired is based on the Company's assessment of the ultimate recoverability of cost, rather than by recognizing temporary declines in value. The determination of whether a decline affects the ultimate recoverability of cost is influenced by criteria such as (1) the significance of any decline in net assets of the FHLB as compared with the capital stock amount for the FHLB and the length of time this situation has persisted; (2) commitments by the FHLB to make payments required by law or regulation and the level of such payments in relation to the operating performance of the FHLB; (3) the impact of legislative and regulatory changes on institutions and, accordingly, the customer base of the FHLB; and (4) the liquidity position of the FHLB. Based on the above, the Company has determined that there is not an other-than-temporary impairment on the FHLB stock investment as of December 31, 2022 or 2021.

During the year ended December 31, 2022, the Company entered into an agreement with an investment fund designed to help accelerate technology adoption at banks. The Company committed up to $250,000 in capital for the fund, however, the Company is not obligated to fund the commitment prior to a capital call. During the year, the Company contributed $55,000. This equity investment does not have a readily determinable fair value and is held at cost minus impairment, if any. This method will be applied until the investment does not qualify for the measurement election (e.g., if the investment has a readily determinable fair value).

Bank-owned life insurance (BOLI) – The Bank owns bank-owned life insurance for various individuals in management positions. The carrying amount of the life insurance approximates fair value. Fair value of life insurance is estimated using the cash surrender value, less applicable surrender charges. The change in the cash surrender value is included in noninterest income. At December 31, 2022 and 2021, the BOLI had a total cash surrender value of $13,996,000 and $13,679,000, respectively.

Loans held-for-sale – Certain Small Business Administration (SBA) and United States Department of Agriculture (USDA) loans that may be sold prior to maturity are designated as held-for-sale at origination and are recorded at the lower of cost or market, determined on an aggregate basis. A valuation allowance is established if the market value of such loans is lower than their cost, and operations are charged or credited for valuation adjustments. The Company typically sells the guaranteed portion of the SBA or USDA loan and retains the unguaranteed portion.

Loans – Loans that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are reported at the principal balance outstanding, net of deferred loan fees and unearned income. Interest revenue on loans is generally accrued based on the principal amount outstanding. The accrual of interest on loans is discontinued when the payment of principal or interest is considered to be in doubt, or when a loan becomes contractually past due by 90 days or more with respect to principal or interest, unless the credit is well secured and in the process of collection. When a loan is placed on nonaccrual status, any accrued but uncollected interest is reversed from current income. Subsequent payments received, in general, on nonaccrual loans are recorded as principal reductions. Nonaccrual loans may be restored to accrual status when principal and interest become current and full repayment is expected.

Loan origination fees are deferred and amortized as yield adjustments over the contractual lives of the related loans. Other loan fees and charges, representing service costs for the prepayment of loans, delinquent payments, or miscellaneous loan services, are recorded as income when collected.

Allowance for loan losses – The allowance for loan losses is maintained at a level considered adequate to absorb potential losses in the loan portfolio. The allowance for loan losses is increased by charges to income and decreased by charge-offs. Subsequent recoveries, if any, are credited to the allowance. The adequacy of the allowance is determined by management based on evaluation and review of the loan portfolio considering loan loss experience, current economic conditions, changes in the composition of the loan portfolio, and other risk factors. The Company also maintains an unallocated allowance amount to provide for uncertainties inherent in a loan portfolio that could affect management's estimate of probable losses. Allocations of the allowance may be made for specific loans, but the entire allowance is available for any loan that, in management's judgment, should be charged off.

The Company considers a loan as impaired when it is probable that all amounts due (principal plus interest) will not be collected according to the contractual terms of the loan agreement. Factors considered by management include payment status, collateral value, and probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower.

The allowance for impaired loans is determined based on the present value of estimated cash flows or on the fair value of the collateral if the loan is collateral-dependent. Although management uses available information to recognize losses on loans, because of uncertainties associated with local economic conditions, collateral values, and future cash flows on impaired loans, it is reasonably possible that a material change could occur in the allowance for loan losses in the near term.

Various regulatory agencies, as an integral part of their examination processes, periodically review the Company's allowance for loan losses. Such agencies may require the Company to recognize additional losses based on their judgments using information available to them at the time of their examination.

Loan sales and servicing – When the Company sells the guaranteed portion of SBA or USDA loans, it generally retains the rights to service them. The Company initially records an asset representing the right to service loans at fair value, which is calculated by discounting the future cash flows from servicing at the discount rate that approximates the current market rate and discounting the future estimated prepayment speeds. This value is then carried and amortized in proportion to, and over the period of, the estimated net servicing income. As the servicing rights should be carried at the lower of cost or market, for the purposes of evaluating and measuring impairment, they are periodically reevaluated based on current prepayment speeds and market discount rates. Any impairment is measured as the amount by which the carrying value of servicing rights for a stratum exceeds its fair value.

The cash proceeds from sale equal the principal amount of loans and the respective premiums, reflective of the adjusted yield to the investor based on the current market rates. Because the portion retained does not carry an SBA or USDA guarantee, a discount is recorded on the retained portion of the loan and accreted into interest income.

Premises and equipment – Premises and equipment are stated at cost, less accumulated depreciation and amortization. Depreciation is provided using the straight-line method over three to 39 years (leasehold improvements are amortized over the lesser of the useful life or the terms of the respective leases). Repairs and maintenance are charged to operating expenses as incurred.

Leases – The Company accounts for leases in accordance with Financial Accounting Standards Board (FASB) Accounting Standards Update (ASU) No. 2016-02, *Leases* (Topic 842), recognizing on the balance sheet the assets and liabilities arising from operating leases. Accordingly, the Company recognizes a liability to make lease payments and a right-of-use (ROU) asset representing the right to use the underlying asset for the lease term.

Impairment of long-lived assets – Long-lived assets are evaluated for impairment whenever events or changes in circumstances indicate that the carrying value of an asset may not be recoverable. No impairment loss was recognized in 2022 or 2021.

Other real estate owned (OREO) – Assets acquired through or in lieu of loan foreclosure are held-for-sale and are initially recorded at lower of cost or estimated fair value, less cost to sell, at the date of foreclosure. Losses arising from the acquisition of property, in full or partial satisfaction of loans, are charged to the allowance for loan losses. Subsequent to foreclosure, valuations are periodically performed by management and the assets are carried at the lower of carrying amount or fair value less cost to sell. Revenue and expenses from operations and changes in the valuation allowance are included in noninterest expense. There were no OREO assets during 2022 or 2021.

Share-based compensation – The Company measures the cost of employee services received in exchange for an award of share-based compensation based on the grant-date fair value of the award. The cost is recognized over the requisite service period, except for awards granted to retirement-eligible employees, which are fully expensed by the grant date.

Income taxes – The Company records its provision for income tax under the liability method. Deferred tax assets and liabilities are reflected at currently enacted income tax rates applicable to the period in which the deferred tax assets or liabilities are expected to be realized or settled. As changes in tax laws or rates are enacted, deferred tax assets and liabilities are adjusted through the provision for income taxes. Deferred taxes result from temporary differences in the recognition of certain income and expense amounts between the Company's consolidated financial statements and its tax returns.

Earnings per common share – Basic earnings per common share (EPS) are computed by dividing net income available to common shareholders by the weighted-average number of common shares outstanding during the period. Diluted earnings per share reflect the weighted-average potential dilution that could occur if all potentially dilutive shares or other commitments to issue common stock were exercised or converted into common stock using the treasury stock method.

Comprehensive income – Comprehensive income includes all changes in shareholders' equity during a period, except those resulting from transactions with shareholders. Besides net income, other components of comprehensive income include the net-of-tax effect of changes in the net unrealized gain or loss on securities available-for-sale.

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

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

Advertising costs – The Company expenses advertising costs as they are incurred. Total advertising expenses were approximately $178,000 and $99,000 in 2022 and 2021, respectively.

Fair value measurements – The Company recognizes the fair value of financial instruments in accordance with ASC 825-10, *Financial Instruments – Overall, Recognition and Measurement of Financial Assets and Financial Liabilities*, which requires use of the exit price notion when measuring the fair value of financial instruments for disclosure purposes. Fair value is defined as the exit price, the price that would be received for an asset or paid to transfer a liability, in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date under current market conditions. It also establishes a consistent framework for measuring fair value and expands disclosure requirements about fair value measurements. In determining fair value, the Company maximizes the use of observable inputs and minimizes the use of unobservable inputs.

Valuation inputs refer to the assumptions market participants would use in pricing a given asset or liability using one of the three valuation techniques within the fair value hierarchy. Inputs can be observable or unobservable. Observable inputs are those assumptions that market participants would use in pricing the particular asset or liability. These inputs are based on market data and are obtained from a source independent of the Company.

Unobservable inputs are assumptions based on the Company's own information or estimate of assumptions used by market participants in pricing the asset or liability. Unobservable inputs are based on the best and most current information available on the measurement date.

All inputs, whether observable or unobservable, are ranked in accordance with a prescribed fair value hierarchy that gives the highest ranking to quoted prices (unadjusted) in active markets for identical assets or liabilities (Level 1) and the lowest ranking to unobservable inputs (Level 3). Fair values for assets or liabilities classified as Level 2 are based on one or a combination of the following factors: (i) quoted prices for similar assets; (ii) observable inputs for the asset or liability, such as interest rates or yield curves; or (iii) inputs derived principally from or corroborated by observable market data.

There were no transfers between Level 1, Level 2, and Level 3 during 2022 or 2021.

Revenue recognition – The Company recognizes revenue in accordance with ASC 606, *Revenue from Contracts with Customers*, which (i) creates a single framework for recognizing revenue from contracts with customers that fall within its scope and (ii) revises when it is appropriate to recognize a gain (loss) from the transfer of nonfinancial assets, such as OREO. To determine revenue recognition for arrangements that an entity determines are within the scope of Topic 606, the Company performs the following five steps: (i) identify the contract(s) with a customer; (ii) identify the performance obligations in the contract; (iii) determine the transaction price; (iv) allocate the transaction price to the performance obligations in the contract; and (v) recognize revenue when (or as) the Company satisfies a performance obligation. The majority of the Company's revenues come from fee and interest income including loans and securities, which are outside the scope of ASC 606. The Company's services that fall within the scope of ASC 606 are presented within noninterest income and are recognized as revenue as the Company satisfies its obligation to the customer. Services within the scope of ASC 606 include deposit service charges.

All of the Company's revenue from contracts with customers in the scope of ASC 606 is recognized in noninterest income except for gains/losses on the sale of other real estate owned. Gains/losses on the sale of other real estate owned are included in noninterest expense and are generally recognized when the performance obligation is complete. This is typically at delivery of control over the property to the buyer at time of each real estate closing.

Service charges on deposit accounts – The Company earns fees from its deposit customers for account maintenance, transaction-based activity, and overdraft services. Account maintenance fees consist primarily of account fees and analyzed account fees charged on deposit accounts on a monthly basis. The performance obligation is satisfied and the fees are recognized on a monthly basis as the service period is completed. Transaction-based fees on deposit accounts are charged to deposit customers for specific services provided to the customer, such as non-sufficient funds fees, overdraft fees, and wire fees. The performance obligation is completed as the transaction occurs and the fees are recognized at the time each specific service is provided to the customer.

Subsequent events – Subsequent events are events or transactions that occur after the date of the consolidated statements of financial condition but before the consolidated financial statements are issued. Recognized subsequent events are events or transactions that provide additional evidence about conditions that existed at the date of the consolidated statements of financial condition, including the estimates inherent in the process of preparing the consolidated financial statements. Non-recognized subsequent events are events that provide evidence about conditions that did not exist at the date of the consolidated statements of financial condition but arose after that date. Management has reviewed events through March 30, 2023, the date the consolidated financial statements were issued.

Reclassifications – Certain reclassifications have been made to the 2021 comparable information to conform to the 2022 presentation. Such reclassifications do not alter the net income or equity balances as previously reported.

Note 2 – Investment Securities

The following is a summary of the investment securities as of December 31 (in thousands):

	Amortized Cost	Gross Unrealized Gain	Gross Unrealized Loss	Estimated Fair Value
2022				
Available-for-sale				
Municipal bonds	$ 34,076	$ 82	$ (1,410)	$ 32,748
Corporate bonds	12,015	-	(701)	11,314
SBA securities	4,533	-	(68)	4,465
	$ 50,624	$ 82	$ (2,179)	$ 48,527
2021				
Available-for-sale				
Municipal bonds	$ 34,460	$ 2,514	$ -	$ 36,974
Corporate bonds	11,996	255	(425)	11,826
SBA securities	6,327	-	(103)	6,224
	$ 52,783	$ 2,769	$ (528)	$ 55,024

The amortized cost and estimated fair value of securities as of December 31, 2022, by contractual maturity, are shown below. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties (in thousands):

	Available-for-Sale	
	Amortized Cost	Estimated Fair Value
Due in one year or less	$ 470	$ 470
Due from one to five years	7,726	7,533
Due from five to ten years	17,948	17,279
Due in more than ten years	24,480	23,245
	$ 50,624	$ 48,527

Securities with an amortized cost of $30,547,000 and $13,048,000 as of December 31, 2022 and 2021, respectively, were pledged to secure public deposits and for other purposes as required or permitted by law.

There was no sale of available-for-sale securities during 2022 or 2021.

Gross unrealized losses on investment securities available-for-sale and the estimated fair value of the related securities, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, were as follows as of December 31 (in thousands):

	Less Than 12 Months		12 Months or More		Total	
2022	Unrealized Losses	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses	Estimated Fair Value
Available-for-sale						
SBA securities	$ -	$ -	$ (68)	$ 4,465	$ (68)	$ 4,465
Corporate bonds	(266)	4,427	(435)	6,887	(701)	11,314
Municipal bonds	(1,410)	25,791	-	-	(1,410)	25,791
	$ (1,676)	$ 30,218	$ (503)	$ 11,352	$ (2,179)	$ 41,570
2021						
Available-for-sale						
SBA securities	$ -	$ -	$ (103)	$ 6,225	$ (103)	$ 6,225
Corporate bonds	(379)	6,214	(46)	673	(425)	6,887
	$ (379)	$ 6,214	$ (149)	$ 6,898	$ (528)	$ 13,112

At December 31, 2022 and 2021, there were 69 and 7 securities, respectively, in unrealized loss positions. Consideration is given to current market and interest rate conditions, and near-term prospects of the issuer, the length of time and the extent to which the fair value has been less than cost, and whether the Company intends to sell or will be required to sell. In analyzing an issuer's financial condition, the Company considers whether the securities are issued by the federal government or its agencies, whether downgrades by bond rating agencies have occurred, and the results of reviews of the issuer's financial condition. The Company considers the unrealized losses on its investments in an unrealized loss position at December 31, 2022 and 2021, to be not other-than-temporary.

Note 3 – Loans and Allowance for Loan Losses

The composition of the loan portfolio was as follows as of December 31 (in thousands):

	2022	2021
Construction and land	$ 1,071	$ 2,879
Multifamily	2,763	2,836
Commercial real estate	277,688	241,108
Residential real estate	96,455	13,190
Commercial and industrial	79,703	65,051
Consumer and other	33	55
	457,713	325,119
Allowance for loan losses	(4,580)	(4,575)
Net deferred loan costs	1,308	1,221
	$ 454,441	$ 321,765

Residential real estate loans are secured by non-consumer residential real estate.

Allowance for loan loss – Management believes that as of December 31, 2022 and 2021, the allowance for loan losses were adequate to absorb losses inherent in the loan portfolio. The allowance, however, is an estimate that is inherently uncertain and depends on the outcome of future events.

The following table presents the activity in the allowance for loan losses by segment for the years ended December 31 (in thousands):

	Beginning Balance	Provision for Loan Losses	Charge-offs	Recoveries	Transfers	Ending Balance
2022						
Construction and land	$ 30	$ (20)	$ -	$ -	$ -	$ 10
Multifamily	27	(4)	-	-	-	23
Commercial real estate	2,982	(198)	-	5	-	2,789
Residential real estate	25	111	-	-	-	136
Commercial and industrial	718	260	-	-	-	978
Consumer and other	-	-	-	-	-	-
Unallocated	793	(149)	-	-	-	644
	$ 4,575	$ -	$ -	$ 5	$ -	$ 4,580
2021						
Construction and land	$ 28	$ 2	$ -	$ -	$ -	$ 30
Multifamily	47	(20)	-	-	-	27
Commercial real estate	3,564	(582)	-	-	-	2,982
Residential real estate	-	25	-	-	-	25
Commercial and industrial	778	(82)	-	22	-	718
Consumer and other	47	(47)	-	-	-	-
Unallocated	104	704	-	-	(15)	793
	$ 4,568	$ -	$ -	$ 22	$ (15)	$ 4,575

A loan is considered impaired when the Company has determined that it may be unable to collect payments of principal or interest when due under the terms of the loan. In the process of identifying loans as impaired, management takes into consideration factors that include payment history and status, collateral value, financial condition of the borrower, and the probability of collecting scheduled payments in the future. Minor payment delays and insignificant payment shortfalls typically do not result in a loan being classified as impaired. The significance of payment delays and shortfalls is considered by management on a case-by-case basis, after taking into consideration the totality of circumstances surrounding the loans and the borrowers, including payment history and amounts of any payment shortfall, length and reason for delay, and likelihood of return to stable performance. Impairment is measured on a loan-by-loan basis for all loans in the portfolio except for the smaller groups of homogeneous consumer loans in the portfolio.

The following table presents loans individually evaluated for impairment by class of loans as of December 31 (in thousands):

	Recorded Investments (Loan Balance Less Charge-off)	Unpaid Principal Balance	Related Allowance	Average Investment in Impaired Loans	Interest Income Recognized
2022					
With no allowance recorded					
Commercial real estate	$ 288	$ 288	$ -	$ 291	$ -
2021					
With no allowance recorded					
Commercial real estate	$ 295	$ 295	$ -	$ 332	$ -

The following table presents the balance in the allowance for loan losses and the recorded investment in loans by portfolio segment and based on impairment method as of December 31 (in thousands):

	Allowance for Loan Losses			Loans Receivable		
	Ending Balance	Ending Balance Individually Evaluated for Impairment	Ending Balance Collectively Evaluated for Impairment	Ending Balance	Ending Balance Individually Evaluated for Impairment	Ending Balance Collectively Evaluated for Impairment
2022						
Construction and land	$ 10	$ -	$ 10	$ 1,071	$ -	$ 1,071
Multifamily	23	-	23	2,763	-	2,763
Commercial real estate	2,789	-	2,789	277,688	288	277,400
Residential real estate	136		136	96,455	-	96,455
Commercial and industrial	978	-	978	79,703	-	79,703
Consumer and other	-	-	-	33	-	33
Unallocated	644	-	644	-	-	-
	$ 4,580	$ -	$ 4,580	$ 457,713	$ 288	$ 457,425

	Allowance for Loan Losses			Loans Receivable		
	Ending Balance	Ending Balance Individually Evaluated for Impairment	Ending Balance Collectively Evaluated for Impairment	Ending Balance	Ending Balance Individually Evaluated for Impairment	Ending Balance Collectively Evaluated for Impairment
2021						
Construction and land	$ 30	$ -	$ 30	$ 2,879	$ -	$ 2,879
Multifamily	27	-	27	2,836	-	2,836
Commercial real estate	2,982	-	2,982	241,108	295	240,813
Residential real estate	25	-	25	13,190	-	13,190
Commercial and industrial	718	-	718	65,051	-	65,051
Consumer and other	-	-	-	55	-	55
Unallocated	793	-	793	-	-	-
	$ 4,575	$ -	$ 4,575	$ 325,119	$ 295	$ 324,824

The following table presents the recorded investment in nonaccrual loans by type as of December 31 (in thousands):

	2022	2021
Commercial real estate	$ 288	$ 295

Past due loans – Loans are considered past due if the required principal and interest payments have not been received as of the date such payments were due.

The following table presents past due loans, net of partial loan charge-offs, by type as of December 31 (in thousands):

	30 - 59 Days Past Due	60 - 89 Days Past Due	90 Days or More Past Due	Total Past Due	Current	Total Loans
2022						
Construction and land	$ -	$ -	$ -	$ -	$ 1,071	$ 1,071
Multifamily	-	-	-	-	2,763	2,763
Commercial real estate	-	-	288	288	277,400	277,688
Residential real estate	-	-	-	-	96,455	96,455
Commercial and industrial	-	-	-	-	79,703	79,703
Consumer and other	-	-	-	-	33	33
	$ -	$ -	$ 288	$ 288	$ 457,425	$ 457,713
2021						
Construction and land	$ -	$ -	$ -	$ -	$ 2,879	$ 2,879
Multifamily	-	-	-	-	2,836	2,836
Commercial real estate	-	-	-	-	241,108	241,108
Residential real estate	-	-	-	-	13,190	13,190
Commercial and industrial	-	-	-	-	65,051	65,051
Consumer and other	-	-	-	-	55	55
	$ -	$ -	$ -	$ -	$ 325,119	$ 325,119

Credit quality indicator – Federal regulations provide for the classification of lower quality loans and other assets, such as debt and equity securities, as substandard, doubtful, or loss. An asset is considered substandard if it is inadequately protected by the current net worth and pay capacity of the borrower or of any collateral pledged. Substandard assets include those characterized by the distinct possibility that the Company will sustain some loss if the deficiencies are not corrected. Assets classified as doubtful have all the weaknesses inherent in those classified substandard, with the added characteristic that the weaknesses present make collection or liquidation in full highly questionable and improbable on the basis of currently existing facts, conditions, and values. Assets classified as loss are those considered uncollectible and of such little value that their continuance as assets without the establishment of a specific loss reserve is not warranted.

When the Company classifies problem assets as either substandard or doubtful, it may determine the loan is impaired and establish a specific allowance to address the risk specifically, or the Company may allow the loss to be addressed in the general allowance. General allowances represent loss allowances that have been established to recognize the inherent risk associated with lending activities, but that, unlike specific allowances, have not been specifically allocated to particular problem assets. When an insured institution classifies problem assets as a loss, it is required to charge off such assets in the period in which they are deemed uncollectible. At December 31, 2022 and 2021, the Company had no loans classified as doubtful or loss. Assets that do not currently expose the Company to sufficient risk to warrant classification as substandard or doubtful but possess identified weaknesses are designated as either watch or special mention assets. Assets not otherwise classified or criticized are graded pass.

Additionally, the Company categorizes loans as performing or nonperforming based on payment activity. Loans that are more than 90 days past due and nonaccrual loans are considered nonperforming.

The following tables represent the internally assigned grade as of December 31 by type of loan (in thousands):

Credit Risk Profile by Internally Assigned Grade

2022	Construction and Land	Multifamily	Commercial Real Estate	Residential Real Estate	Commercial and Industrial	Consumer and Other
Grade						
Pass	$ 1,071	$ 2,763	$ 276,014	$ 96,455	$ 76,728	$ 33
Watch	-	-	143	-	2,967	-
Special mention	-	-	1,243	-	8	-
Substandard	-	-	288	-	-	-
	$ 1,071	$ 2,763	$ 277,688	$ 96,455	$ 79,703	$ 33

Credit Risk Profile Based on Payment Activity

	Construction and Land	Multifamily	Commercial Real Estate	Residential Real Estate	Commercial and Industrial	Consumer and Other
Performing	$ 1,071	$ 2,763	$ 277,400	$ 96,455	$ 79,703	$ 33
Nonperforming	-	-	288	-	-	-
	$ 1,071	$ 2,763	$ 277,688	$ 96,455	$ 79,703	$ 33

Credit Risk Profile by Internally Assigned Grade

2021	Construction and Land	Multifamily	Commercial Real Estate	Residential Real Estate	Commercial and Industrial	Consumer and Other
Grade						
Pass	$ 2,879	$ 2,836	$ 221,611	$ 13,190	$ 64,991	$ 55
Watch	-	-	15,640	-	60	-
Special mention	-	-	3,562	-	-	-
Substandard	-	-	295	-	-	-
	$ 2,879	$ 2,836	$ 241,108	$ 13,190	$ 65,051	$ 55

Credit Risk Profile Based on Payment Activity

	Construction and Land	Multifamily	Commercial Real Estate	Residential Real Estate	Commercial and Industrial	Consumer and Other
Performing	$ 2,879	$ 2,836	$ 240,813	$ 13,190	$ 65,051	$ 55
Nonperforming	-	-	295	-	-	-
	$ 2,879	$ 2,836	$ 241,108	$ 13,190	$ 65,051	$ 55

Loans classified as troubled debt restructurings totaled $288,000 and $295,000 at December 31, 2022 and 2021, respectively. A troubled debt restructuring is a loan to a borrower that is experiencing financial difficulty that has been modified from its original terms and conditions in such a way that the Company is granting the borrower a concession of some kind. The Company has granted a variety of concessions to borrowers in the form of loan modifications. The modifications granted can generally be described in the following categories:

Rate modification – A modification in which the interest rate is changed.

Term modification – A modification in which the maturity date, timing of payments, or frequency of payments is changed.

Payment modification – A modification in which the dollar amount of the payment is changed. Interest-only modifications in which a loan is converted to interest-only payments for a period of time are included in this category.

Combination modification – Any other type of modification, including the use of multiple categories above.

Upon identifying those receivables as troubled debt restructurings, the Company identified them as impaired for purposes of determining the allowance for loan losses. This requires the loans to be evaluated individually for impairment, generally based on the expected cash flows under the new terms discounted at the loans' original effective interest rates. For troubled debt restructured loans that subsequently default, the method of determining impairment is generally the fair value of the collateral less estimated selling costs.

There were no loans modified as trouble debt restructurings during 2022 or 2021. There were no commitments to lend to borrowers whose loans had been modified under troubled debt restructuring as of December 31, 2022 and 2021.

At December 31, 2022 and 2021, loans (including amounts committed) of $0 and $2,073,000, respectively, represent real estate secured loans that have loan-to-value ratios above supervisory guidelines.

There were no related party loans to officers and directors at December 31, 2022 and 2021.

Note 4 – Premises and Equipment

Premises and equipment as of the following years ended December 31 are summarized as follows (in thousands):

	2022	2021
Land	$ 1,432	$ 1,432
Building	4,284	4,284
Leasehold improvements	925	925
Furniture, fixtures, and equipment	1,452	1,441
Vehicles	90	90
Construction in process	366	-
	8,549	8,172
Less accumulated depreciation and amortization	(2,973)	(2,706)
	$ 5,576	$ 5,466

Total depreciation and amortization expense of premises and equipment for the years ended December 31, 2022 and 2021, amounted to $267,000 and $257,000, respectively.

Note 5 – Leases

The Company has operating leases for its satellite branches. The maturities of these leases stagger through 2027. The Company's leases generally include extension clauses for five years at a time.

The components of lease cost (included in occupancy and equipment expense on the Consolidated Statements of Income) are as follows for the years ended December 31 (in thousands):

	2022	2021
Lease cost		
Minimum rent payments	$ 329	$ 321
Other operating costs	66	51
	$ 395	$ 372

The following table provides supplemental information related to operating leases for the purpose of the measurement of lease liabilities at or for the years ended December 31 (dollars in thousands):

	2022	2021
Operating cash flows from operating leases	$ 329	$ 321
Weighted average remaining lease term	4.15 years	5.13 years
Weighted average discount rate	1.6%	1.6%

The Company's leases typically do not contain a discount rate implicit in the lease contract. As an alternative, the Company uses the incremental borrowing rate commensurate with the lease term.

The following table presents minimum lease payments under the terms of the leases at December 31, 2022 (in thousands):

2023	$ 329
2024	338
2025	347
2026	357
2027	98
Total lease payments	1,469
Less imputed interest	(63)
Total	$ 1,406

Note 6 – Servicing Asset

The sold portions of SBA and USDA loans are not included in the accompanying consolidated statements of financial condition. The sold portions of SBA and USDA loans at December 31, 2022 and 2021, were $141,441,000 and $114,691,000, respectively. The fair value of servicing rights held as of December 31, 2022 and 2021, were $2,475,000 and $2,767,000, respectively.

Changes in the balance of the servicing asset, net of the valuation allowance, were as follows for the years ended December 31 (in thousands):

	2022	2021
Balance, beginning of year	$ 2,400	$ 1,986
Additions	846	1,151
Amortization	(861)	(737)
Balance, end of year	$ 2,385	$ 2,400

At December 31, 2022, the expected weighted-average life of the Company's servicing asset was 4.5 years. Projected annual amortization expense after the year ended December 31, 2022, is estimated to be as follows (in thousands):

2023	$ 467
2024	466
2025	451
2026	378
2027	237
Thereafter	386
Gross carrying value of servicing asset	2,385
Less valuation allowance	-
Net carrying value of servicing asset	$ 2,385

The following represents servicing fees earned in connection with the servicing asset, indicated net of the servicing asset amortization. These amounts are included in the accompanying consolidated financial statements as components of noninterest income for the years ended December 31 (in thousands):

	2022	2021
Servicing fees	$ 478	$ 614

Late fees associated with the servicing asset are immaterial for the years ended December 31, 2022 and 2021.

The projected amortized expense of the servicing asset is an estimate. The amortization expense for future periods was calculated by applying the same quantitative factors, such as servicing asset prepayment assumptions that were used to determine amortization expense for 2021. These factors are inherently subject to significant fluctuations, primarily due to the effect that changes in interest rates have on loan prepayment experience. Accordingly, any projection of servicing asset amortization in future periods is limited by the conditions that existed at the time the calculations were performed and may not be indicative of actual amortization expense that will be recorded in future periods. The constant prepayment rate as of December 31, 2022 and 2021, is 16.3% and 16.7%, respectively. The discount rate as of December 31, 2022 and 2021, is 18.1% and 11.3%, respectively.

Note 7 – Deposits

The scheduled maturities of time deposits as of December 31, 2022, are as follows (in thousands):

2023	$ 136,339
2024	5,719
2025	844
2026	346
2027	201
	$ 143,449

Brokered deposits of $1,000 and $25,001,000 were included in money market accounts as of December 31, 2022 and 2021, respectively. Brokered deposits of $37,784,000 and $10,000,000 were included in time deposit accounts as of December 31, 2022 and 2021, respectively. The Company held related party deposits of $228,000 and $550,000 as of December 31, 2022 and 2021, respectively. At December 31, 2022 and 2021, time deposits equal to or greater than $250,000 totaled $77,074,000 and $36,573,000, respectively.

Note 8 – Commitments and Contingencies

Litigation – In the normal course of business, U & I Financial Corp. and UniBank are involved in various legal claims. Management has reviewed all legal claims with counsel and has taken into consideration the views of such counsel regarding the outcome of the claims. In management's opinion, the final disposition of all such claims will not have a material adverse effect on the financial condition, results of operations, or cash flows of the Company.

Financial instruments with off-balance-sheet risk – The accompanying consolidated financial statements do not reflect various other commitments and contingent liabilities. These commitments and contingent liabilities include various commitments to extend credit and standby letters of credit, which arise in the normal course of business. Commitments to extend credit are legally binding loan commitments with set expiration dates. Standby letters of credit are conditional commitments issued by the Company to guarantee the performance of a customer to a third party. They are intended to be disbursed, subject to certain conditions, upon request of the borrower.

The Company evaluates the creditworthiness of each customer. The amount of collateral obtained, if deemed necessary by the Company upon the extension of credit, is based on management's evaluation of the borrower. Collateral for commercial loans may vary but may include securities; accounts receivable; inventory; property, plant, and equipment; and income-producing commercial or other properties.

The following is a summary of the Company's financial instruments relating to extension of credit with off-balance-sheet risk as of December 31 (in thousands):

	2022	2021
Commitments to extend credit	$ 855	$ 2,523

Note 9 – Borrowing Arrangements

The Company periodically uses FHLB advances as a funding source to provide operating liquidity and to fund loan origination. At December 31, 2022, the Company had total borrowings outstanding of $22,000,000, including $12,000,000 of overnight advances at rate of 4.60% and $10,000,000 of 3-week fixed advance at a rate of 4.02%. At December 31, 2021, the Company had $10,000,000 of overnight advances outstanding at a rate of 0.30%.

As of December 31, 2022 and 2021, under the FHLB borrowing agreement, the borrowing capacity was limited to the lower 45% of total assets or available collateral balance. The Company has pledged loans as collateral with an approximate total carrying value of $162,830,000 and $119,559,000 as of December 31, 2022 and 2021, respectively. The unused and available line of credit at December 31, 2022 and 2021, were $100,123,000 and $73,413,000, respectively.

The Company also uses borrowings from the Federal Reserve Bank of San Francisco through the discount window. As of December 31, 2022 and 2021, the Company had no overnight borrowings outstanding. These borrowing lines are collateralized by pledged loans and securities with an approximate carrying value of $82,338,000 and $22,721,000 as of December 31, 2022 and 2021, respectively.

In addition, the Company had three unsecured lines of credit to borrow up to a total of $26,500,000 for overnight purchase of federal funds as of December 31, 2022 and 2021, at the then current rates. As of December 31, 2022 and 2021, there were no outstanding balances on these lines.

Note 10 – Income Taxes

The provision for income taxes consists of the following for the years ended December 31 (in thousands):

	2022	2021
Current income tax provision	$ 2,693	$ 2,473
Deferred income tax provision (benefit)	11	(479)
	$ 2,704	$ 1,994

Reconciliation of the provision for income tax expense based on the statutory income tax rate to actual income tax expense is provided as follows (in thousands):

	2022		2021	
	Amount	Percent	Amount	Percent
Federal income tax at statutory rate	$ 2,905	21%	$ 2,204	21%
Interest income on tax-exempt bonds	(210)	-2%	(211)	-2%
Income from bank owned life insurance	(67)	0%	(66)	-1%
Equity compensation	29	0%	47	0%
State tax	34	0%	-	0%
Other	13	0%	20	0%
	$ 2,704	19%	$ 1,994	19%

The cumulative temporary differences, as tax effected, are as follows as of December 31 (in thousands):

	2022	2021
Deferred tax assets		
Allowance for loan losses	$ 973	$ 961
Organizational costs	1	2
Unrealized loss on securities available-for-sale	446	-
Stock based compensation	61	52
Lease liability	299	362
Other	61	30
Total deferred tax assets	1,841	1,407
Deferred tax liabilities		
Unrealized gain on securities available-for-sale	-	(471)
Deferred loan costs	(174)	(27)
Servicing asset	(95)	(35)
Fixed asset basis	(33)	(124)
Stock based compensation	-	(12)
Right-of-use assets	(299)	(362)
Other	(42)	(89)
Total deferred tax liabilities	(643)	(1,120)
Net deferred tax assets	$ 1,198	$ 287

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management considers the scheduled reversal of deferred tax liabilities, the projected future taxable income, and tax-planning strategies in making this assessment. A valuation allowance against deferred tax assets at the consolidated statement of financial condition date is not considered necessary because it is more likely than not that the deferred tax asset will be fully realized.

The Company applies a more-likely-than-not recognition criterion. The Company had no material unrecognized tax benefits at December 31, 2022 and 2021. The Company recognizes interest accrued and penalties related to unrecognized tax benefits in tax expense. During the years ended December 31, 2022 and 2021, the Company recognized no material interest and penalties. The Company files income tax returns in the U.S. federal and various state jurisdictions and is no longer subject to examination for years before 2018.

Note 11 – Stock-Based Compensation

During 2006, the Company's Board of Directors granted the 2006 incentive and nonqualified share-based compensation plan that provided for the issuance of options to purchase its authorized but unissued common stock to eligible employees and directors. The exercise price of each option equals the fair market value of the Company's stock on the date of grant, and options are scheduled to vest over periods ranging from three to five years. The 2006 incentive and nonqualified share-based compensation plan expired in November 2016 and all stock compensation expense was fully recognized. In 2018, the Company's shareholders approved an equity incentive plan (the Plan). The Plan permits the grant of incentive stock options, nonqualified stock options, and restricted stock awards. The maximum amount of common stock that may be issued under the Plan is 824,256, of which there are 82,426 shares allowable for restricted stock grants. As of December 31, 2022, 172,089 shares remained available to grant out of the Plan, of which 4,092 remained available for restricted stock. The Plan will expire in 2028.

Stock options – Incentive stock and nonqualified stock options are awarded with an exercise price generally equal to the fair market value of the Company's stock as of the grant date, and vest ratably over their respective vesting periods, provided continuous service by the awardees. The exercise period commences on the vesting date and expires 10 years from the grant date. Certain option awards provide for accelerated vesting upon a "change in control" as defined by the Plan.

The fair value of each option award is estimated on the date of grant using the Black-Scholes-Merton valuation model that uses the assumptions noted in the following table. Expected volatilities are based on historical volatility of the Bank's stock and other factors. The expected term of options granted was evaluated by a calculation that factored in the contractual term and vesting period and considered different employee segments. The risk-free interest rate for periods within the contractual life of the option is based on the U.S. Treasury yield curve in effect at the time of grant.

	2022	2021
Assumptions		
Risk-free interest rate	1.26%-1.73%	0.58-0.70%
Dividend yield	2%	0-2%
Expected volatility	30%-35%	30%
Expected option life in years	5.0-7.5	6.5-7.5

The following is a summary of the incentive and nonqualified stock option activity for the year ended December 31, 2022:

	Number of Options Outstanding	Weighted-Average Exercise Price	Weighted-Average Remaining Term
Outstanding, beginning of year	635,943	$ 6.57	8.12
Options granted	39,500	10.74	-
Options exercised	(107,039)	6.15	-
Options forfeited/cancelled	(63,167)	6.80	-
Outstanding, end of year	505,237	$ 6.95	7.51
Options expected to vest assuming 0% forfeiture rate	325,839	$ 7.19	7.74
Options exercisable at year-end	179,398	$ 6.52	7.10

The weighted-average grant-date fair value of all options granted during 2022 was $3.04. As of December 31, 2022, there was $559,000 in unrecognized compensation cost related to incentive and nonqualified stock options granted under the Plan. The cost is expected to be recognized over the remaining weighted-average period of 2.28 years.

Restricted stock – The fair value of restricted stock awards granted is equal to the fair market value of the Company's stock at the date of grant. Restricted stock awards vest ratably over three years from the date of grant.

The following is a summary of the nonvested restricted stock award activity for the year ended December 31, 2022:

	Number of Shares Outstanding	Weighted-Average Grant Date Fair Value	Weighted-Average Remaining Term
Outstanding, beginning of year	5,000	$ 6.59	1.50
Restricted stock vested	(2,500)	6.89	-
Outstanding, end of year	2,500	$ 6.59	0.50
Restricted stock expected to vest assuming 0% forfeiture rate	2,500	$ 6.59	0.50

As of December 31, 2022, there was $8,000 in unrecognized compensation cost related to restricted stock awards. The cost is expected to be recognized over the remaining weighted average vesting period of 0.5 years.

The Company's pre-tax compensation expense for share-based employee compensation was $281,000 and $459,000 for the years ended December 31, 2022 and 2021, respectively.

Note 12 – Employee Benefit Plan

On January 1, 2008, the Company established a 401(k) profit sharing plan (the 401(k) Plan), which is available to all eligible employees who have completed three months of service. Each employee is allowed to contribute to the 401(k) Plan up to the maximum percentage allowable, but not to exceed the limits of the Internal Revenue Service. As of January 1, 2018, the 401(k) Plan requires the Company to match 75% up to 8% of employee deferrals. Total employer contribution expense amounted to approximately $205,000 and $356,000 for 2022 and 2021, respectively.

Note 13 – Fair Value

The Company used the following methods and assumptions in estimating fair value disclosure for financial instruments. Financial assets and liabilities recorded at fair value on a recurring and nonrecurring basis are as listed below:

Securities available-for-sale – Available-for-sale securities are valued using prices from an independent pricing service using Level 2 inputs. The fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, live trading levels, trade execution data, market consensus prepayment speeds, credit information, and the bond's terms and conditions, among other things.

Impaired loans – A loan is considered to be impaired when it is probable that all of the principal and interest due under the original underwriting terms of the loan may not be collected. Fair value of collateral-dependent loans is measured based on the fair value of the underlying collateral. The fair value is determined through appraisals, which requires a significant degree of management judgment.

As of December 31, assets measured at fair value on a recurring basis (there were no liabilities measured at fair value on a recurring basis) are as follows (in thousands):

	Level 1 Quoted Prices in Active Markets	Level 2 Significant Other Observable Inputs	Level 3 Significant Unobservable Inputs	Total Fair Value
2022				
Assets				
Securities available for sale				
Municipal bonds	$ -	$ 32,748	$ -	$ 32,748
Corporate bonds	-	11,314	-	11,314
SBA securities	-	4,465	-	4,465
Total	$ -	$ 48,527	$ -	$ 48,527
2021				
Assets				
Securities available for sale				
Municipal bonds	$ -	$ 36,974	$ -	$ 36,974
Corporate bonds	-	11,826	-	11,826
SBA securities	-	6,224	-	6,224
Total	$ -	$ 55,024	$ -	$ 55,024

As of December 31, assets measured at fair value on a nonrecurring basis (there were no liabilities measured at fair value on a nonrecurring basis) are as follows (in thousands):

	Level 1 Quoted Prices in Active Markets	Level 2 Significant Other Observable Inputs	Level 3 Significant Unobservable Inputs	Total Fair Value
2022				
Assets				
Impaired loans	$ -	$ -	$ 288	$ 288
2021				
Assets				
Impaired loans	$ -	$ -	$ 295	$ 295

Quantitative information about Level 3 fair value measurements – The range and weighted average of the significant unobservable inputs used to fair value Level 3 nonrecurring assets as of December 31, 2022 and 2021, along with the valuation techniques used, are shown in the following table (in thousands):

	Fair Value at December 31, 2022	Valuation Technique	Unobservable Input	Range (Weighted Average) [1]
Impaired loans	$ 288	Market comparable	Adjustment to appraisal value	8%

[1] Discount to appraisal value

	Fair Value at December 31, 2021	Valuation Technique	Unobservable Input	Range (Weighted Average) [1]
Impaired loans	$ 295	Market comparable	Adjustment to appraisal value	8%

[1] Discount to appraisal value

Carrying amounts and estimated fair values of financial instruments, not previously presented, as of December 31 are as follows (in thousands):

	Carrying	Estimated	Fair Value Level		
December 31, 2022	Amount	Fair Value	Level 1	Level 2	Level 3
Financial assets					
Cash and due from banks	$ 42,003	$ 42,003	$ 42,003	$ -	$ -
Securities available for sale	48,527	48,527	-	48,527	-
Loans receivable, net	454,441	442,560	-	-	442,560
Servicing asset	2,385	2,475	-	-	2,475
Federal Home Loan Bank and					
Federal Reserve Bank stock, at cost	2,432	2,432	2,432	-	-
Accrued interest receivable	1,755	1,755	1,755	-	-
Financial liabilities					
Savings, money market, and NOW	227,314	227,314	227,314	-	-
Time deposits	143,449	141,943	-	141,943	-
Accrued interest payable	316	316	316	-	-
Borrowings	22,000	22,000	-	22,000	-
December 31, 2021					
Financial assets					
Cash and due from banks	$ 31,096	$ 31,096	$ 31,096	$ -	$ -
Securities available for sale	55,024	55,024	-	55,024	-
Loans receivable, net	321,765	322,476	-	-	322,476
Servicing asset	2,400	2,767	-	-	2,767
Federal Home Loan Bank stock				-	-
Federal Reserve Bank stock, at cost	1,800	1,800	1,800		
Accrued interest receivable	1,123	1,123	1,123	-	-
Financial liabilities					
Savings, money market, and NOW	198,960	198,960	198,960	-	-
Time deposits	76,933	77,001	-	77,001	-
Accrued interest payable	24	24	24	-	-
Borrowings	10,000	10,000	-	10,000	-

Note 14 – Regulatory Matters

U & I Financial Corp. and UniBank are subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by the regulators that, if undertaken, could have a direct material effect on the financial statements. Under capital adequacy guidelines and regulatory framework for prompt corrective actions, U & I Financial Corp. and UniBank must meet specific capital guidelines that involve quantitative measures of assets, liabilities, and certain off-balance-sheet items as calculated under regulatory accounting practices. U & I Financial Corp. and UniBank's capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors. Management believes that as of December 31, 2022 and 2021, U & I Financial Corp. and UniBank met all of the capital adequacy requirements to which they are subject.

U & I Financial Corp. and UniBank are periodically examined by the Federal Reserve Bank and the Department of Financial Institutions of the State of Washington. As of December 31, 2022, U & I Financial Corp. and UniBank are categorized as well capitalized under the regulatory framework. To be categorized as well capitalized, the Bank must maintain minimum amounts and ratios (set forth in the following table) of total and Tier I capital (as defined in the regulations) to risk-weighted assets (as defined), of Tier I capital (as defined) to average assets (as defined), and common equity Tier 1 capital. There are no conditions or events that have occurred since that notification that management believes would result in a change to the institution's category. The Company's consolidated assets are less than $3 billion at the beginning of the year, therefore consolidated ratios are not required to be disclosed.

The Bank's actual capital amounts and ratios are presented in the table below as of December 31 (in thousands):

	Actual		For Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2022						
Total capital (to risk-weighted assets)	$ 77,921	16.91%	$ 36,864	≥ 8.00%	$ 46,080	≥ 10.00%
Tier I capital (to risk-weighted assets)	$ 73,341	15.91%	$ 27,658	≥ 6.00%	$ 36,878	≥ 8.00%
Common equity Tier 1 capital	$ 73,341	15.91%	$ 20,744	≥ 4.50%	$ 29,963	≥ 6.50%
Tier I capital (to average assets)	$ 73,341	12.83%	$ 22,865	≥ 4.00%	$ 28,582	≥ 5.00%
As of December 31, 2021						
Total capital (to risk-weighted assets)	$ 68,434	20.60%	$ 26,576	≥ 8.00%	$ 33,220	≥ 10.00%
Tier I capital (to risk-weighted assets)	$ 64,277	19.35%	$ 19,931	≥ 6.00%	$ 26,575	≥ 8.00%
Common equity Tier 1 capital	$ 64,277	19.35%	$ 14,948	≥ 4.50%	$ 21,592	≥ 6.50%
Tier I capital (to average assets)	$ 64,277	15.24%	$ 16,871	≥ 4.00%	$ 21,088	≥ 5.00%

The Federal Reserve and the FDIC approved final capital rules in July 2013 that substantially amended the existing capital rules for banks. These rules reflect, in part, certain standards initially adopted by the Basel Committee on Banking Supervision in December 2010 (which standards are commonly referred to as "Basel III") as well as requirements contemplated by the Dodd-Frank Act.

Under the amended capital rules, there is a capital ratio of common equity Tier I capital to risk-weighted assets ratio. Common equity Tier I capital generally consists of retained earnings and common stock (subject to certain adjustments). In March 2015, the Company exercised a one-time irrevocable option to exclude investment components of accumulated other comprehensive income. The Company is also required to establish a “conservation buffer,” consisting of a common equity Tier I capital amount equal to 2.5% of risk weighted assets. An institution that does not meet the conservation buffer will be subject to restrictions on certain activities including payment of dividends, stock repurchases, and discretionary bonuses to executive officers.

Note 15 – Earnings Per Share

The following table presents a reconciliation of the components used to compute basic and diluted earnings per share (dollars in thousands, except per-share amounts) at December 31:

	2022	2021
Net income	$ 11,129	$ 8,502
Basic weighted-average common shares outstanding	5,494,698	5,556,544
Plus common stock options considered outstanding for dilutive purposes (excludes antidilutive options)	154,210	143,438
Diluted weighted-average common shares outstanding	5,648,908	5,699,982
Basic earnings per share of common stock	$ 2.03	$ 1.53
Diluted earnings per share of common stock	$ 1.97	$ 1.49

Antidilutive options for 2022 and 2021 were 0 for both years.

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